



## UC SAN DIEGO FOUNDATION ENDOWMENT INVESTMENT AND SPENDING POLICY

### PURPOSE

This Policy statement includes both objectives and guidelines intended to apply to the pooled endowment investment assets (“Endowment”) in the UC San Diego Foundation. This Policy is designed to:

- Establish appropriate risk and return objectives in light of the risk tolerance and the perpetual investment time horizon for the Endowment.
- Establish asset allocation guidelines and suitable investments for the Endowment, consistent with the risk and return objectives of the policy.
- Describe the roles and responsibilities of parties overseeing the Endowment.
- Provide benchmarks for ongoing monitoring of investment performance of the Endowment.

### I. GENERAL INVESTMENT AND SPENDING POLICY

The UC San Diego Foundation has adopted the principles of and requirements under the Uniform Prudent Management of Institutional Funds Act. Endowment investment policy and decisions for asset placement are based on a long-term investment strategy appropriate for an institutional endowment to be held in perpetuity. The Endowment will be invested to maximize long-term total return under the parameters described below. A spending rate will be determined annually.

The Endowment investment policy shall serve to diversify investments and provide a balance that will enhance total return while avoiding undue risk concentration in any single asset class or investment category. The Endowment spending policy will be determined giving consideration to achieving an objective of an estimable revenue stream for fund holders that retains its purchasing power.

### II. ENDOWMENT RETURN GOALS AND RISK PROFILE

The primary investment objective for the Endowment is to preserve or enhance the real value of the Endowment and, thus, the purchasing power of the endowment spending released (including administrative costs). The Foundation seeks to maximize the return on endowed pool assets, within a prudent level of risk, by utilizing a diversified portfolio of securities that delivers return in the form of both asset appreciation and income.

Giving consideration to the objective, the return goals are as follows:

1. **Returns Equaling Inflation-Adjusted Spending Rate.** To achieve an average total annual net return equivalent to the endowment spending rate (noted below) adjusted for inflation. (Inflation is defined as the Consumer Price Index, US Department of Labor, Bureau of Labor Statistics US

City Average, All Items, Base Period 1982-1984 =100). This goal shall be measured over an annualized, rolling three, five, and ten-year period.

2. **Outperform Peer Group.** To outperform the average total annual net return of peer endowments of similar size, as measured over rolling three, five and ten-year periods.

Portfolio performance will be calculated and monitored as noted in Appendix B. The actual asset allocation and the benchmark indexes will be determined by the Investment Committee from time-to time, and reviewed by the Committee and reported to the Board at least quarterly.

The acceptable risk profile for the Endowment should generally be to assume a prudent level of risk for the return goal desired. While negative returns in any single year may be unavoidable, over longer terms, asset allocations should be selected which are expected to achieve overall positive portfolio returns. In order to assess and monitor portfolio risk, the Investment/Finance Committee will review its asset allocation policy at least annually.

Risk can be construed to include multiple different outcomes including loss of principal, failure to meet an expected return or most commonly volatility of investment returns around an expected mean (standard deviation). The Investment Committee's policy regarding investment risk, consistent with modern portfolio theory, is that risk cannot be eliminated but should be managed. Investment committee members, with the help of the Foundation's investment consultant, investment managers, and Foundation staff, are responsible for understanding the risks inherent in various investment strategies, ensuring that they are properly compensated for these risks, and measuring and monitoring them. Risk is considered in the hiring of new investment managers as well as in the continued monitoring of existing investment managers and the overall portfolio. Risk is also considered in the selection of individual asset classes and the overall portfolio asset allocation. Most importantly, the level of overall portfolio risk taken should be consistent with the overall return objectives of UC San Diego Foundation.

### III. SPENDING POLICY

The Endowment Spending Policy (stated as a percentage) will be reviewed annually and set in the spring of each year (with an effective date of the upcoming July 1 to June 30 fiscal year) by recommendation of the Investment/Finance Committee to the Board of Trustees. An endowment administration cost recovery fee of 55 basis points will be included in the spending policy and will be paid by the Foundation to the UCSD campus as a funding source for operating costs of Advancement.

Endowment spending made available to fund holders will be in an amount that the Board deems prudent for the uses, benefits, purposes, and duration for which the endowment fund is established. Prior to the beginning of each fiscal year, endowment fund holders will be notified of projected spending for that fiscal year.

Spending will be calculated annually, and made available at least quarterly, based on a formula and rate as approved by the Board annually.

#### IV. RESPONSIBILITIES

The following parties associated with the Endowment shall discharge their respective responsibilities in accordance with all applicable fiduciary standards as follows: (1) in the sole interest of the Endowment's beneficiaries; (2) with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and of like aims; and (3) by diversifying the investments so as to minimize the risk of large losses.

- A. Board of Trustees: The Board of Trustees has overarching fiduciary responsibility for the assets of the Foundation, including the Endowment. (The Board also recognizes that it shares this fiduciary role with the UC Regents.) The Board is responsible for determining and approving, upon recommendation by the Investment/Finance Committee, the Foundation's Investment and Spending Policies overall asset allocation ranges and targets; risk/return objectives, setting guidelines for reporting and monitoring of performance, and the use of any consultants. In determining these items, the Board and the Committee will ensure that any governing laws and UC Regents policies are adhered to pertaining to the investments of the campus foundations as in effect from time-to-time.
- B. Investment/Finance Committee: The members of the Investment/Finance Committee are delegated authority by the Board of Trustees to provide oversight of the day-to-day administrative issues associated with the Endowment's assets. The Committee has the authority to implement this Investment and Spending Policy; specific responsibilities of the Investment/Finance Committee include the following:
1. Establish and, when deemed necessary, recommend modifications to the Endowment Investment and Spending Policy to the Board for approval.
  2. Review investment policy annually to ensure compliance and relevance to the current law, financial and economic trends, and to meet the needs of the Endowment.
  3. Determine the overall asset allocation ranges and targets, and risk/return objectives, and report changes in such to the Board for approval from time-to-time.
  4. Select specific investments, professional investment managers, brokers, and administrators, and negotiate and monitor terms and conditions of their services.
  5. Cause investment purchases to be made, via staff, in accordance with policy, and instruct or assist staff in carrying out policy as needed.
  6. Monitor performance of the Endowment against appropriate benchmarks at least quarterly, and more often if necessary.
  7. Assure proper custody of the investments.
  8. Report the Endowment asset allocation, and performance results at least quarterly to the Board of Trustees on the Endowment, and as requested to the UC Office of the Chief Investment Officer (OCIO) or UC Regents.
  9. Retain an investment consultant to assist with this process as necessary.
- C. Investment Consultant: An investment consultant will be charged with the responsibility of advising the Investment Committee on investment and spending policy, asset allocation,

manager structure, investment manager selection, performance analysis and monitoring and education. The investment consultant must agree to act as a “fiduciary” to the Endowment.

The investment consultant shall advise the Investment/Finance Committee of any restrictions within this Policy that may prevent the investment manager(s) from obtaining the objectives and goals set forth herein. Any violation of the investment guidelines or other sections of the Policy discovered by the investment consultant in the preparation of its regular performance review shall be reported immediately to the Investment/Finance Committee and discussed at their next regularly scheduled meeting.

- D. Investment Manager(s): As appropriate, and based upon the advice of the investment consultant, industry-regulated investment products will be used, and/or investment manager(s) will be hired and delegated the responsibility of investing and managing the Endowment’s assets in accordance with this Investment Policy and all applicable law. Each investment manager must either be (1) registered under the Investment Company Act of 1940, (2) registered under the Investment Advisors Act of 1940, (3) a bank, as defined in that Act, (4) an insurance company qualified under the laws of more than one state to perform the services of managing, acquiring or disposing of the Endowment’s assets, or, (5) such other person or organization authorized by applicable law or regulation to function as an investment manager including the Office of the Chief Investment Officer of the Regents of the University of California and its pooled or vintage funds. Managers will be monitored and will adhere to the Guidelines for Investment Managers in Appendix B of this Policy.

## **V. PRUDENCE, ETHICS AND CONFLICT OF INTEREST**

All fiduciaries involved in the investment process shall act responsibly and without conflict with other business or personal interests, in accordance with the Foundation’s Conflict of Interest Policy and annual declarations. The standard of prudence to be applied to the Investment/Finance Committee, the investment consultant, each investment manager, and each other fiduciary with discretion respecting management of Endowment assets shall be the “prudent investor” rule. This rule requires each fiduciary to invest and manage endowed assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust. In satisfying this standard, the fiduciary shall exercise reasonable care, skill, and caution. A fiduciary’s investment and management decisions respecting individual assets must be evaluated not in isolation but in the context of the endowed portfolio as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the endowment.

## **VI. ENDOWMENT ASSET CLASS GUIDELINES**

The Endowment assets may be invested in any combination of individual securities, separately managed accounts with investment managers, commingled funds, mutual funds, or in the pools or separate programs offered to campus foundations as managed by the UC OCIO (including the GEP and related vintage pools). In cases of the use of investment managers, they will have full discretion over their portfolio management decisions in accordance with guidelines provided by this Policy. In the case of commingled funds and mutual funds, their management will be carried out within their respective structures and in accordance with the prospectus material published.

The composite asset classes of Endowment investments that may be deployed are noted below. The permissible asset allocation ranges and the targets for each category, along with additional specifics, are stated in Appendix A and B of this Policy.

A. **Equity Investments:**

The equity portion shall be invested under the following guidelines:

1. Allowable investments include US and non-US publicly traded common stocks, preferred stocks, stock warrants and rights, convertible bonds, as well as REITs (real estate investment trusts) and any other investments as allowed by respective prospectuses.
2. Equity securities shall be diversified so that any direct investments in companies do not exceed 5% of the value of the Endowment's equity portfolio based on cost at the time of acquisition or 7% at market value of the equity portfolio; this excludes indexed or ETF funds.
3. The Endowment shall not hold more than 5% of the equity securities, or those securities convertible into equity securities, of a single issuer, excluding indexed or ETF funds.

B. **Fixed Income Investments:**

The fixed income portion shall be invested under the following guidelines:

1. Allowable investments include US and non-US corporate and government bonds, asset-backed securities and any other fixed income investments as allowed by respective prospectuses, including inflation-protected securities.
2. With the exception of U. S. Government and Agency issues, no more than 10% of the bond portfolio at market will be invested as direct investments of securities of a single issuer or 5% of the individual issue; this excludes indexed or ETF funds.

C. **Alternative Investments:**

Alternative investments are those outside the traditional asset classes of stocks, bonds and cash, and include a wide array of investment products. The Investment/Finance Committee recognizes that alternative investment classes may help to reduce the Endowment's volatility and/or enhance overall performance. It is the intent of the Investment Committee to place a portion of assets, as specified in Appendix B, in alternative investment strategies.

D. **Cash**

Endowed cash will be invested in the STIP fund as managed by the UC OCIO. Cash returns on investments or new endowed gifts will be held in STIP for purposes of meeting payout requirements or until the cash can be invested in other asset classes in accordance with this Policy.

**VII. ENDOWED ASSETS RECEIVED BY GIFT**

Certain endowed gift assets may be received by the Foundation from time to time with a limited means of liquidation, or that the Investment/Finance Committee determines should be held and retained as the sole endowed asset of a particular fund. Such assets and funds will be excluded from this policy. Spending for that fund will be determined by a separate action of the Investment/Finance Committee, depending on the type of asset involved.

**APPENDIX A**

**TARGET ASSET ALLOCATION, LIQUIDITY MANAGEMENT, AND REBALANCING**

**Target Asset Allocation**

The target asset allocation for the Endowment is determined by the Investment/Finance Committee to facilitate the achievement of the Endowment investment objectives within the established risk parameters. Allocation of funds between asset classes may be the single most important determinant of the investment performance over the long-term. Formal asset allocation studies and a review of capital market assumptions should be conducted at least every two years, with annual evaluations of the validity of the adopted asset allocation.

The Endowment assets shall be divided into the following general asset classes, which are further described in Appendix B. The targets and ranges for each class are included.

<b>Asset Class</b>	<b>Permissible Range</b>	<b>Target Asset Allocation</b>
U.S. Equities	15-35%	21 %
Developed Non-US Equities	10-30%	17 %
Emerging Markets Equities	0-15%	6 %
<b>Total Public Equities</b>	<b>40%-60%</b>	<b>44 %</b>
<b>Fixed Income</b>	<b>5%-20%</b>	<b>12%</b>
Real Estate & Real Assets	5-15%	11 %
Private Equity	5-15%	13 %
Diversifying Strategies	10-30%	20%
<b>Total Alternative Investments</b>	<b>20%-50%</b>	<b>44%</b>
<b>Cash</b>	<b>0%-5%</b>	<b>0%</b>

### **Liquidity Management**

Foundation staff will monitor cash flow on a regular basis, and sufficient liquidity shall be maintained to ensure spending policy is met for fund holders. When withdrawals become necessary, staff will notify the investment manager(s) as far in advance as possible to allow them sufficient time to liquidate assets as necessary.

### **Rebalancing**

Foundation staff will use best efforts to rebalance the investment portfolio on an ongoing basis (and no less than quarterly) as cash returns and new gifts to the endowment are received, or market value fluctuations occur in asset classes that require divestment and redeployment to other asset classes. When possible, dollar cost averaging will be deployed. The Investment/Finance Committee will approve a set of rebalancing guidelines and amend them from time-to-time to provide staff with guidance as to sub-asset class allocations, and asset placement where over or under weightings are necessary. All new investments and rebalancing actions will be reported to the Investment/Finance Committee at least quarterly.

The purpose of rebalancing is to move the investment portfolio towards the target asset allocation taking into consideration factors such as market conditions, planned asset allocation actions, circumstances of the product/manager being used, and liquidity of the asset classes. While the target asset allocation is unlikely to be precisely achieved, the portfolio is expected to remain within the boundaries of the ranges around the target asset allocation. The Committee may, from time-to-time, make a tactical asset allocation decision to not rebalance for a particular reason or time frame.

## APPENDIX B

### **PERFORMANCE MEASUREMENT, MANAGER REVIEW AND CORRECTIVE ACTIONS, ASSET CLASS DEFINITIONS, AND OTHER MATTERS**

#### **Performance Measurement**

With the advice and analysis provided by the Investment Consultant, the Investment/Finance Committee will review the realized return for the period, or Portfolio Return (PR), at least quarterly and for rolling one, three, five and ten-year periods. The PR will be reviewed and benchmarked to the return goals noted in Section II of this Policy.

In addition, using appropriate benchmarks as determined by the Investment Committee for each composite asset class, as well as for each manager, Portfolio Return (PR) will be analyzed quarterly and for similar rolling periods as noted above by the Investment Consultant in terms of the contribution to return as described by four components where:

$$\text{PR} = \text{PAA} + \text{STAA} + \text{SB} + \text{MS}$$

1. **Policy Asset Allocation (PAA)** – The Policy Asset Allocation measures and is computed by the weighted average return of a broad set of asset class indices according to the target allocation specified in this Policy, Appendix A. The PAA represents the return the portfolio would achieve if the Foundation pursued a pure indexing strategy in accordance with the target allocations. The policy asset allocation is the primary driver of overall return.
2. **Short-Term Asset Allocation (STAA)** – The Short-Term Asset Allocation measures the incremental benefit of decisions to deviate from the target allocation. These decisions are usually the second most important driver of returns. An example would be to maintain, for a temporary period of time, an overweight to equities and an underweight in real estate versus the targets. The contribution of the STAA to the PR is computed as the difference between the benchmark returns using the portfolio's actual weights and the target allocations for each asset class. The goal of STAA contribution to return is to be zero or positive.
3. **Style Bias (SB)** – The Style Bias measures the incremental benefit of choosing investment styles within an asset class that deviate from the weightings in the asset class benchmark. An example would be if the portfolio weighting of small-cap equities differed from its weighting in the equity benchmark index. The contribution of the SB to the PR is computed as the difference between the benchmark returns using the portfolio actual allocation weights and the benchmark weights for each style within each asset class.
4. **Manager Selection (MS)** – Manager Selection measures the incremental benefit of selecting active managers that outperform their relevant benchmarks. It is calculated as the difference in returns between the each manager's actual performance and that of its benchmark or the difference between PR and the SB. Decisions related to manager selection should be positive to overall returns.

The Benchmarks to be used for performance measurement for the composite asset classes and managers will be determined from time-to-time by the Investment /Finance Committee. Such Benchmarks will be reviewed as necessary, and at least annually, by the Investment/Finance Committee to ensure that benchmarks are both current and appropriate.

### **Manager Review and Corrective Actions**

The Investment/Finance Committee, with the assistance of the investment consultant, will also periodically review the qualitative developments of each investment manager and/or product. This evaluation should include:

- Changes in the investment philosophy
- Changes in the organizational structure or financial condition (including any significant changes in total assets under management)
- Changes in key personnel
- Changes in the fee structure
- Advice from investment consultants who are retained by the Investment/Finance Committee and any other qualities that the Investment/Finance Committee deems appropriate.

This review should also include an assessment as to whether each investment manager has operated within the scope of this Policy. Investment manager(s) must disclose all major changes in organization or investment philosophy to the Investment/Finance Committee members within 30 days. Further, all registered investment advisors must present updated ADV-II forms on an annual basis to the Investment/Finance Committee.

Investment managers shall report not less than quarterly on the performance of the portfolio, including comparative gross returns for the funds and their respective benchmarks, as well as a complete accounting of all transactions involving the Endowment's investments during the quarter, together with a statement of beginning balance, fees, capital appreciation, income and ending balance for each account.

Corrective action should be taken by the Committee naturally as a result of the ongoing review process of both portfolio returns and all components of the contribution to returns. While there may be unusual occurrences at any time, the following are instances where corrective action may be in order:

1. Any organizational change that may materially affect the management process will be noted by the investment management and discussed with the Investment/Finance Committee. If the Investment/Finance Committee deems appropriate, the investment manager may be called upon to discuss changes.
2. Violation of terms of contract without prior approval for the Investment/Finance Committee constitutes grounds for termination.
3. As part of its overall asset allocation strategy, the Investment/Finance Committee will select managers with certain styles and approaches to portfolio diversification. Therefore, it is critical that managers adhere to the original intent of the Investment/Finance Committee. Should either the consultant or Investment/Finance Committee ascertain that significant changes in investment style have occurred, this may be grounds for termination.
4. Managers may be replaced at any time as part of an overall restructuring.

## **Asset Class Definitions**

The composite asset classes as defined in Section VI in the Policy are further defined to include the following and may include index funds and funds of funds as determined by the Committee:

### **I. Equity Investments**

#### **US Large, Mid, and Small Cap Equity**

Investments are primarily in stocks of large, medium, and small U.S. companies.

#### **International Equity – Developed Markets and Emerging Markets**

Investments are primarily in stocks of non-U.S. companies.

The specific portfolio allocation biases among large, mid and small cap US equities, as well as between developed and emerging international markets, will be determined by the investment committee from time-to-time, and will adhere to the broad policy ranges and targets.

### **II. Fixed Income**

Investments are fixed income securities, including U.S. and non-U.S. corporate bonds, government debt instruments (including Treasury Inflation-Protected Securities (TIPS)), and mortgage-backed issues. Exposures may include below-investment grade (“high yield”) and non-dollar denominated foreign strategies.

The specific portfolio allocation biases between US and non-US, investment grade and below-investment grade fixed income will be determined by the investment committee from time-to-time, and will adhere to the broad policy ranges and targets.

#### **Alternative Investments**

This class may include real estate, private equity, diversifying strategies, real return funds, or other investments the trustees deem appropriate.

#### **Real Estate & Real Assets**

Real estate may include public or private investments in physical properties, accessed through commingled funds, separate accounts, or direct investments. Common property types associated with real estate investing are apartments, office buildings, retail centers, and industrial parks. Domestic real estate investment portfolios generally own many geographically diverse properties across the United States. Real assets may be in similar inflation-protection minded strategies, and may include timber or commodities.

#### **Private Equity**

Investments include private equity such as venture capital and buyouts, as well as private debt and distressed/opportunistic strategies.

### **Diversifying Strategies**

Investments may include hedge fund and related strategies that seek positive returns in all market environments and/or returns non-correlated with the market. Strategies utilized may include (but are not restricted to) long-short, short-bias, equity market neutral, merger arbitrage, global macro, convertible arbitrage, commodity trading, distressed and special situations. Oftentimes fund managers may employ explicit or implicit leverage to achieve their desired investment strategy. Some specialty strategies may include structured notes, asset-backed securities, agency and non-agency mortgages, commodities, distressed debt, and real estate, as well as traditional equity and fixed income securities. Some managers in this group may employ a static strategy that is dedicated to a single asset type, while others attempt to add value by tactically allocating to various asset classes that they perceive to be undervalued during particular periods of time due to temporary market conditions or inefficiencies. The Diversifying Strategies underlying strategic allocations will be determined by the investment committee from time-to-time, and will adhere to the broad policy ranges and targets.

## **OTHER MATTERS**

### Guidelines for Active Investment Managers

- A. Proxy Voting: The investment manager(s) shall have the sole and exclusive right to vote any and all proxies solicited in connection with the portion of the securities held by the Endowment under their management. The investment manager(s) shall furnish the Investment/Finance Committee with a written proxy voting policy statement, and shall keep records with respect to its voting decisions and submit a report annually to the Investment/Finance Committee summarizing votes cast.
- B. Trading and Execution: The investment manager(s) shall use their best efforts to obtain execution of orders through responsible brokerage firms at the most favorable prices and competitive commission rates.