

The Arkansas 4-H Foundation, Inc.
Spending Endowment Policy
(Effective July 22, 2009)

The Arkansas 4-H Foundation, Inc. establishes endowment funds to support donors' purposes in perpetuity. Gifts of cash or cash generated from conversion of a non-cash asset are invested in the Arkansas 4-H Foundation, Inc. endowment investment pool.

The Arkansas 4-H Foundation, Inc. endowment investment policy has as its goal to provide a real total return from assets invested that will preserve or increase the purchasing power of the endowment capital, while generating the maximum current income stream to support the activities of funds held for the Arkansas 4-H program of the University of Arkansas, Division of Agriculture, Cooperative Extension Service.

When an endowment is created by the Arkansas 4-H Foundation, Inc., three distinct funds are established: an *endowment principal fund*, an *income stabilization fund* and an *endowment spendable fund*.

Endowment Principal Fund

Each endowment principal fund that participates in the endowment investment pool will have three values: book value, spending base, and market value.

Book Value

The book value is the original gift plus any subsequent gifts (including corporate and State matches) that are placed in the endowment's principal fund.

Spending Base

Each endowment's principal fund has a spending base that represents the fund's base for calculating endowment spending, transfers and fee assessments. The spending base is reviewed at the end of the fiscal year for adjustment of the investment performance.

Market Value

The market value is the actual value of each endowment fund's share of the investment portfolio at a specific point in time. This value is updated quarterly.

Endowment Spendable Fund

The Foundation's Board of Directors will review and set spending policy with a maximum goal of 5.0% of the annual earnings, which includes a 0.5% yearly administrative fee and 4.5% for actual spending. In years where the return is less than 5% plus inflation rate, then the administrative fee will be prorated. The administrative fee will be prorated at 0.1% per every 1% of the spending rate. The spending rate will be reviewed by the Board to determine annual spending payout. To achieve the objective of maintaining purchasing power, the endowment's return must be equal to the payout distributed annually plus inflation and investment /administrative costs. The spending policy will be determined by audited balances of the

investment income as of June 30. The spending rate, inflation rate, and income stabilization fund rate will be decided at the October board meeting.

The spending rate for the fiscal year and past fiscal years is:

YEAR	APPROVED SPENDING RATE
2010	
2011	
2012	
2013	
2014	
2015	
2016	
2017	
2018	

First spending rate effective for Fiscal Year 2011

The endowment spendable fund allows spending in accordance with the written agreement between the donor and the Foundation. Additional restrictions may be imposed for funds that receive state matching gift monies.

Spending Base Adjustments

In the short-term, the market can be highly volatile. The Foundation's investment policy is designed to return a net positive gain in market value (growth) over an extended period of time. It recognizes that there may be periods of decline in value, but these should be more than offset by periods of increase in value.

Underwater Endowments

The term “underwater endowment” refers to those endowments where the market value is less than its book value (corpus). Under periods of extreme market stress when the endowment is either “underwater” or interest rates are below historical norms or when instability of global markets threatens the very fabric of the Endowment, Arkansas 4-H Foundation, Inc. will initiate any needed temporary spending restraints to ensure the ongoing sustainability of their resources.

At the end of each fiscal year, a comparison will be made of the fund’s market value to book value. If the ratio of market value to book value falls below the principal fund (corpus), no spending will be allowed, unless spending approval is granted from the donor or the board of Directors of the Arkansas 4-H Foundation, Inc. The endowment will be frozen until market value of the original principal fund (corpus) is 3.0% above its book value. The 3.0% will be allocated to the following: 1.0% Spending Rate, 1.0% Inflation (back to corpus), 1.0% Income Stabilization Account. Endowment Spending Accounts will also be frozen in the event of an endowment that is underwater, unless spending approval is granted from the donor or the board of Directors of the Arkansas 4-H Foundation, Inc. Monies may be transferred from the Endowment Spending Account to the principal fund to help prevent an underwater endowment.

Endowment Administrative Fee

The administrative fee will be prorated at 0.1% per every 1% of the spending rate. The administration fee is to support the Foundation's administration costs of the endowment and fundraising programs, unless the donor of the endowment prohibits an administrative fee being charged, or other arrangements have been made.

Other Endowment Policies

The minimum *investment objective* of the endowment fund is to earn a total rate of return that exceeds the sum of: the annual rate of change in the Consumer Price Index (CPI) *plus* the level of the Spending Income Allocation Rate as set out in this policy.

The *purchasing power* of the endowment fund will be preserved by the addition of an inflation adjustment factor to each endowment principal account.

The Arkansas 4-H Foundation, Inc. will maintain an Income Stabilization Fund. When there are insufficient investment earnings to support the annual spending income allocation, transfers are made from this fund. The Income Stabilization Fund shall *not exceed 15%* of the aggregate market value of the endowment principal accounts. Prior to attaining this maximum level, a portion of the investment earnings shall be added to the Endowment Principal Accounts, as determined by the Board of Directors of the Arkansas 4-H Foundation or their designees (committee). The Income Stabilization Fund will be supported by excess funds calculated.

Total Earnings – (Spending Allocation Rate + Investment Fees + Positive Change in the Consumer Price Index*) = Income Stabilization Fund (*Maximum of 15% of Market Value of the Endowment*)

The spending policy for the Arkansas 4-H Foundation, Inc. will be based on a five-year rolling average of the market value, based on audited financials as of June 30 each year. The five-year average will begin on June 30, 2009.

The Arkansas 4-H Foundation, Inc. will follow guidelines set forth by the Uniform Prudent Management of Institutional Funds Act and any other act that may impact the foundation. The board will keep the following in mind when making decisions on endowments:

UPMIFA establishes the “prudent person” standard, stating that “the foundation shall act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances.” To assist in determining the corpus balance for a donor-restricted endowment fund, UPMIFA identifies seven factors that a not-for-profit organization should consider. These factors are:

- 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 appreciation of investments;
the other resources of the institution; and
the investment policy of the institution.

Example

Here is an example of how spending policy works. Assume a gift of \$5,000 and no addition to the gift. Also, assume we are able to earn an average of 10% on our investments. Further assume a 5% spending rate

	1977 Year 1	1981 Year 5	1986 Year 10	1991 Year 15	1996 Year 20	2001 Year 25	2006 Year 30	2007 Year 31	2008 Year 32	2009 Year 33
Beginning Balance	5,000	6,078	7,757	9,900	12,635	16,125	20,581	21,610	22,690	23,825
Earnings	500	608	776	990	1,263	1,613	2,058	2,161	2,269	2,382
Spending	250	304	388	495	632	806	1,029	1,080	1,135	1,191
Ending Balance	5,250	6,381	8,144	10,395	13,266	16,932	21,610	22,690	23,825	25,016

Note: Calendar Year(s) based upon assumption that original \$5,000 endowment was donated in 1976.

Notice that each year the endowment grows and the spending rate also grows. This method of calculation is designed to allow both the endowment and yearly transfers to earning to keep pace with inflation which has averaged a little more than 3% for the past sixty years. Of course, this simple example does not reflect the fact that markets don't always go up and that we don't always earn 10%, or factor in the Income Stabilization Fund. This example was designed to show our policies are aimed at protecting both the endowment and the spending rate from the effect of inflation.

Summary

The Arkansas 4-H Foundation, Inc., and the Board of Directors will decide on an appropriate spending policy, reflecting estimates of future investment returns, asset mix, role of inflation, and margin of error.

*Only Positive Consumer Price Indexes will be calculated, no calculations will be allowed for negative Consumer Price Indexes, to maximize endowment growing power.

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