

# Standard Practice Guide Policies

## University Investments and Endowment Funds

501.11

**Applies to:** All departments and units of the university

### I. POLICY

The University of Michigan's investment policies are governed and authorized by University Bylaws and the Board of Regents. The university is subject to the Uniform Prudent Management of Institutional Funds Act (UPMIFA) enacted by the State of Michigan in 2009.

The university maintains centralized management for substantially all of its cash and investments. Individual units of the university are not allowed to invest funds directly.

### II. TYPES OF FUNDS

The university has four basic types of funds to invest: operating funds, endowment, life income agreements and insurance and benefits reserves.

#### A. OPERATING FUNDS

Operating funds are composed of operational working capital and unexpended bond proceeds. Both operational working capital and unexpended bond proceeds are invested in accordance with an adopted Investment Policy Statement.

Operational working capital funds are deposited by units and departments and are made available to depositors for operating expenses or capital projects. Operational working capital balances are automatically accumulated by each fund and department for investment in the University Investment Pool (UIP).

The UIP provides depositors daily access to their funds without risk of loss, with a corresponding rate of return. Pursuant to the UIP distribution policy approved by the Board of Regents, the rate of return is based on the 90-day U.S. Treasury Bill rate with such rate not to exceed 2.50% in any event. Depositors receive distributions calculated on the basis of their month-end UIP balances, whether positive or negative. Depositors are defined as university school, college, or unit cash balances in total by Fund-Department combination.

UIP distributions are credited (or debited if negative balance) to each Fund-Department combination automatically monthly, at month-end. A request can be made to have distributions applied to a predetermined chartfield. UIP distributions to more detailed chartfield combinations (i.e. project/grant) are the responsibility of individual units. Monthly UIP distributions are generally not distributed to sponsored programs, agency or endowment funds.

Additional information about the UIP, including current and historical distribution rates, is available

on the Financial Operations website. Financial Operations is responsible for the administration of the UIP.

## B. ENDOWMENT

Endowment funds are invested for the long-term, with a prudent portion of investment returns distributed to support university programs and operations.

There are two types of endowments: true endowment and quasi-endowment.

True endowment funds are those funds received from donors with the stipulation that the principal remain intact and be invested in perpetuity to produce income that is to be expended for the purposes specified by the donor. The minimum amount of external funding needed to establish a true endowment fund is \$25,000. True endowment funds include contributions from bequests, trust distributions or outright gifts to the university from external donors and endowment distributions if specified by the donor. The Office of the Vice President and General Counsel reviews all True Endowment gift agreements. University funds may not be used to create, or add to, a true endowment.

Quasi-endowment consist of amounts (restricted gifts or unrestricted funds) that have been allocated by university units for long-term investment purposes, but are not limited by donor stipulations requiring the university to preserve principal in perpetuity. The source of these funds may be from donors, including contributions from bequests, trust distributions or outright gifts to the university that were not designated as a true endowment, or surplus departmental operating capital.

Quasi-endowment funds have the same long-term investment strategy as true endowments. The primary differences are that quasi-endowments may be established using internal department funds and the principal balance may be withdrawn and expended, based upon university policy, generally after a minimum five-year investment period or lock-up. The same lock-up period applies to quarterly distributions that are re-invested into the quasi-endowment. The minimum amount needed to establish a quasi-endowment fund is \$50,000 of university internal funds or \$25,000 of donor-directed external funds.

Before a quasi-endowment may be established, sufficient (positive) working capital must be available in UIP at the Fund-Department Group level for unrestricted funds and at the full chartfield level for restricted funds. Working capital from the General Fund cannot be considered when determining surplus departmental operating capital. In determining surplus departmental operating capital, cash flow needs throughout the minimum five-year investment period must be considered.

If sufficient working capital is not available, the university may require liquidation of quasi-endowments.

The University Controller is the approving authority for the establishment of all new endowments.

### 1. UNIVERSITY ENDOWMENT FUND

The majority of true endowment and quasi-endowment funds are invested in the University Endowment Fund (UEF), a unitized pool invested in the university's Long Term Portfolio.

#### a. CONTRIBUTIONS

Contributions to the UEF buy shares at the share value as of the end of each quarter (September, December, March and June). Share values are determined quarterly based on the market value of the overall pool. The market value of an endowment can be determined by multiplying the number of shares an endowment owns by the current

quarter's share value. Market value and owners' shares are available via query in M-Pathways.

New contributions consist of all cash additions to the UEF pool during a quarter. New contributions received buy additional shares of participation in the UEF at quarter end, based on the quarter ending share value.

The share value is recalculated quarterly based on the market value of the pool. This is accomplished by taking the pool's current market value, subtracting any new contributions, and then dividing by the number of pre-existing shares in the pool. Once the share value has been determined, the new contribution is divided by the share value to determine how many new shares will be purchased and added to the pool.

Distributions on shares associated with a new contribution will begin at the end of the next quarter, after the contribution has purchased shares in the UEF, in accordance with the table below::

<b>New Contribution Received</b>	<b>Shares Purchased</b>	<b>Share Value Used</b>	<b>First Distributor</b>
January – March	March 31	March 31	June 30
April – June	June 30	June 30	September 30
July – September	September 30	September 30	December 31
October – December	December 31	December 31	March 31

**b. DISTRIBUTIONS**

The UEF distribution policy, set by the Board of Regents, insulates the university's budget from market volatility and provides for a quarterly distribution per share. The annual distribution rate is 4.5 percent of the one-quarter lagged seven year moving average fair value of UEF shares.

To protect endowment principal in the event of a prolonged market downturn, distributions are limited to 5.3 percent of the current market value of UEF shares. The limit on endowment distributions will be applied using the current one-quarter lagged market value of UEF shares.

**c. WITHDRAWALS**

True Endowment Funds cannot be withdrawn. Withdrawals may be made from Quasi-Endowment Funds based upon university policy, generally after a five-year investment period, by submitting a Quasi-Endowment Withdrawal Form, which is available on the Financial Operations website. Withdrawals must satisfy any restrictions that may have been placed on the fund's use by either the donor or the department. Generally, the amount available for withdrawal is calculated as follows::

- (1) Determine the number of shares owned by an individual fund
- (2) Subtract the number of shares purchased during the past five years
- (3) The resulting shares are shares which have been on deposit for the required five years

(4) The value of these shares is based on the quarter ending share value at the time of the withdrawal

Withdrawals are completed at the beginning of each quarter (April 1, July 1, October 1 and January 1) and processed at the preceding quarter's share value at the time of the withdrawal (March 31, June 30, September 30 and December 31). Requests for quasi-endowment withdrawals beyond their initial five year-lock period are subject to the following tiered structure for minimum advance notification.

<b>Withdrawal Amount</b>	<b>Minimum Advance Notice (Prior to Quarter End)*</b>	<b>Percent Request Can be Adjusted**</b>
up to \$10 million	90 days	N/A
>\$10 million to \$50 million	180 days	+/- 20%
>\$50 million to \$100 million	1 year	+/- 20%
>\$100 Million	2 years	+/- 20%

\* For determining minimum advance notice, withdrawal requests are treated cumulatively by Department Group (high-level School, College, Unit) within a rolling 12-month period.

\*\* Submitted requests can be cancelled within five business days; otherwise, they cannot be terminated. Beyond this period, for requests in excess of \$10 million, amount can be adjusted by +/- 20% up to 90 days prior to the withdrawal processing date.

Examples: A withdrawal of \$5 million for July 1 needs to be submitted by March 31 while a withdrawal of \$60 million for July 1 needs to be submitted by June 30 of the previous calendar year. Adjusting the amount originally requested of \$60 million by +/- 20% (\$12 million) needs to be submitted by March 31.

For additional information about the UEF, also referred to as the university's pooled endowment funds, visit the Financial Operations website.

#### h. EXIGENT CIRCUMSTANCES

In exigent circumstances, the university's Executive Vice President and Chief Financial Officer may suspend new contribution or withdrawal requests for which notification has not already been provided until financial markets stabilize to protect the overall portfolio.

## 2. ENDOWMENT SPECIFIC FUNDS

Endowment Specific Funds may be created in exceptional circumstances when funds cannot be pooled; for example, when a donor gives a gift for the purpose of establishing a fund with property that cannot be readily sold or a donor stipulates that their funds may not be commingled with pooled university funds. These funds may consist of non-publicly traded securities, life insurance policies, real estate, or other items. Because these funds do not have the ability to buy shares in the UEF, they are separately managed in their own individual Endowment Specific Fund.

Financial Operations is responsible for the administration of the UEF and Endowment Specific Funds.

## C. LIFE INCOME AGREEMENTS

The university administers three types of life income agreements: Charitable Gift Annuities,

Charitable Remainder Trusts and Donor Pooled Income Fund. Life income agreements, also referred to as deferred gifts, provide a stream of income to the donor or others for life or for a term of years. Distributions are made quarterly and the principal is not withdrawn for university use until termination of the non-charitable interest.

The Office of University Development is responsible for the administration of life income agreements. The following are general descriptions of the types of life income agreements currently administered by the university.

Charitable Gift Annuity (CGA) is a simple contract between the donor(s) and the university. In exchange for the donor's contribution, the university promises to make fixed quarterly payments for life to one or two annuitants (usually but not necessarily, the donor(s)). Establishing a CGA requires a minimum gift of \$10,000 in cash or readily marketable securities, which is deposited in the university's segregated Gift Annuity Fund. Each annuitant must be at least 50 years of age when annuity payments commence. Contributions to a CGA are irrevocable gifts. Upon the death of the last annuitant, the value associated with the annuity in the Gift Annuity Fund is transferred to the receiving university department as directed by the donor for purposes specified by the donor. Departments must use the money according to the donor's intent and university policy.

Charitable Remainder Trust (CRT) allows a donor to make a charitable gift, which will also provide quarterly payments to one or more beneficiaries for their lifetimes, or for a specific term of years. Upon the death of the income beneficiaries or expiration of the specified number of years, the trust will terminate and the principal will be distributed to the university (and other charitable organizations if so directed by the donor), for purposes specified by the donor. Establishing the trust with the university as trustee requires a minimum \$100,000 irrevocable gift of cash, readily marketable securities and/or other property acceptable to the university.

Donor Pooled Income Fund (DPIF) is a fund that was established by the university to receive irrevocable contributions of property, cash and readily marketable securities from donors; however, the DPIF is closed to new donors. Contributions to the DPIF are pooled for investment purposes and each gift purchases shares of participation in the pool. Designated beneficiaries receive an annual lifetime income that represents their pro rata share of income of the fund. Upon the death of all individuals named as beneficiaries, the donor's participation in the Fund will terminate, and the value of this participation will be distributed for use by the university as the donor has directed. DPIF share values are recalculated monthly. Income distributions are made quarterly to income beneficiaries based on their prorated share of the amount of income earned for that period by the fund.

The university may also have an interest in a charitable lead trust, which provides annual gift income to the university for a specified number of years or for a period measured by the life or lives of an individual or individuals, after which the trust assets again become available to the donor, the donor's family or others. Currently, the university will not act as trustee for a charitable lead trust.

#### D. INSURANCE AND BENEFITS RESERVES

The university is self-insured for various lines of insurance, including medical malpractice, workers' compensation, directors' and officers' liability, property damage, auto liability and general liability through Veritas Insurance Corporation, a wholly-owned captive insurance company. The university is also self-insured for various employee benefits through internally maintained funds. These reserves are invested in the university's various investment portfolios in accordance with the expected duration of the related liabilities.

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Additional information on Expendable & Endowed Gifts (<http://finance.umich.edu/.nops/accounting/gifts>)

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