

# **UNIVERSITY OF KENTUCKY AND AFFILIATED CORPORATIONS**

## **ENDOWMENT INVESTMENT POLICY**

Amended December 2, 2025

**University of Kentucky  
University of Kentucky Research Foundation  
University of Kentucky Gluck Equine Research Foundation, Inc.  
University of Kentucky Humanities Foundation, Inc.  
University of Kentucky Mining Engineering Foundation, Inc.**

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## **I. General**

The University of Kentucky Endowment (“Endowment”) is an aggregation of funds comprised of gifts from donors and grants from the Commonwealth of Kentucky with the requirement they be invested in perpetuity to generate a reliable and steadily growing revenue stream to support the mission of the University now and in the future. The revenue stream, or total return spending distributions, supports scholarships, chairs, professorships, basic research, as well as academic and public service programs, as defined by the individual endowment agreements. The Endowment is expected to provide fiscal stability since the principal is invested for long-term growth and total return spending distributions are generated year after year.

The University of Kentucky has a fiduciary responsibility to prudently manage and preserve the long-term purchasing power of the Endowment, as well as the individual endowment funds, in order to evenly support present and future beneficiaries. This fiduciary responsibility constitutes both a legal and moral obligation to donors and the Commonwealth of Kentucky who intend that their gifts and grants provide support for the University in perpetuity.

The Endowment also includes other funds set aside by the Board of Trustees with the expectation that they be invested on a long-term basis.

## **II. Purpose of the Investment Policy**

In general, the purpose of this policy is to outline a philosophy that will guide the management of the investment assets toward the desired results. It is intended to be sufficiently specific to be meaningful, yet flexible enough to be practical.

This investment policy is set forth by the Investment Committee (“Committee”) of the University of Kentucky Board of Trustees in order to:

- a. Define and assign the responsibilities.
- b. Establish a clear understanding of the investment goals and objectives of the Endowment assets.
- c. Offer guidance and limitations regarding the investment of Endowment assets.
- d. Establish a basis of evaluating investment results.
- e. Manage the Endowment’s assets according to industry best practices and applicable laws.

The investment policy shall be formally reviewed annually and at such other times as desired by the Committee and Endowment investment staff. Any modifications to the policy shall be approved by the Committee.

### **III. Roles and Responsibilities**

#### **Responsibilities of the Investment Committee**

The Board of Trustees has established the Investment Committee with members appointed annually by the Chair of the Board of Trustees. The Committee is responsible for the review and oversight of the Endowment investments of the University of Kentucky and its affiliated corporations. As a standing committee of the Board, the Investment Committee must have at least five (5) Trustee members, including the Committee Chair under Governing Regulation II.G.5.

Governing Regulation II.G.5 of the University of Kentucky sets forth the specific responsibilities of the Investment Committee as follows:

This Committee is responsible for review and oversight of the endowment investment programs of the University and its affiliated corporations and entities. These responsibilities include: (1) formulating and reviewing investment policies; (2) appointing, monitoring and evaluating investment managers and consultants; and (3) reviewing and approving plans for the general management of the endowment funds of the University.

In addition to the five voting Trustees, this Committee may have up to five non-voting Community Advisory Members to aid it in its functions by providing specialized advice and support. The President, in consultation with the Board Chair, will appoint the Community Advisory Members. The Community Advisory Members will serve for a three-year term and may be reappointed.

#### **Responsibilities of Investment Staff and Endowment Advisory Group**

##### Investment Staff

The senior Endowment investment staff ("Staff") will consist of the University's Executive Vice President for Finance and Administration, Chief Investment Officer, and Investment Director. Staff is responsible for executing the policies and decisions enacted by the Committee and the general daily activities and administration of the Endowment assets. The Staff will prepare analysis and recommendations for the Committee on development of policies and guidelines, selection of an appropriate long-term asset allocation, and selecting an appropriate manager structure. The Staff will perform other duties as delegated by the Committee. The Staff will maintain summaries of the investment guidelines for the various investment managers and periodically provide to the

Committee.

#### Endowment Advisory Committee

An Endowment Advisory Committee of senior University administrators and faculty may be established by the President to advise the Executive Vice President for Finance and Administration and Staff on various matters pertaining to the prudent management of individual endowment funds.

#### **Responsibilities of Investment Consultant**

The Committee may engage an independent Investment Consultant (“Consultant”) to assist the Committee and Staff in developing policies and guidelines, selecting an appropriate long-term asset allocation, selecting an appropriate manager structure, identifying investment managers, evaluating investment performance, and offering other services as requested. The Consultant will prepare quarterly and annual assessments of investment performance that include results for the total endowment and each individual investment manager compared to appropriate market indices and manager universes. The Consultant will also periodically provide in-depth and detailed analysis of each manager's portfolio.

#### **Responsibilities of Investment Custodian**

The Committee will engage an Investment Custodian (“Custodian”) for the University's endowment investments. The Custodian will establish and maintain direct account relationships with each investment manager and perform core custodial functions, including security safekeeping, collection of income, processing and settlement of trades, collection of proceeds of maturing securities, distribution of income, and daily investment of cash. The Custodian will provide account statements and other reports as requested by the Staff.

## **IV. Delegation of Authority**

The Committee delegates the following investment related activities.

#### **Hiring of Investment Managers**

In collaboration with the Consultant, the Staff will appoint, monitor and evaluate external investment managers for the investment asset allocation and strategies approved by the Committee. The Staff and Consultant will provide updates to the Committee on manager appointments, terminations, and the ongoing monitoring and evaluation of existing managers at each meeting and at other times as requested by the Committee. Investment staff may implement temporary investments as needed due to investment manager, strategy, or portfolio structure

changes. Investment managers intended to have a long-term role in the portfolio will be selected utilizing an alternative search process approved by the Chief Procurement Officer, as described in the memorandum included in Appendix 1.

### **Management of Endowment Assets**

Each individual investment manager will exercise discretion over the securities or assets in accordance with specified investment guidelines. Investment managers that utilize separate accounts to manage Endowment assets will adhere to specific investment manager guidelines established by Staff with the assistance of the Consultant. Investment managers that utilize commingled fund structures will have discretion to manage the assets in accordance with the policies and guidelines outlined in the respective fund governing documents.

## **V. Financial and Investment Objectives**

The Investment Committee has established the following financial and investment objectives for the Endowment:

1. To preserve the long-term purchasing power of the endowment assets and the related revenue stream over time to evenly allocate support between current and future beneficiaries (intergenerational equity).
2. To earn an average annual return, after expenses, of at least 7.5% per year over full economic market cycles.

### **Kentucky Uniform Prudent Management of Institutional Funds Act (KRS 273.600 to 273.645)**

Endowment assets will be managed by the Investment Committee in accordance with the provisions of the Kentucky Uniform Prudent Management of Institutional Funds Act (KRS 273.600 to 273.645), included in Appendix 2.

### **Spending Distribution Policy**

The Investment Committee has established a “hybrid” spending distribution policy, which includes both the market value of the endowment and the level of inflation in determining the spending distribution each year. The annual spending distribution will be calculated by taking a weighted average comprising 60 percent of the prior year’s spending distribution, adjusted for inflation<sup>1</sup>, and 40% of the amount that results when the target annual spending distribution rate

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<sup>1</sup> Inflation will be measured by the U.S. Department of Labor Bureau of Labor Statistics Consumer Price Index for All Urban Consumers (CPI-U).

of 4.0% is applied to the average market value of the Endowment over the preceding 36 months. The spending distribution amount determined by the formula will be constrained so that the calculated rate is at least 3.5%, and not more than 5%, of the current Endowment market value. The hybrid spending distribution formula is depicted below:

$$\begin{aligned} & 60\% * (\text{Prior Year Spending Distribution} * [1 + \text{Annual Percent Change in CPI-U}]) \\ + & 40\% * (4\% * \text{Average Market Value for Preceding 36 Months}) \end{aligned}$$

Note: the calculated spending distribution rate must fall between 3.5% and 5% of the current market value of the Endowment.

### **Management Fee**

Eligible endowments will be assessed an annual management fee of 1.00% of the current market value (assessed monthly) to support administrative costs.

### **Underwater Endowment Funds<sup>2</sup>**

The target spending distribution rate and management fee established by the Investment Committee represent maximum amounts that can be withdrawn annually from individual endowment funds. The Treasurer may reduce or suspend withdrawals from individual endowment funds that are underwater.

Spending distributions and management fee withdrawals will be suspended on all endowments underwater by more than 20%. Endowments underwater more than 10% will undergo a formal review by University Financial Services and appropriate College Dean to determine the appropriate level of spending distributions in accordance with the following factors set forth in the Kentucky Uniform Prudent Management of Institutional Funds Act:

- the duration and preservation of the endowment fund;
- the purposes of the institution and the endowment fund;
- general economic conditions;
- the possible effect of inflation or deflation;
- the expected total return from income and the appreciation of investments;
- other resources of the institution;
- the investment policy of the institution.

The Treasurer has authority to approve exceptions of the policy to suspend spending distributions and management fee withdrawals on certain quasi and term endowments that are underwater by more than 20%.

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<sup>2</sup> Underwater endowments are those in which the market value is less than the contributed value.

### New Endowment Funds

Spending distributions on new endowment funds will be delayed for at least one year in order to build a reserve for future spending distributions.

## VI. Investment Policies

### Diversification

Disciplined management of the asset allocation is necessary and desirable. Diversification of investments among assets that are not similarly affected by economic, political, or social developments is highly desirable. The general policy shall be to diversify investments so as to provide a balance that will enhance total return, while avoiding undue risk concentrations in any single asset or investment category.

### Asset Allocation

To ensure broad diversification, the asset allocation will be set with the following target percentages and within the following ranges:

<b><u>ASSET CATEGORY</u></b>	<b><u>TARGET</u></b>	<b><u>RANGE</u></b>
<b>GLOBAL EQUITY</b>	<b>64%</b>	<b>40 – 75%</b>
<i>Public</i>	40	
<i>Private</i>	24	
<b>FIXED INCOME</b>	<b>12</b>	<b>5 - 25</b>
<i>Public Fixed Income</i>	10	
<i>Private Credit</i>	2	
<b>REAL ASSETS</b>	<b>12</b>	<b>5 - 20</b>
<i>Public</i>	3	
<i>Private</i>	9	
<b>DIVERSIFYING STRATEGIES</b>	<b>12</b>	<b>5 - 20</b>

*Note: Sub-asset category (e.g., Public Equity) figures reflect working targets. Investment staff has flexibility to adjust sub-asset category exposures within broader, asset category (e.g., Global Equity) ranges, based on market conditions and ongoing research.*

*Global Equity* – The allocation will consist of public and private equity-oriented funds managed by external investment firms. This is expected to be the highest risk, highest return asset category of the four, and the primary driver of portfolio growth over time. The allocation will be diversified by factors including security, sector, geography, market capitalization, and manager style. Private equity investments will be made with the expectation that long-term returns materially exceed those of the public markets.

*Fixed Income* –The allocation will consist of obligations of sovereign nations and corporations,



mortgage- and asset-backed securities, money market instruments, and bank deposits. The allocation will consist of two broad categories: 1) public fixed income and 2) private credit. The primary role of the public fixed income portfolio is to provide a partial hedge in the event of economic contraction, deflation, and/or severe flight to quality. It is expected that this portion of the portfolio would serve as one of the primary sources of spending during such periods, when the prices of other assets in the Portfolio may decline. Therefore, while the public fixed income allocation may include some investments rated below investment-grade, it is generally expected to have a high quality rating on average (typically “A” or better by a recognized bond rating agency). The private credit allocation may include obligations of any credit quality and is expected to generate long-term returns that materially exceed those of the public credit markets.

*Real Assets* – The allocation will consist of public and private assets. Public real assets may include Real Estate Investment Trusts (REITs), Master Limited Partnerships (MLPs), natural resource equities, commodities, and Treasury Inflation-Protected Securities (TIPS). Private real assets may include real estate, natural resources, and infrastructure. Private real assets are expected to generate long-term returns that materially exceed those of public real asset alternatives. Private assets may include real estate near the University campus which is deemed to have strategic value for the University. For diversification purposes not more than 2% of the portfolio will be invested in local real estate as opposed to external managers. The 2% maximum will be defined as the market value of the portfolio at the time of investment. All real assets are expected to provide inflation protection as well as generate positive real rates of return.

*Diversifying Strategies* – The allocation will consist of a diverse group of managers and strategies with a goal of earning positive returns over time, but with low sensitivity to the public equity markets. Included in this category are strategies such as long/short equity, low beta equity, event-driven and special situations investing, merger and capital structure arbitrage, quantitative strategies, global macro, long/short credit, and distressed securities. The beta (sensitivity to equity markets) of the diversifying strategies allocation is generally expected to fall between 0.25 and 0.35 when measured over a multi-year period. The diversifying strategies portfolio is expected to generate a long-term return greater than a passive blend of equities and fixed income with a commensurate risk profile. Returns should generally be better than equities when equity markets fall significantly, and behind equities when equity markets rise significantly.

## **Rebalancing**

Rebalancing is a term that describes the periodic movement of funds from one asset class or category to another for the purpose of realigning the assets with the asset allocation target. A rebalancing strategy is an important element of asset allocation policy. Systematic rebalancing will ensure that the portfolio’s risk profile remains consistent with this investment policy. However, excessively tight ranges and frequent rebalancing can lead to unnecessary transaction costs.

The Committee has chosen to adopt a rebalancing policy that is governed by allocation ranges rather than time periods. The ranges, specified in the table above, are a function of the volatility and liquidity of each asset class and the proportion of the total fund allocated to the asset category. While the allocation to all asset categories remains within these limits, Staff will first use cash flows, as available, to prudently manage allocations relative to the target. When an asset category violates the lower or upper limits, public market funds will be actively rebalanced back to the target.

When any one of the public market asset categories hits a trigger point, the entire fund may be rebalanced back to asset category target allocations with the understanding that it may be impractical to return the private asset categories precisely to target in the short term. Accordingly, qualitative considerations (e.g., transaction costs, liquidity needs, investment time horizons, etc.) will be considered in determining the potential timing and extent of rebalancing.

Staff is responsible for developing and implementing a rebalancing plan that is appropriate for existing market conditions, with a primary objective of minimizing transaction costs and portfolio disruptions. In the event an allocation trigger point is not reached, Staff may still make minor changes among asset categories and within individual asset categories, as needed, to more effectively implement the program and to maintain proper exposure to the approved asset allocation and asset category portfolio structures. Staff will report the results of all rebalancing activity to the Investment Committee at the regular meetings.

### **Liquidity**

The Endowment is intended to provide a reliable and steadily growing revenue stream to support the mission of the University in perpetuity. As a result, the Endowment has a long-term orientation. In addition, the withdrawal rate from the Endowment fund is well defined, predictable, and of modest size relative to the total assets. Staff, assisted by the Consultant, is responsible for managing the liquidity of the portfolio to fund spending distributions and capital calls while maintaining the appropriate market exposure.

Certain appropriate investment options, particularly in alternative asset classes, involve fund structures with liquidity constraints that align with less liquid portfolio holdings. The tradeoff between return opportunities and liquidity will be considered throughout the portfolio construction process.

Sufficient liquidity should be maintained to fulfill the spending distributions and operating objectives of the Pool. Portfolio liquidity will be monitored using a three-tier system:

Liquid: available within 90 days

Semi-liquid: available in 90 days or more but less than 2 years

Illiquid: available only in 2 years or more

<u>Classification of Asset</u>	<u>Guideline</u>
Liquid	no less than 35%
Combined: Semi-liquid & Illiquid	no more than 65%
Illiquid	no more than 45%

New commitments will be made to illiquid/private capital investments with the intent to keep current market value of liquid holdings above 35% of the total Fund. Illiquid percentages will be calculated based on current market value. Staff, assisted by the Consultant, will complete annual forecasting and make appropriate commitments to reach and maintain the approved policy allocation and liquidity while ensuring diversification across vintage year, strategy, geography, etc.

It is recognized that significant changes in investment market values could cause the portfolio to be positioned outside of these guidelines. If this occurs, Staff will communicate this to the Investment Committee and develop a plan to reposition the portfolio consistent with these guidelines over a reasonable time frame.

### **Proxy Voting**

The Committee delegates full authority for proxy voting to its investment managers for the securities under their discretionary authority and requires the investment managers to vote all proxies in the best interest of the Endowment. In addition, when requested, the managers will report to the Committee on their proxy-voting policies and activities on the Endowment's behalf.

Proxy voting related to governance issues regarding investment managers hired to manage Endowment assets, and their related investment legal structures, terms and conditions, will be voted on by the Staff in the best economic interest of the Endowment. The Staff may solicit assistance of the Consultant on governance issues.

### **Transaction Costs**

The Committee requires the investment managers, in their capacity as fiduciaries, to manage the transactions costs they incur on the Endowment's behalf in the best interests of the University. When requested, the managers will report to the Committee on the transactions costs incurred and the brokers used on the Endowment's behalf.

### **Transition Management**

Transitions between investment managers are an important and inevitable element of portfolio management, typically resulting from manager terminations or changes to the investment strategy of the portfolio. The optimal method to use in executing a transition may vary significantly from one transition to another based on the types of assets involved and the timeframe in question. Generally, the Endowment's objective in a manager transition is to

implement the change in a cost-effective, timely manner while maintaining the appropriate market exposure. It is imperative to note that the cost of transition is not commissions alone, but also bid/ask spread, market impact and opportunity cost. The market impact cost is the effect trading will have on the market price of the shares being traded. The opportunity cost, sometimes referred to as implementation shortfall, is the cost of market movements over the time it takes to trade. Efforts should be made to minimize the total cost rather than any single cost component. Selecting a transition manager can be done at the Staff's discretion with the assistance of the Consultant. Use of futures contracts and exchange traded funds may be required in order to maintain appropriate market exposure during a transition.

## VII. Performance Evaluation

Endowment performance will be monitored and reviewed over short and long-term time periods, with an emphasis on longer-term periods in order to include full market cycles and reflect the endowment's long-term investment strategy. Performance will be evaluated at three levels; total Endowment, asset class and individual manager. All three levels will include a market index and peer group measurement review. Performance will be reviewed on a gross and net return basis and will include risk metrics and risk-adjusted returns.

### Performance Benchmarks

The total Endowment performance will be measured against two principal benchmarks:

1. The primary performance objective of achieving a long-term total return, net of fees and expenses, of at least 7.5%. It is expected that portfolio performance will vary significantly from this benchmark over shorter periods. Therefore, performance compared to this benchmark will be evaluated only over very long periods (ten years or more).
2. A Policy Benchmark consisting of market indexes reflecting the Endowment's "strategic target" asset allocation percentages. Performance compared to this benchmark will be evaluated over rolling three- to five-year periods. The current Policy Benchmark appears in the following table:

<b><u>ASSET CATEGORY</u></b>	<b><u>TARGET</u></b>	<b><u>INDEX</u></b>
<b>GLOBAL EQUITY</b>	<b>64%</b>	
Public	40	MSCI All Country World IMI Index (ACWI IMI)
Private	24	Cambridge Associates (CA) Private Equity and

Venture Capital indices [1] [2]		
<b>FIXED INCOME</b>	<b>12%</b>	
Public Fixed Income	10	Barclays Aggregate Bond Index
Private Credit	2	Cambridge Associates Private Credit Index [1] [3]
<b>REAL ASSETS</b>	<b>12%</b>	
Public	3	1/3 each Bloomberg Barclays U.S. TIPS Index, NAREIT Index and Alerian Midstream Energy Index
Private	9	CA Private Real Estate, Natural Resources, and Infrastructure indices [1]
<b>DIVERSIFYING STRATEGIES</b>	<b>12%</b>	<b>25% MSCI ACWI IMI / 75% BBG Short-Term Govt/Corp Index</b>

[1] Cambridge Associates Private Benchmarks will be weighted based on the actual exposures of the underlying private investment asset classes for each respective allocation.

[2] PE / VC Indices contain the following sub-asset classes: Buyouts, Growth Equity, Venture Capital, and Distressed Securities (Credit Opportunities / Control Oriented Distressed).

[3] Private Credit indices contain the following sub-asset classes: Credit Opportunities, Subordinated Capital, and Senior Debt.

In addition to these principal benchmarks, performance may from time-to-time be compared to a peer group of similar institutions.

The asset class performance will be measured against:

1. The asset class' index.
2. A peer group universe of similar asset classes.

The individual manager performance will be measured against:

1. The manager's specific market indexes.
2. A peer group universe of similar investment styles.

#### **Long-Only Active Managers**

Managers will be measured against their primary benchmark and their peer universe.

#### **Long/Short Managers (Hedge Funds)**

Managers will be measured against their primary benchmark. Secondary benchmarks will also be used, including relevant asset class benchmarks and absolute return measures (T-bills + X%).

#### **Private Capital Managers**

The majority of private equity, private real asset, and private credit funds will be invested with

private partnerships. These partnerships typically range from 7-15 years in life, during which time the Fund may not be able to sell the investment. Additionally, the partnership may not produce meaningful returns for 3-5 years (depending on the strategy). New investments will create a drag on fund performance in the early years (3-5 years) until these investments begin to mature. This drag on performance is often referred to as the J-curve, due to the shape created by plotting a line graph with performance on the y-axis and time on the x-axis. Private, illiquid manager performance will be measured utilizing internal rate of return (IRR) calculations, and Multiple of Invested Capital (MOIC), and will be compared to an appropriate peer group. An IRR calculated from the inception of the partnership will be the primary performance measurement tool utilized for all private capital managers. Performance will be measured relative to the best available benchmark, understanding that some investments may not have entirely comparable indices.

### **Performance Expectations**

It is expected that, at each level, the Endowment, the asset class, and the individual active managers should exceed the index return and should be above median against the appropriate peer group universes over full market cycles. It is expected that risk (and risk adjusted returns) will be in line with the risk associated with the specific market benchmarks over full market cycles.

## **APPENDIX 1**

### **Memorandum Regarding Selection of Investment Managers**



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December 13, 2021

To: Todd Shupp, Chief Investment Officer

From: Barry Swanson, Chief Procurement Officer 


Re: Selection of Investment Managers

Pursuant to KRS 45A.095 (I), and for the reasons detailed in the attached Opinion of General Counsel# 2016-02, I have determined that selection of investment managers for the investment of the University's endowment funds is not feasible to bid using the formal competitive negotiation process set forth in KRS 45A.085. Therefore, the University's investment staff may utilize the alternative process described in the attached Opinion.



## MEMORANDUM

TO: University of Kentucky Board of Trustees Investment Committee

FROM: William E. Thro, General Counsel 

DATE: November 29, 2021

RE: Update of *Opinion of General Counsel 2016-02*

At the request of Chief Investment Officer Todd Shupp, I have reviewed *Opinion of General Counsel 2016-02, Use of Alternative Competitive Negotiation Approach for the Selection of Investment Managers* ("2016 OGC") to determine if any updates are necessary following the Investment Committee's 2021 hiring of Cambridge Associates to replace FEG as the fiduciary investment consultant to the University of Kentucky and its Investment Committee.

The 2016 OGC's discussion of FEG's role primarily focuses on the process by which the University chose its investment consultant, and not the ultimate identity of the consultant:

This new process places enhanced emphasis on the integrity, quality, and depth of the investment consultant's research capabilities. The University recently completed a competitive, in-depth formal RFP search process to identify a new investment consultant with strong capabilities across several areas, including manager research. In reviewing responses to this RFP, the Evaluation Committee thoroughly vetted each firm and its capabilities. This included a review of the firm's manager search processes, its code of ethics and approach to mitigating potential conflicts of interest. The firm selected . . . has agreed to serve as a fiduciary of the University and work in the University's best interest when conducting all business, and will do so on a flat fee consulting basis. The firm has deep research capabilities, particularly in alternative strategies, and they have been very transparent regarding their manager search process.

The University selected Cambridge Associates in 2021 using the same in-depth formal RFP search process to hire a firm with similarly deep research capabilities and transparency around their manager search processes. Cambridge Associates also

seeblue.

will serve as a fiduciary of the University. Other than the switch to a new consultant, the investment manager process described more fully in the attached 2016 OGC, which has been utilized successfully numerous times over the last five years, remains the same.

After confirming the process remains the same and reviewing the relevant statutes and court decisions for any updates, my ultimate conclusion, as expressed in the 2016 OGC, remains unchanged. Because the University has determined that it is not feasible to bid external investment manager services through the formal RFP process, the University may legally use the alternative selection process described in the 2016 OGC, involving current University investment staff and the current fiduciary investment consultant, as the method most advantageous to the University's ability to fulfill its mission. The process utilizes most key competitive negotiation objectives promoted by the Model Procurement Code, including cost, transparency, avoidance of conflicts of interest, and the overriding principle to achieve the best value.

If you have any questions, please contact me or Shannan Stamper, Deputy General Counsel for Finance & Administration.

**Opinion of General Counsel  
Opinion # 2016-02**

**Use of Alternative Competitive Negotiation  
Approach for the Selection of Investment Managers**

**INTRODUCTION**

The University uses external investment managers for investment of the University's Endowment funds across multiple investment classes. The University previously attempted to hire these investment managers through the Purchasing Division's formal Request for Proposal process. The University's senior financial leadership has proposed that the University select future investment managers utilizing an alternative competitive negotiation process to obtain the most advantageous opportunities providing best value to the University by utilizing the manager research capabilities of the University's investment consultant. Some members of the Board of Trustees' Investment Committee have expressed a concern that use of the alternative competitive negotiation process may violate state law. In response, the University's senior financial leadership has requested a formal Opinion of the General Counsel on the question.

**QUESTION PRESENTED:** Does Kentucky law allow the University to utilize this new competitive negotiation approach outside of the traditional formal RFP processes?

**see blue.**

**SUMMARY ANSWER:** Yes. As described in further detail below, because the University has determined that it is not feasible to bid external investment manager services through the formal RFP process, the University may legally shift to this alternative selection process as the method most advantageous to the University's ability to fulfill its mission. The new process will still utilize most key competitive negotiation objectives promoted by the Model Procurement Code, including cost, transparency, avoidance of conflicts of interest, and the overriding principle to achieve the best value.

## **I. BACKGROUND**

### **A. The University Endowment and Role of Investment Managers**

The University Endowment is an aggregation of funds comprised of gifts from donors and grants from the Commonwealth of Kentucky with the requirement they be invested in perpetuity to generate a reliable and steadily growing income stream, to support the mission of the University now and in the future. The revenue stream or total return spending distributions, supports scholarships, chairs, professorships, basic research, as well as academic and public service programs, as defined by the individual endowment agreements. The Endowment is expected to provide fiscal stability since the principal is invested for long-term growth and total return spending distributions are generated year after year. The Endowment also includes other funds set aside by the Board of Trustees with the expectation that the Board will invest the funds on a long-term basis.

The University has a fiduciary responsibility to prudently manage and preserve the long-term purchasing power of the Endowment, as well as the individual endowment funds, in order to support present and future beneficiaries. This fiduciary responsibility constitutes both a legal and moral obligation to donors and the Commonwealth of Kentucky who intend that their gifts and grants provide support for the University in perpetuity.

The Board of Trustees has established the Investment Committee with members appointed annually by the Chair of the Board of Trustees to be responsible for the review and oversight of the Endowment. Governing Regulation II.E(2)(e)<sup>1</sup> of the University of Kentucky sets forth the specific responsibilities of the Investment Committee, including “(a) formulating and reviewing investment policies; (b) appointing, monitoring and evaluating investment managers and consultants; and (c) reviewing and approving plans for the general management of the endowment funds of the University.”

In compliance with its duties, the Investment Committee has set forth the investment policies in an Endowment Investment Policy, last amended June 18, 2015 (“Policy”).<sup>2</sup> That Policy provides for the selection of investment managers by University senior financial management under the following guidelines:

In collaboration with the Consultant, the Staff will appoint, monitor, and evaluate external investment managers for the investment asset allocation and strategies approved by the Committee. The Staff and Consultant will provide updates to the Committee on manager

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<sup>1</sup> <http://www.uky.edu/regs/files/gr/gr2.pdf>

<sup>2</sup> <https://www.uky.edu/EVPFA/Controller/files/endow/POLICY.pdf>

appointments, terminations, and the ongoing monitoring and evaluation of existing managers, at each meeting and at other times as requested by the Committee.

Each individual investment manager will exercise discretion over the securities or assets in accordance with specified investment guidelines.

Investment managers that utilize separate accounts to manage Endowment assets will adhere to specific investment manager guidelines established by Staff with the assistance of the Consultant. Each investment manager using a separate account is required to summarize its holdings and transactions on a monthly basis.

Investment managers that utilize a mutual fund investment structure, a commingled trust fund structure or a limited partnership structure will have discretion to manage the assets in accordance with the policies and guidelines outlined in the respective mutual fund's prospectus; the commingled trust fund's offering memorandum or limited partnership's private placement memorandum.

*Policy* at 6. Under the Endowment Policy, the investment managers are required to act as fiduciaries of the University and must manage the transaction costs they incur on the Endowment's behalf in the best interests of the University. *Policy* at 11. These transaction costs or fees are charged to the Endowment income stream.

## **B. Kentucky Model Procurement Code**

The General Assembly adopted Kentucky Model Procurement Code in 1978, effective January 1, 1979.<sup>3</sup> Codified at KRS Chapter 45A, the Model Procurement Code has the following purposes:

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<sup>3</sup> The legislation was based on a model procurement code authored by the American Bar Association. Kentucky was among the first states to adopt it, and kept the word "Model" in the legislation's title. *See* KRS 45A.005 (title).

- (a) To simplify, clarify, and modernize the law governing purchasing by the Commonwealth;
- (b) To permit the continued development of purchasing policies and practices;
- (c) To make as consistent as possible the purchasing laws among the various states;
- (d) To provide for increased public confidence in the procedures followed in public procurement;
- (e) To insure the fair and equitable treatment of all persons who deal with the procurement system of the Commonwealth;
- (f) To provide increased economy in state procurement activities by fostering effective competition; and
- (g) To provide safeguards for the maintenance of a procurement system of quality and integrity.

KRS 45A.010. The Model Procurement Code applies "to every expenditure of public funds by this Commonwealth under any contract or like business agreement." KRS 45A.020(1). Key facets of the Model Procurement Code include public advertisement of a request for bid or proposal for at least seven (7) days, and the following methods of soliciting contract vendors: (1) competitive sealed bidding, by which the public agency solicits bids with no negotiation and awards the contract to the lowest, responsible and responsive bidder; (2) competitive negotiation, by which the public agency solicits proposals emphasizing other factors alongside price, and negotiates with one or more responsive bidders before awarding the contract; and (3) non-competitive negotiations, by which a public agency may award a contract in a situation where there is only one known capable supplier of a commodity or service, or when competition is not feasible. *See* KRS 45A.080 (competitive sealed bidding); KRS 45A.085 (competitive negotiation); KRS 45A.095 (noncompetitive negotiation). Personal service contracts are exempt from competitive sealed bidding under KRS 45A.095(g).

The University has traditionally used competitive negotiation under KRS 45A.085 to select its investment managers. Among the requirements for this process are “adequate public notice,” KRS 45A.085(2), and that the award “be made to the responsible offeror whose proposal is determined in writing to be the *most advantageous* to the [University].” KRS 45A.085(6) (emphasis added).

### **C. The Formal RFP Process and Its limitations**

KRS 164A.630(1)(b) requires the University to follow the Model Procurement Code. University contracts are requisitioned through the University’s Purchasing Division, whose procedure for solicitation is set forth in the University’s Business Procedures Manual.

Currently, when the University’s investment staff determines that a new investment manager is needed to implement the strategies set forth in the Investment Policy, the staff contacts the Purchasing Division. The Purchasing Division then compiles a Request for Proposal with the assistance and input from the investment staff.

In order to streamline its own processes, the Purchasing Division always incorporates the University’s standard and general terms and conditions into the RFP. These general terms and conditions necessarily cover a broad range of anticipated services or contract needs. Not every standard term or condition will be germane to the service or product solicited.

The RFP is then publicly advertised on the Purchasing Division’s website for



three to four weeks. Potential responsive bidders are required to note any objections or exceptions to the terms and conditions of the Request (including the standard and general terms and conditions) in their responses.

Once the deadline for responses passes, the Purchasing Division includes the investment staff as part of a committee to review the responses received. The committee may choose certain respondents to come to the University to make a presentation.

Once the committee makes a recommended selection, the Purchasing Division, with input from the Office of Legal Counsel, works on completing a contract with the selected manager. In other purchasing areas, this may simply involve issuing a standard "Notice of Price Contract Award" that incorporates the Request for Proposal and the vendor's response into a final contract.

In the investment management area, however, the selected managers often have their own legal agreements that require review by the University, depending on the nature of the investment. Such agreements may include subscription agreements or partnership agreements. Many investment options involve agreements that cannot be altered due to federal securities law or other factors such as number of other investors. While many managers are open to reconciling a few discrete concerns through what is known as a "side letter," reconciling these agreements with the formal RFP document has taken considerable time and effort on the part of all University staff involved. Moreover, the time spent completing this entire process is lengthy.

The University's senior financial management has identified the following key constraints of using the formal RFP process for the selection of investment managers:

Time: Within the current formal RFP process, once the investment office decides to conduct a manager search, it typically takes three to six months to create the RFP, await responses, review proposals, and select a finalist.<sup>4</sup> Many investment opportunities arise and require action more quickly than is feasible in this timeline, and investment staff have determined that the University is missing out on this source of potential return. Forward-looking return forecasts across asset classes are relatively low in the current market environment, and investment staff have determined that the University needs to have an increased ability to make active, tactical investment decisions that are not possible under the University's traditional procurement process.<sup>5</sup>

Constrained Universe: Based on the investment staff's experience, the formal RFP structure limits the universe of available managers, since many smaller and/or highly successful firms do not seek investors with the University's process requirement. These managers often have limited capacity for new investors and therefore do not pursue investments from clients with additional, operational requirements related to formal RFP's, though many will otherwise work with investors to address specific investor requests related to an investor's public status through the use of "side letters." While the investment staff cannot precisely quantify how large of a return opportunity the University is missing due to managers choosing not to participate in

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<sup>4</sup> A key portion of the delay is due to the time the RFP is publicly advertised on the University's website. Although the Model Procurement Code requires an advertisement period of only seven (7) days, the Purchasing Division typically recommends a longer posting and response period for requests that will involve complex matters or proposals. Because any exceptions to an RFP must be noted in an offeror's initial response, much of the time necessary for an investment manager to prepare a response to a formal RFP involve making exceptions to the University's general terms and conditions.

<sup>5</sup> The Endowment Policy tasks the University's investment staff with, among other tasks, rebalancing Endowment assets when certain asset classes hit a trigger point and with developing a rebalancing plan appropriate for existing market conditions. Time delays due to the formal RFP process could potentially disrupt this rebalancing.

the current structure, they are confident that missed opportunities exist.

Cost: The University's portfolio contains substantial exposure to alternative investment managers. The University has implemented the majority of these investments in fund of fund structures, since building a diversified portfolio of direct, alternatives managers using a RFP structure is not practical. Fund of fund structures have been used largely because they are simpler and faster to implement via formal RFP, but these vehicles are materially more expensive than a direct investment program. Higher fees result in lower net of fees performance and reduce the value of the endowment portfolio.

#### **D. Proposed New Investment Manager Search Process**

Given the challenges identified above, University senior financial management have recommended an alternative approach to selecting managers that directly engages the research capabilities of its investment consultant. Instead of the Purchasing Division issuing a formal RFP for each manager search, they propose having the University's investment consultant provide investment staff with a search document that includes detailed information on their recommended, fully-vetted and approved managers in a given asset class. Investment staff would then conduct an in-depth review of these search candidates and work with the consultant's research staff to select the most appropriate managers for finalist consideration. At this stage, the manager selection process would closely resemble the finalist review process in the current formal RFP structure, thus retaining an essential competitive negotiation feature of the formal procurement process. Investment staff would conduct additional due diligence via conference calls and/or meetings to gain more familiarity with each firm and ask targeted questions to assist in making the manager selection, including request for a best and final offer

and negotiation of fee terms. The objective of the search process will be to select the firm that offers the best value for the University and whose proposal is the most advantageous to the University's ability to fulfill its mission.

At the conclusion of the search process, senior financial leadership would negotiate and execute the required contractual documents, in consultation with the Office of Legal Counsel.

This new process places enhanced emphasis on the integrity, quality, and depth of the investment consultant's research capabilities. The University recently completed a competitive, in-depth formal RFP search process to identify a new investment consultant with strong capabilities across several areas, including manager research. In reviewing responses to this RFP, the Evaluation Committee thoroughly vetted each firm and its capabilities. This included a review of the firm's manager search processes, its code of ethics and approach to mitigating potential conflicts of interest. The firm selected, Fund Evaluation Group ("FEG"), has agreed to serve as a fiduciary of the University and work in the University's best interest when conducting all business, and will do so on a flat fee consulting basis. The firm has deep research capabilities, particularly in alternative strategies, and they have been very transparent regarding their manager search process. FEG has also demonstrated its ability to help the University save several thousands of dollars in fees in the alternative portfolio by utilizing their research on direct funds and investing through a nondiscretionary fund-of-one legal entity FEG will form on our behalf to facilitate execution of contractual documents.

This process also requires active, ongoing oversight and participation by University investment staff, which over the past eighteen (18) months has enhanced its capabilities by hiring a Chief Investment Officer, Investment Operations Analyst, and an Investment Intern. Further expansion is expected, and plans include the addition of a full-time Investment Analyst. Given this enhanced capacity to focus on the endowment investment portfolio, the University is prepared to take a more active role in manager due diligence.

Investment staff will conduct periodic reviews of the consulting firm and its staff. This will include onsite meetings at FEG's headquarters to meet with senior research team leaders and a review of any changes to staff or processes. The investment office will also review the firm's ADV filings, particularly disclosures in Parts 2A and 2B that provide updates on any regulatory issues and material changes affecting the firm.

This new process is intended and designed to remain transparent and competitive, and the investment office will continue its existing process of providing a report on investment manager searches, hires, and terminations at each Investment Committee meeting.

### **III. LEGAL ANALYSIS**

The analysis of whether the proposed new process is permissible under Kentucky statutes governing university procurement and financial management begins—and ends—with the statutory text. As the Supreme Court of Kentucky recently explained:

It must be clear at the outset that the first rule of statutory interpretation is that the text of the statute is supreme. Upon review, “the words of the text are of paramount concern, and what they convey, in their context, is what the text means.” In determining what the text means, words will be presumed to be understood in their ordinary meanings, unless context mandates otherwise. But most significantly, we will not construe a meaning that the text of the statute cannot bear.

*Owen v. University of Kentucky*, 2016 WL 2604779 at 3 (Ky. 2016). “Where a statute is plain and unambiguous on its face, we are not at liberty to construe the language otherwise, *even though such a construction may be more consistent with the statute's legislative purpose.*” *Pennyrite Allied Cmty. Servs., Inc. v. Rogers*, 459 S.W.3d 339, 343 (Ky. 2015) (emphasis added). “It is not for [the courts] to rewrite the statute so that it covers only what we think is necessary to achieve what we think [the legislature] really intended.” *Lewis v. City of Chicago*, 560 U.S. 205, 215 (2010). Thus, “it is ultimately the provisions of our laws rather than the principal concerns of our legislators by which we are governed.” *Oncale v. Sundowner Offshore Servs., Inc.*, 523 U.S. 75, 79 (1998). Consequently, the courts cannot “displace the legislature's judgment for our own.” *Owen*, 2016 WL 2604779 at 5.

In determining whether the statutes—as written—allow the University to utilize the proposed process, the analysis must focus on three issues: (1) the authority of the University to manage its own Endowment; (2) the application of the Model Procurement Code to Investment Manager Contracts; and (3) assuming the Model Procurement Code does apply to Investment Manager Contracts, is the proposed process consistent with the Model Procurement Code. Each of these issues is addressed below.

**A. University Has the Authority to Manage Its Own Endowment**

The post-secondary institution financial self-management statutes, KRS 164A.550 through 164A.630 (“financial self-management statutes”), allow the state’s universities to elect to exercise all or some of a variety of financial self-management powers granted under the legislation, including the power to “receive deposit, collect, retain, invest, disburse and account for all funds received or due from any source.” KRS 164A.560(2). The University has exercised its option to exercise all powers available to it under these statutes. *See* 765 KAR 1:010.<sup>6</sup>

**B. Application of the Model Procurement Code to the Investment Manager Contracts**

Upon the University’s election to exercise powers under the financial self-management statutes, KRS 164A.630(1)(b) requires the University to be bound by the Kentucky Model Procurement Code in carrying out those powers. As noted above, the Model Procurement Code applies “to every expenditure of public funds by this Commonwealth under any contract or like business agreement.”<sup>7</sup> KRS

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<sup>6</sup> Even if the University had not made this election, other applicable statutes grant the University control of “private funds or contributions” made to the University. *See* KRS 41.290 (requiring every state agency to remit private contributions to the State Treasury, except for “private funds or contributions made and available to the governing board of the state supported institutions of higher learning.”).

<sup>7</sup> However, the Model Procurement Code does not automatically apply to use of state funds by localities that have not adopted the Code. *Laurel Const. Co., Inc. v. Paintsville Utility Comm’n*, 336 S.W.3d 903 (Ky. App. 2010) (holding that Model Procurement Code did not apply to Utility Commission’s award of contract to build water tower using funds from a Kentucky Infrastructure Authority grant that required the Commission to perform “consistent with” KRS Chapter 45A).

45A.020(1). Though there is some ambiguity as to whether the Model Procurement Code would apply to an endowment made up entirely of privately donated funds,<sup>8</sup> the Model Procurement Code applies to expenditures of Endowment funds used to pay investment managers because the Endowment includes “public funds.”

**C. The Model Procurement Allows Exemption from Formal RFP Requirements When “Not Feasible”**

As discussed above, the University has traditionally used the formal RFP competitive negotiation process to select investment managers. KRS 45A.095, however, allows the University to utilize noncompetitive negotiation outside the formal RFP process under one of three circumstances: (1) for sole source purchases; (2) when “competition is not feasible,” as determined by the purchasing officer in writing prior to award, or (3) when emergency conditions exist. KRS 45A.095(1).<sup>9</sup>

The Kentucky Courts have not addressed what constitutes a situation when “competition is not feasible.” Some guidance can be gleaned from the circumstances

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<sup>8</sup> See KRS 164A.615 (“Nothing contained in KRS 164A.555 to 164A.630 shall be construed to prevent an institution or an affiliated corporation from enforcing or carrying out the bona fide terms of any gift, grant, conveyance, devise or bequest from any private person, corporation, foundation, estate or entity contributing funds or any other thing of value to the institution or affiliated corporation.”); Ky. AG Op. 82-520 (1982) (S. Beshear, A.G.) (“KRS Chapters 45 and 45A concern public funds of the Commonwealth such that these provisions are not applicable to the private funds and contributions [of state supported institutions of higher learning] covered in KRS 41.290.”)

<sup>9</sup> See also Ky. AG Op. 92-40 (1992) (Gorman, A.G.) (“The emergency conditions exception is only one of three exceptions to the competitive bidding requirement, the other two being sole source purchases and situations when competition is not feasible.”)



in which sole source is allowed, specified in 45A.095(1) as a “situation in which there is only one (1) known capable supplier of a commodity or service, occasioned by the unique nature of the requirement, the supplier, or market conditions.” However, the text of the statute does not limit the “not feasible” requirement to a “unique” situation, but rather defers to a determination made by the purchasing officer.

There are two reasons why the present circumstances are a “unique” situation. First, the University’s senior financial staff has demonstrated that the formal RFP process is not feasible for selecting investment managers. Second, the proposed process furthers the broad purposes of the model procurement code. Each of these reasons is addressed below.

**1. Senior Financial Management Staff Have Demonstrated That the Formal RFP Process Is “Not Feasible” for Selecting Investment Managers.**

The constraints and limitations of the current formal RFP process detailed above justify a determination that formal competitive negotiation conducted strictly under KRS 45A.085 is not a feasible method for selecting investment managers that would provide services most advantageous to the University. This infeasibility results from the University’s need to anticipate or react to ever changing market conditions in a deliberate but timely manner. The time and market constraints inherent in the formal RFP process do not allow the University to meet this need, and generally increases the costs to the University in the form of both higher fees

and lost opportunities. Therefore, sufficient evidence exists to allow the University's purchasing officer to determine that the use of the formal RFP process to select investment managers is "not feasible."

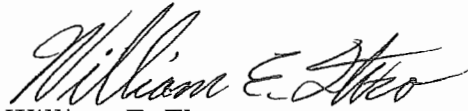
**2. The Proposed New Selection Process Furthers the Purposes of the Model Procurement Code by Retaining Key Competitive Negotiation Elements**

Although the formal RFP process has proven "not feasible" for selecting investment managers, the University should still strive to meet as many of the purposes and policies of the Model Procurement Code as possible. The new selection process proposed by the University's investment staff complies with these purposes and policies by retaining many of the key facets of competitive negotiation listed in KRS 45A.085. The new process will utilize solicitation of offers through its fiduciary investment consultant, and University officials will actively review the offers along with the consultant. University officials will engage with offerors to perform additional due diligence, and will negotiate with offerors regarding fees and other terms. Therefore, the new process has been clearly defined and designed to select the firm that offers the best value for the University and whose proposal is the most advantageous to the University's ability to fulfill its mission. Moreover, University officials will report on searches conducted under the new process to the Investment Committee, thus safeguarding the quality and integrity of, and maintaining public confidence in, the process.

## CONCLUSION

For the reasons detailed above, the University may adopt the new alternative competitive negotiation process to select external investment managers for the Endowment as described above.

August 4, 2016

A handwritten signature in black ink, appearing to read "William E. Thro". The signature is fluid and cursive, with the first name "William" being the most prominent part.

William E. Thro  
General Counsel  
University of Kentucky

**APPENDIX 2**

**Kentucky Uniform Prudent Management of Institutional Funds Act  
(KRS 273.600 to KRS 273.645)**

**273.600 Definitions for KRS 273.600 to 273.645.**

In KRS 273.600 to 273.645:

- (1) "Charitable purpose" means the relief of poverty, the advancement of education or religion, the promotion of health, the promotion of a governmental purpose, or any other purpose the achievement of which is beneficial to the community;
- (2) "Endowment fund" means an institutional fund or part thereof that, under the terms of a gift instrument, is not wholly expendable by the institution on a current basis. The term does not include assets that an institution designates as an endowment fund for its own use;
- (3) "Gift instrument" means a record or records, including an institutional solicitation, under which property is granted to, transferred to, or held by an institution as an institutional fund;
- (4) "Institution" means:
  - (a) A person, other than an individual, organized and operated exclusively for charitable purposes;
  - (b) A government or governmental subdivision, agency, or instrumentality, to the extent that it holds funds exclusively for a charitable purpose; or
  - (c) A trust that had both charitable and noncharitable interests, after all noncharitable interests have terminated;
- (5) "Institutional fund" means a fund held by an institution exclusively for charitable purposes. The term does not include:
  - (a) Program-related assets;
  - (b) A fund held for an institution by a trustee that is not an institution; or
  - (c) A fund in which a beneficiary that is not an institution has an interest, other than an interest that could arise upon violation or failure of the purposes of the fund;
- (6) "Person" means an individual, corporation, business trust, estate, trust, partnership, limited liability company, association, joint venture, public corporation, government or governmental subdivision, agency, or instrumentality, or any other legal or commercial entity;
- (7) "Program-related asset" means an asset held by an institution primarily to accomplish a charitable purpose of the institution and not primarily for investment; and
- (8) "Record" means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 1, effective July 15, 2010.

**273.605 Standard of conduct in managing and investigating institutional fund.**

- (1) Subject to the intent of a donor expressed in a gift instrument, an institution, in managing and investing an institutional fund, shall consider the charitable purposes of the institution and the purposes of the institutional fund.
- (2) In addition to complying with duty of loyalty imposed by law other than in KRS 273.600 to 273.645, each person responsible for managing and investing an institutional fund shall manage and invest the fund in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.

- (3) In managing and investing an institutional fund, an institution:
- (a) May incur only costs that are appropriate and reasonable in relation to the assets, the purposes of the institution, and the skills available to the institution; and
  - (b) Shall make a reasonable effort to verify facts relevant to the management and investment of the fund.
- (4) An institution may pool two (2) or more institutional funds for purposes of management and investment.
- (5) Except as otherwise provided by a gift instrument, the following rules apply:
- (a) In managing and investing an institutional fund, the following factors, if relevant, shall be considered:
    - 1. General economic conditions;
    - 2. The possible effect of inflation or deflation;
    - 3. The expected tax consequences, if any, of investment decisions or strategies;
    - 4. The role that each investment or course of action plays within the overall investment portfolio of the fund;
    - 5. The expected total return from income and the appreciation of investments;
    - 6. Other resources of the institution;
    - 7. The needs of the institution and the fund to make distributions and to preserve capital; and
    - 8. An asset's special relationship or special value, if any, to the charitable purposes of the institution;
  - (b) Management and investment decisions about an individual asset shall be made not in isolation but rather in the context of the institutional fund's portfolio of investments as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the fund and to the institution;
  - (c) Except as otherwise provided by law other than KRS 273.600 to 273.645, an institution may invest in any kind of property or type of investment consistent with this section;
  - (d) An institution shall diversify the investments of an institutional fund unless the institution reasonably determines that, because of special circumstances, the purposes of the fund are better served without diversification;
  - (e) Within a reasonable time after receiving property, an institution shall make and carry out decisions concerning the retention or disposition of the property or to rebalance a portfolio in order to bring the institutional fund into compliance with the purposes, terms, and distribution requirements of the institution as necessary to meet other circumstances of the institution and the requirements of KRS 273.600 to 273.645; and
  - (f) A person that has special skills or expertise, or is selected in reliance upon the person's representation that the person has special skills or expertise, has a duty to use those skills or that expertise in managing and investing institutional funds.

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 2, effective July 15, 2010.

**273.610 Appropriation for expenditure or accumulation of endowment -- Rules of construction.**

- (1) Subject to the intent of a donor expressed in the gift instrument, an institution may appropriate for expenditure or accumulate so much of an endowment fund as the institution determines is prudent for the uses, benefits, purposes, and duration for which the endowment

fund is established. Unless stated otherwise in the gift instrument, the assets in an endowment fund are donor-restricted assets until appropriated for expenditure by the institution. In making a determination to appropriate or accumulate, the institution shall act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, and shall consider, if relevant, the following factors:

- (a) The duration and preservation of the endowment fund;
  - (b) The purposes of the institution and the endowment fund;
  - (c) General economic conditions;
  - (d) The possible effect of inflation or deflation;
  - (e) The expected total return from income and the appreciation of investments;
  - (f) Other resources of the institution; and
  - (g) The investment policy of the institution.
- (2) To limit the authority to appropriate for expenditure or accumulate under subsection (1) of this section, a gift instrument must specifically state the limitation.
- (3) Terms in a gift instrument designating a gift as an endowment, or a direction or authorization in the gift instrument to use only "income," "interest," "dividends," or "rents, issues, or profits," or "to preserve the principal intact," or words of similar import:
- (a) Create an endowment fund of permanent duration unless other language in the gift instrument limits the duration or purpose of the fund; and
  - (b) Do not otherwise limit the authority to appropriate for expenditure or accumulate under subsection (1) of this section.

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 3, effective July 15, 2010.

### **273.615 Delegation of management and investment functions.**

- (1) Subject to any specific limitation set forth in a gift instrument or in law other than KRS 273.600 to 273.645, an institution may delegate to an external agent the management and investment of an institutional fund to the extent that an institution could prudently delegate under the circumstances. An institution shall act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, in:
- (a) Selecting an agent;
  - (b) Establishing the scope and terms of the delegation, consistent with the purposes of the institution and the institutional fund; and
  - (c) Periodically reviewing the agent's actions in order to monitor the agent's performance and compliance with the scope and terms of the delegation.
- (2) In performing a delegated function, an agent owes a duty to the institution to exercise reasonable care to comply with the scope and terms of the delegation.
- (3) An institution that complies with subsection (1) of this section is not liable for the decisions or actions of an agent to which the function was delegated.
- (4) By accepting delegation of a management or investment function from an institution that is subject to the laws of the Commonwealth, an agent submits to the jurisdiction of the courts of the Commonwealth in all proceedings arising from or related to the delegation or the performance of the delegated function.
- (5) An institution may delegate management and investment functions to its committees, officers, or employees as authorized by law of the Commonwealth other than KRS 273.600 to 273.645.

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 4, effective July 15, 2010.

**273.620 Release or modification of restrictions on management, investment, or purpose.**

(1) If the donor consents in a record, an institution may release or modify, in whole or in part, a restriction contained in a gift instrument on the management, investment, or purpose of an institutional fund. A release or modification may not allow a fund to be used for a purpose other than a charitable purpose of the institution.

(2) The court, upon application of an institution, may modify a restriction contained in a gift instrument regarding the management or investment of an institutional fund if the restriction has become impracticable or wasteful, if it impairs the management or investment of the fund, or if, because of circumstances not anticipated by the donor, a modification of a restriction will further the purposes of the fund. The institution shall notify the Attorney General of the application, and the Attorney General shall be given an opportunity to be heard. To the extent practicable, any modification shall be made in accordance with the donor's probable intention.

(3) If a particular charitable purpose or a restriction contained in a gift instrument on the use of an institutional fund becomes unlawful, impracticable, impossible to achieve, or wasteful, the court, upon application of an institution, may modify the purpose of the fund or the restriction on the use of the fund in a manner consistent with the charitable purpose expressed in the gift instrument. The institution shall notify the Attorney General of the application, and the Attorney General shall be given an opportunity to be heard.

(4) If an institution determines that a restriction contained in a gift instrument on the management, investment, or purpose of an institutional fund is unlawful, impracticable, impossible to achieve, or wasteful, the institution, sixty (60) days after notification to the Attorney General, may release or modify the restriction, in whole or part, if:

- (a) The institutional fund subject to the restriction has a total value of less than fifty thousand dollars (\$50,000);
- (b) More than twenty (20) years have elapsed since the fund was established; and
- (c) The institution uses the property in a manner consistent with the charitable purposes expressed in the gift instrument.

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 5, effective July 15, 2010.

**273.625 Reviewing compliance with KRS 273.600 to 273.645.**

Compliance with KRS 273.600 to 273.645 is determined in light of the facts and circumstances existing at the time a decision is made or action is taken, and not by hindsight.

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 6, effective July 15, 2010.

**273.630 Application of KRS 273.600 to 273.645 to existing institutional funds.**

KRS 273.600 to 273.645 apply to an institutional fund existing on or established after July 15, 2010. As applied to institutional funds existing on July 15, 2010, KRS 273.600 to 273.645 govern only decisions made or actions taken on or after that date.

**Effective:** July 15, 2010



**History:** Created 2010 Ky. Acts ch. 34, sec. 7, effective July 15, 2010.

**273.635 Relation of KRS 273.600 to 273.645 to the Electronic Signatures in Global and National Commerce Act.**

KRS 273.600 to 273.645 modify, limit, and supersede the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. secs. 7001 et seq., but does not modify, limit, or supersede Section 101 of that act, 15 U.S.C. sec. 7001(a), or authorize electronic delivery of any of the notices described in Section 103 of that act, 15 U.S.C. sec. 7003(b).

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 8, effective July 15, 2010.

**273.640 Uniformity of application and construction of the Kentucky Uniform Prudent Management of Institutional Funds Act.**

In applying and construing this uniform act, consideration shall be given to the need to promote uniformity of the law with respect to its subject matter among states that enact it.

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 9, effective July 15, 2010.

**273.645 Short title for KRS 273.600 to 273.645.**

KRS 273.600 to 273.645 may be cited as the Kentucky Uniform Prudent Management of Institutional Funds Act.

**Effective:** July 15, 2010

**History:** Created 2010 Ky. Acts ch. 34, sec. 10, effective July 15, 2010.