THE CAMPANILE FOUNDATION

Supporting San Diego State University

Endowment Management Handbook

July 2024

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1. Introduction

1-1. What is an Endowment?

An endowment is established through a donation that includes a legal requirement that the initial contribution remains intact indefinitely. These donations are preserved and invested by The Campanile Foundation (the Foundation), a philanthropic tax-exempt foundation and an official auxiliary of San Diego State University (SDSU). The aim is to create a continual source of spendable income from the returns on the donation for the purpose specified by the donor.

1-2. Why are Endowed Donations Valuable to SDSU?

Endowed donations can be designated for specific or general uses and are especially valuable to SDSU because of their enduring nature. Such donations enable long-term planning for various campus programs.

2. TCF Endowment Management

2-1. How are Endowment Funds Administered?

At the Foundation, endowment fund management is governed by the principles outlined in its Investment Policy Statement, which adheres to the Uniform Prudent Management of Institutional Funds Act and other applicable laws. The endowment funds are pooled for investment purposes, enhancing financial efficiency and stability. Each individual endowment fund contributes to this combined portfolio by holding units, allowing for proportional benefit from the overall performance.

2-2. How are New Contributions Handled?

New contributions to any endowment fund are allocated to the principal of the fund and invested within this pooled structure. The annual spending policy, recommended by the Finance & Investment Committee and reviewed and approved by the Board of Directors, dictates the expendable income that is distributed each quarter to the endowment's designated income fund(s). This distribution supports the specific purposes intended by donors and is managed within the constraints of the policies. The total return of the endowment funds, after accounting for the quarterly distribution, is reinvested to safeguard against inflation and promote fund growth.

2-3. What is the Endowment Investment Strategy?

The endowment investment strategy is primarily managed according to the directives set forth in the Investment Policy Statement, aligning with the guidelines from the Uniform Prudent Management of Institutional Funds Act. The endowment funds are strategically invested through a diversified portfolio that includes various asset classes to achieve a balance of risk and return conducive to long-term growth. This portfolio typically comprises equities, fixed income securities, and alternative investments, such as private equity and real estate.

2-4. What are the Investment Goals?

The endowment investment strategy follows the goals set out in the Foundation's Investment Policy Statement. These goals focus on increasing the value of the Foundation's assets over time. The strategy aims to achieve a return on investment that exceeds the benchmarks set for periods of 3-5 years and beyond 5 years. Specifically, the endowment aims to secure a real return of 4.0% after expenses and aims to perform better than the return rates of benchmark indices that match the Foundation's planned asset distribution.

2-5. Who Oversees the Investment Management?

The management of these investments is overseen by the Finance and Investment Committee of the Foundation, which operates under the approval of its Board of Directors. The committee is responsible for setting annual spending rates, reviewing investment performance, and making necessary adjustments to the strategic asset allocation to reflect current economic conditions and market opportunities.

2-6. How are Investments Monitored and Rebalanced?

Investments are continually monitored and rebalanced to maintain adherence to the target asset allocation, ensuring that the endowment remains well-positioned to capture growth while mitigating risks associated with market volatility. By employing a blend of internal oversight and external investment management expertise, the Foundation strives to achieve financial returns that support its long-term educational and institutional goals.

2-7. What are the Guidelines for Spending Endowment Returns?

The policy on the expenditure of the return earned on endowed funds specifies that the Foundation manages permanently restricted assets with the donor's stipulation that the original donation must be maintained indefinitely. However, the Foundation is allowed to spend the income and gains derived from these assets according to its spending policy.

2-8. What is the Annual Spending Rate?

The Foundation has established an annual spending rate of 4.0% of the endowment's market value, which is applied to the rolling 3-year average unit value of the endowment. This rate is reviewed annually by the Finance & Investment Committee, which may propose changes based on their assessments. The spending policy is designed to protect the principal of the endowment while providing a stable and sustainable income stream for the university's purposes, thus preserving the real spending power of the assets over time.

2-9. How is Endowment Management Structured?

The operational principles of endowment investment and management are similar to those of stock investments. The endowment funds are typically pooled in a unitized investment structure. This pooling allows each individual endowment to own units in the investment pool, with the units being revalued at the end of each quarter. New endowments can only enter the pool at these quarter-end periods, purchasing units based on the quarter-end unit value.

2-10. How Does the Investment Process Work?

Here's how the process works: Each new endowment buys into the pool by purchasing a certain number of units, determined by the amount of the investment and the unit. The unit value is calculated using a 3-year moving average unit value to ensure a fair and stable entry point for new investments. As the unit value increases over time, new endowments buy fewer units for the same investment amount, reflecting the appreciation of the investment pool.

2-11. Can You Provide an Example of the Investment Process?

For instance, let's consider an endowment pool with a total market value of $400,000,000 as of December 31, 2022, and 400,000 units in the pool. This valuation places the unit value at $1,000 per unit. If the Smith Endowment were to contribute $100,000 after the gift fee of 5%, it would buy units in the pool based on the current unit value. On January 1, 2023, the Smith Endowment would purchase units at $1,000 per unit, resulting in the acquisition of 100 units.

2-12. How Does the 3-Year Moving Average Unit Value Help?

This straightforward example illustrates the mechanics of how endowment investments are managed, showing the process by which new contributions are assimilated into the pooled investment structure and highlighting the impact of unit value appreciation on new investments. The use of the 3-year moving average unit value helps in smoothing out short-term fluctuations and provides a more consistent basis for investment.

2-13. How Does Distribution Work?

The distribution of returns from the endowment funds is carefully calculated based on the market value of the endowment at the end of the previous quarter. For example, if a new gift of $100,000 is received on January 1, 2023, no distribution would be made on March 31, 2023, because the endowment value on December 31, 2022, did not account for this new gift.

2-14. What is the Distribution Policy for Different Types of Endowments?

The distribution amount varies depending on the type of endowment. For a true endowment, where the principal must be preserved, the distribution amount cannot exceed the surplus of the market value over the historical value (principal) at the end of the previous quarter.

2-15. How Does a Quasi-Endowment Differ in Distribution?

In contrast, for a quasi-endowment, the entire market value can potentially be distributed, subject to policy limits. According to the Foundation’s Investment Policy Statement, the maximum distribution rate is set at 4% of the endowment's market value annually.

2-16. What Happens if an Endowment is 'Underwater'?

In situations where the market value of a true endowment is less than its historical value at the end of a quarter - referred to as being 'underwater' - no distribution is made in the following quarter. For instance, if the market value of a true endowment is $90,000 and the historical value is $100,000 as of March 31, 2023, indicating that the fund is underwater, no distribution will occur on June 30, 2023. However, if market conditions improve and the endowment value exceeds the historical value by June 30, 2023, a distribution will be made on September 30, 2023. This policy ensures that the endowment funds are managed to protect their long-term value while supporting the university's ongoing financial needs.

3. Endowment spending calculation examples

The actual spending for any individual endowment is computed quarterly using the following information.

Units and Unit Value:

- **Unit**: Represents a share or portion of the endowment pool. Each endowment fund owns a certain number of units in the overall endowment pool.
- **Unit Value**: The monetary value of each unit in the endowment pool, which is calculated based on the total value of the endowment pool divided by the total number of units.

Calculation Process:

1. **Units Held**: The number of units held in an individual endowment as of the end of the previous quarter.
2. **3-Year Moving Average Unit Value**: The average value of a unit over the past three years.
3. **Distribution Percentage**: Maximum of 4.0% annually
4. **Estimated Annual Distribution**: This is calculated as:

   Units Held × 3-Year Moving Average Unit Value × Distribution Percentage

5. **Amount Available for Distribution**: This depends on whether the endowment is "true" or "quasi".
   - For "true" endowments, it is the difference between the last quarter's market value and the historical gift amount.
   - For "quasi" endowments, it is the entire market value.
6. **Final Annual Distribution**: The lesser of the estimated annual distribution or the amount available for distribution.
7. **Final Quarterly Distribution**: The final annual distribution divided by 4.

Example 1: Quasi Endowment A

- Units Held: 4,361.09
- 3-Year Moving Average Unit Value: $708.87
- Distribution Percentage: 4%

Estimated Annual Distribution:
4,361.09 × 708.87 × 0.04 = $123,658

Market Value: $3,053,212, **Historical Gift Amount**: $2,658,117
Since this is a quasi endowment, the amount available for distribution is the entire market value:
Amount Available = $3,053,212

Final Annual Distribution:
Lesser of Estimated Distribution or Amount Available = $123,658

Final Quarterly Distribution:
Final Annual Distribution ÷ 4 = $30,915

Example 2: True Endowment B – Well Established

- Units Held: 334.80
- 3-Year Moving Average Unit Value: $708.87
- Distribution Percentage: 4%

Estimated Annual Distribution:
334.80 × 708.87 × 0.04 = $9,493

Market Value: $234,391, **Historical Gift Amount**: $94,126
Since this is a true endowment, the amount available for distribution is the market value minus the historical gift amount:
Amount Available = $234,391 − $94,126 = $140,265

Final Annual Distribution:
Lesser of Estimated Distribution or Amount Available = $9,493

Final Quarterly Distribution:
Final Annual Distribution ÷ 4 = $2,373

Example 3: True Endowment C – Slightly Above Historical Gift Amount

- Units Held: 95.65
- 3-Year Moving Average Unit Value: $708.87
- Distribution Percentage: 4%

Estimated Annual Distribution:
95.65 × 708.87 × 0.04 = $2,712

Market Value: $66,963, **Historical Gift Amount**: $66,500
Since this is a true endowment, the amount available for distribution is the market value minus the historical gift amount:
Amount Available = $66,963 − $66,500 = $463

Final Annual Distribution:
Lesser of Estimated Distribution or Amount Available = $463

Final Quarterly Distribution:
Final Annual Distribution ÷ 4 = $116

Example 4: True Endowment D - Underwater

- Units Held: 447.02
- 3-Year Moving Average Unit Value: $708.87
- Distribution Percentage: 4%

Estimated Annual Distribution:
447.02 × 708.87 × 0.04 = $12,675

Market Value: $312,957, **Historical Gift Amount**: $323,592
Since this is a true endowment and the market value is less than the historical gift amount (the endowment is underwater). Therefore, the amount available for distribution is $0.
Amount Available = $0

Final Annual Distribution:
Lesser of Estimated Distribution or Amount Available = $0

Final Quarterly Distribution:
Final Annual Distribution ÷ 4 = $0

4. Definition of Terms

True Endowment

An endowment fund established by donor-restricted gifts to provide a permanent source of income. The principal amount of the gift is maintained intact, and only the investment income generated by it is used for purposes specified by the donor.

Quasi-Endowment

An endowment fund that is invested to allow for the expenditure of both principal and income. Unlike true endowments, quasi-endowments are not permanent funds but are considered long-term investments.

Market Value

The total value of the endowment fund's investments at a specific point in time. This includes all activities such as donations, distributions, transfers and investment performance.

Historical Value

The total of all gifts less any gift fees plus any transfers of funds into the endowment. This value represents the original amount of donations made to the endowment, and it serves as a baseline for determining whether an endowment is underwater.

Underwater Endowment

An endowment fund where the current market value is less than the historical value. In this situation, distributions may be suspended until the fund's market value recovers above the historical value.

Restricted Fund

A fund where the donor has specified particular uses for the gift. The institution must use the fund's income and sometimes the principal for the donor's specified purpose.

Unrestricted Fund

A fund where the donor has not specified any restrictions on how the gift is to be used. The institution can use the fund's income and principal for any purpose it deems appropriate.

Distribution

The amount of money distributed from the endowment's earnings to income funds to support the institution's operations or specific donor-designated purposes. This distribution is usually calculated as a percentage of the endowment's market value.

Income Fund

A fund that receives distributions from the endowment and is used to support the operations or specific programs designated by the donor. The balance of the income fund is used for expenditures such as scholarships or program funding. Specifically, A funds are assigned for scholarships, and C funds are assigned for campus programs.

Spending Policy

A set of guidelines determining how much of the endowment's earnings can be spent each year. The spending policy is designed to protect the principal of the endowment while providing a stable and sustainable income stream. According to the Investment Policy Statement, the typical spending rate is set at 4.0% of the endowment's market value, applied to a rolling 3-year average unit value.

Investment Performance

The return on the endowment's investments over a specific period, including income from dividends and interest, as well as unrealized and realized capital gains or losses. Investment performance affects the endowment's market value and the amount available for distribution.

Unit

Represents a share or portion of the pooled endowment fund. Each endowment fund holds a certain number of units in the overall endowment pool. Unit and Unit Value are used to calculate the distribution amount.

Unit Value

The monetary value of each unit in the endowment pool. It is calculated by dividing the total market value of the pooled endowment by the total number of units.

Uniform Prudent Management of Institutional Funds Act (UPMIFA)

A set of guidelines for managing and investing endowment funds, emphasizing prudent spending and investment practices. At TCF, endowment fund management adheres to UPMIFA principles outlined in its Investment Policy Statement. Endowment funds are pooled for investment, enhancing financial efficiency and stability. The annual spending policy, recommended by the Finance & Investment Committee and approved by the Board of Directors, dictates quarterly distributions to designated income funds. This ensures funds are managed prudently while promoting growth and safeguarding against inflation.