

FCR 2

Office of the President
May 2, 2017

Members, Board of Trustees:

ESTABLISHMENT OF UNIVERSITY OPERATING QUASI-ENDOWMENT FUND

Recommendation: that the Board of Trustees authorize the establishment of the University Operating Quasi-Endowment Fund and approve the investment of operating cash and investments in the Endowment investment pool, subject to: (1) liquidity targets approved by the Debt Management Committee; (2) a total operating quasi-fund investment limitation of 35%; and (3) an annual maximum contribution of \$75,000,000 as set forth in the Operating Fund Investment Policy.

Background: University Financial Services (UFS) manages the University’s operating cash and investments in accordance with the Operating Fund Investment Policy under the direction of the Treasury Investment Advisory Group, consisting of the Executive Vice President for Finance and Administration, Treasurer, Chief Investment Officer, and Assistant Treasurer. The Operating Fund Investment Policy establishes a tiered management structure based on liquidity needs, return objectives, and Kentucky Revised Statutes. Additionally, UFS oversees the issuance of internal and external debt under the direction of the Debt Management Committee (DMC), which monitors the University’s internal and external debt capacity and establishes liquidity targets on an annual basis to ensure the credit strength of the University is maintained. The table below depicts the tiered structure established by the Operating Fund Investment Policy and the related liquidity targets approved by the DMC:

Category	Liquidity / Duration	Investment Return / Objective	Approved Days Cash on Hand Minimum/Targets
Tier I – Cash, Overnight, & Short-Term Investments	Daily	Principal preservation and liquidity	60 day minimum per Operating Fund Investment Policy
Tier II – Cash On Deposit with Commonwealth (subject to KRS 164A.555)	Daily	Principal preservation and liquidity	
Tier III – Other Operating Investments: Short / Intermediate Term Investments Intermediate / Long-Term Investments	0 to 5 years > 5 to 10 years	Principal preservation and enhanced return on investment	
Total Operating Fund Tiers I – III Days Cash on Hand Approved by DMC			125 to 175 days
Tier IV – Operating Funds Invested in Endowment Investment Pool	> 10 years	Long-term principal preservation and increased return on investment	
Other Cash and Investments	N/A	N/A	
Total Consolidated Monthly Days Cash on Hand Approved by DMC			140 to 195 days

At its March 2006 meeting, the Board of Trustees established the Hospital Quasi-Endowment Fund (Hospital Quasi). At its March 2006 and April 2007 meetings, the Board authorized transfers of up to \$250,000,000 of Hospital reserve funds to the Hospital Quasi. To date, \$225,000,000 has been transferred to the Hospital Quasi, which has grown to a market value of \$283,553,000. Establishment of the Hospital Quasi was recommended as an asset/liability management strategy in conjunction with issuance of bonds for the new Patient Care Facility in order to permit a longer-term investment objective and greater diversification of investments. Over time, the quasi-endowment has generated higher returns than shorter-term fixed income investments, providing additional resources to support the capital and operational needs of the Hospital.

Consistent with the Hospital Quasi-Endowment Fund strategy, establishment of the University Operating Quasi-Endowment Fund (University Quasi) will permit a longer-term investment horizon and greater diversification of investments for the University's long-term reserves, which is expected to produce higher returns over the long-term and generate additional resources to support the operating and capital needs of the University.

Subject to approval of the above recommendation and based on February 28, 2017 market values, \$75,000,000 is eligible for addition to the newly created quasi-endowment fund. Upon approval of the recommendation, UFS will initiate a phased implementation approach and provide ongoing oversight of the operating cash and investment program to ensure adequate liquidity is maintained in accordance with the approved liquidity targets. A report on the operating cash and investments and approved liquidity targets will be provided at each Investment Committee meeting.

Withdrawals from the University Quasi will require approval of the Board of Trustees.

The Operating Fund Investment Policy is available on the University's website at:

<http://www.uky.edu/ufs/sites/www.uky.edu.ufs/files/Operating%20Fund%20Investment%20Policy.pdf>

Action taken: Approved Disapproved Other_____