

## **ENDOWMENT SPENDING POLICY**

From minutes 5/12/2000

**Approval authorizing Changes in Endowment Spending.** Mr. Bostock concluded with a report on the Committee's discussion relating to the proposed spending rate changes. A memorandum providing background (a copy of which, initialed by the Secretary, is attached to the minutes as Appendix G) was mailed to all Trustees with the agenda materials. He explained that the proposed rate would increase the rate of spending from 5.0%, as approved by the Board in 1997, to 5.5%. The 5.5% annual endowment spending rate would include a 4.25% allocation for direct program costs, which will be distributed to each expendable endowment code consistent with current practice. One of the changes in the policy, in addition to the increase in the rate, is the allocation of 1.25% of the 5.5% to the operating budgets of schools and other management units to help defray the academic and administrative support and space costs associated with endowment supported programs. Noting that the proposed spending rate structure is similar to many of Duke's peer institutions, Mr. Bostock reported that the Business and finance Committee unanimously supported the proposal and recommended approval by the Board. The following resolution was approved:

WHEREAS, in May 1997 the Board of Trustees approved a spending policy for the University's Long Term Pool and adopted spending policies which set a target spending rate for the funds of the University in the Long Term Pool equal to five percent (5.0%) per annum, with an additional provision that allowed for periodic special withdrawals from unrestricted quasi-endowment funds (limited to 0.5% of the market value per year of the university's total endowment funds) for special projects and strategic opportunities; and

WHEREAS, although the approved policy included a six-year transition plan to achieve the 5.0% target spending rate, the targeted rate was achieved in the calculation made at December 31, 1998 for the fiscal year 1999-2000, three years earlier than originally anticipated; and

WHEREAS, the endowment-supported programs of the University have historically provided funding only for the direct costs of these programs, with the academic and administrative support costs of these programs being provided by the schools and other sources of internal funding; and

WHEREAS, the growth in the University's Long Term Pool in recent years, combined with a proposed increase in the spending rate from 5.0% to 5.5%, provides the University with a unique opportunity to introduce the practice of distributing a portion of annual endowment spending to help cover academic and administrative support costs associated with endowment-supported programs without decreasing the direct support expectancies of those programs; and

WHEREAS, the increase of the spending rate applicable to the Long Term Pool from 5.0% to 5.5% & is within parameters assumed at Duke Management Company("DUMAC")

for annual rates of inflation (5.0%) and total real return (5.5%) and provides protection of the purchasing power of the endowment funds while providing an adequate level of spendable income for program for program support; and

WHEREAS, the University's Administration has recommended approval of this revised spending policy and, upon due consideration this Board has approved the revised spending policy for the funds of the University invested in its Long Term Pool in accordance with the resolutions set forth herein.

NOW THEREFORE, BE IT RESOLVED,

1. Spending rate. The Long Term Pool spending rate for all funds invested, unless otherwise indicated by special agreement or exempted herein, shall be five and one-half percent (5.5%) per annum, calculated as a percentage of the average of the unit market values of all funds invested in the Long Term Pool of the University at the end of the calendar year for the three (3) calendar years immediately preceding the fiscal year in which the calculation is made; for example, the fiscal year 2000-2001 spending rate will be calculated at December 31, 1999 as five and one-half percent (5.5%) of the average unit market values at calendar year-end for calendar years 1997, 1998, and 1999. Note: the purposes of this three-year calculation are to provide a per unit spending amount which floats with market fluctuations by the use of a three year rolling average of market values.
2. Limitation on Annual Increase of Per Unit Spending. The increase in spendable income available per unit in any given year shall be limited to an increase equal to ten percent (10%) of the spendable income available for the immediately prior fiscal year.
3. Distribution of Spendable Income. The spendable income generated by the application of the spending rate will be allocated and distributed as follows:
  - a. funds other than endowment funds: all of the spendable income generated by the five and one-half percent (5.5%) spending rate will be distributed to the fund;
  - b. endowment funds (both permanent endowment and quasi-endowment funds): the spendable income generated by the five and one-half percent (5.5%) spending rate will be distributed in the following manner:
    - (1) the spendable income generated by four and on quarter (4.25%) will be allocated to direct program costs and distributed to each expendable endowment associated fund code consistent with current practice; and
    - (2) except as provided in 3.b.(3) below, the spendable income generated by one and one-quarter percent (1.25%) will be allocated to help defray the space and academic and administrative support costs associated with endowment-supported programs by distribution to the appropriate

operating budgets of schools and other major management entities within which those endowment-supported programs are operated.

- (3) as to endowment-supported financial aid programs, the spendable income generated by one-half of one percent (.50%) will be allocated to help defray the space and academic and administrative support costs associated with endowment-supported financial aid programs by distribution to the appropriate operating budgets of schools and other major management entities within which those endowment-supported programs are operated; this reduced rate is provided to take into consideration the fact that indirect costs related to financial aid programs are less proportionately related to the size of the supporting endowment funds than are other endowment-supported programs.

c. exemption of certain endowment funds: the following funds shall be exempt from a distribution toward academic and administrative support costs:

- (1) funds which support the Clinical Departments in the School of Medicine, which are already assessed and overhead charge by the School of Medicine;
- (2) funds created to support special projects which are, by their terms, exempt from the spending rate policy of the University; for example, the special endowment funds established to support the programs of the Levine Science Research Initiative;
- (3) funds created to provide matching funds for fund-raising efforts (e.g. Duke Endowment Funds);
- (4) funds which are inactive while accumulating value until a certain funding level is reached;

d. review of portion of annual spending allocated to academic and administrative support costs: the proposed portion (1.25%) of the total spending rate of 5.5% is believed to be appropriate and to accurately reflect a conservative allocation of indirect costs; however, to ensure continued reasonableness, the Administration will conduct an annual review of the accuracy and appropriateness of the academic and administrative support component of the spending rate and report its results to this Board of Trustees.

4. Effective date. The spending rate policy approved herein shall be effective July 1, 2000.
5. Special endowments and special reserve funds. Special endowments and special reserve funds invested in the Long Term Pool described in 3.c.(2) above will continue to return one hundred percent (100%) of annual earnings

to principal and this Board of Trustees will continue to authorize an annual spending plan for each such endowment or fund.

6. Return of principal. In permanent endowment agreements in which the donor has stipulated a return of a portion of annual earnings to principal, this will be accomplished through growth in the unit market value, which contains both realized and unrealized gains.
7. Review of Spending Rate. The Administration will conduct a review, within five years from the effective date of this resolution, of the various assumptions and elements on which this resolution has been based to ensure that the spending rate of five and one-half percent (5.5%) adopted herein is still valid. The results of this review will be reported to the Board of Trustees at a date no later than the annual meeting to be held in May 2005.
8. Annual Reports. Annual reports on the operation of this spending rate policy will be submitted to this Board of Trustees.
9. Effect of this Resolution. This resolution shall supersede and replace the Spending Policy Resolution of this Board of Trustees approved May 16, 1997 and all other resolutions which may conflict with the provisions of this resolution.

AND BE IT FURTHER RESOLVED, that the Officers of the University are hereby directed to undertake all efforts and execute all documentation required to implement the corporate action described above.