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April 1, 2016

The Honorable Orrin G. Hatch
Chairman, United States Senate
Committee on Finance
219 Dirksen Senate Office
Building Washington, D.C.
20510-6200

The Honorable Kevin Brady
Chairman, Committee on
Ways and Means
1102 Longworth HOB
Washington, D.C. 20515

The Honorable Peter Roskam
Chairman, Committee on
Ways and Means Oversight
Subcommittee
1102 Longworth HOB
Washington, D.C. 20515

Dear Chairmen Hatch, Brady and Roskam:

I am pleased to submit the following information about Smith College's endowment in response to your letter dated February 8, 2016.

Smith College invests its endowment assets prudently in order to achieve a long-term rate of return sufficient to fund a portion of its spending and to increase investment value equal to or above inflation. The college uses a diversified investment approach incorporating multiple asset classes, strategies and managers. The investment committee of the Smith College Board of Trustees oversees the college's investments and authorizes major investment decisions.

Endowment Management

Smith College's investments are overseen by the college's investment committee and managed by Investure LLC. Investure acts as the college's investment office and is charged with the responsibility for implementing and administering the college's investment policy. The investment office serves as the primary contact for all money managers. Investure reports to the investment committee monthly and meets with the committee no fewer than three times per year.

Smith manages its endowment investments to maximize annualized returns net of costs over rolling 10-year periods while adhering to stated risk parameters. The investment committee seeks 1) to avoid 25% or greater peak-to-trough declines in inflation-adjusted unit value; and 2) to avoid annualized shortfalls exceeding 3% relative to the mean return of the 50 largest endowments reporting to the National Association of College and University Business Officers (NACUBO), over rolling 10-year periods.

Restrictions (Question 1 a-f)

The college's endowment consists of approximately 2,000 individual funds established for a variety of purposes. These include:

- Permanently restricted net assets that are subject to donor stipulations requiring that they be maintained in perpetuity.
- Temporarily restricted net assets that are (primarily) gains on the investments of permanently restricted net assets.
- Unrestricted net assets that are not subject to donor stipulations restricting their use but that may be designated for specific purposes by the college. Those funds designated by the college are considered quasi-endowments and by their nature are included within unrestricted net assets.

Table 1. Endowment Totals by Net Asset Restriction

<i>\$ millions</i>	<u>2015</u>	<u>2014</u>	<u>2013</u>
Unrestricted	389.9	408.0	372.6
Temporarily Restricted	997.5	970.4	830.6
Permanently Restricted	394.3	377.4	354.2
Total	1,781.7	1,755.8	1,557.4

Table 2. Use Restrictions of the College's Endowment Funds
as of June 30

	2015		2014		2013	
	<u>\$ millions</u>	<u>%</u>	<u>\$ millions</u>	<u>%</u>	<u>\$ millions</u>	<u>%</u>
Financial Aid	687	39%	664	38%	586	38%
Instruction	434	24%	413	23%	370	24%
Unrestricted	267	15%	291	17%	259	17%
Academic Support	191	11%	189	11%	164	10%
Other	110	6%	108	5%	96	6%
Facilities	93	5%	91	5%	82	5%
Total	1,782	100%	1,756	100%	1,557	100%

The long-term investing horizon for the endowment allows for a large allocation to equity-oriented strategies where the potential for long-term capital appreciation exists. For the purpose of diversification, other assets, including but not limited to hedging and derivatives, are used to reduce risk and overall portfolio volatility.

**Table 3. Allocation of the College’s Investment Portfolio
as of June 30**

	<u>2015</u>	<u>2014</u>	<u>2013</u>
Global Equity	33%	35%	34%
Private Partnerships	32%	31%	33%
Alternative Equity	27%	26%	25%
Fixed Income & Cash	8%	8%	8%
	100%	100%	100%

The investment committee recognizes the need to maintain adequate liquidity in the endowment portfolio. Recognizing that private partnership cash flows are unpredictable, at least 60% of total endowment assets are held in investment vehicles utilizing lock-ups of five years or less. Under normal circumstances, private partnership investments, including unfunded capital commitments, will not exceed 65%.

Management Fees (Question 4)

Smith spent \$4.6 million on management and administrative fees related to its investment pool in 2014-15 (\$4.1 million in 2013-14, \$4.2 million in 2012-13). Fees have averaged 0.25% of the end-of-year market value of the investment pool over the past ten years, ranging from a low of 0.12% in 2009-10 to a high of 0.60% in 2011-12. The college makes performance-based and other fee payments to its investment manager, as defined in a contract that delineates the fee schedule. The performance-based incentive fee available to the investment manager is based on investment return in excess of a predefined threshold or “hurdle return.” The investment committee reviews management fees annually. In addition to covering investment management fees, the college charges custodial and legal fees directly to the investment pool.

Other Investments Not Held in the Endowment (Question 2)

Smith held an additional \$189 million in investments outside of the endowment in 2014-15 (\$162 million in 2013-14, \$164 million in 2012-13). These funds include assets held and invested within the college’s pool on behalf of other entities, such as the Alumnae Association of Smith College and the Smith Students’ Aid Society; college-held reserves; various other restricted assets that are held outside of the investment pool and are not available for expenditure; and short-term investments whose income is available for immediate use in support of the college’s educational mission.

Note: Question 5 is not applicable to Smith College

Endowment Spending and Use

Spending Rate (Questions 3, 6 and 8)

As affirmed in its 2008 report to the Senate Finance Committee, Smith’s endowment generates a critical funding stream that allows the college to provide financial aid to students with need, shape the composition of its faculty to meet curricular objectives, maintain and expand facilities, develop

new initiatives and programs to respond to current societal and intellectual challenges, and keep pace with technological changes integral to teaching and learning. By employing a spending rate approach that seeks the largest responsible annual contribution to operations while providing adequate downside protection against periods of declining returns, the college has grown its endowment to provide approximately 30% of operating revenues.

The college's current endowment spending rate policy has been in place since 2005-06 and reads as follows:

Responsibility for the spending policy resides with the finance committee of the board of trustees. A formal spending policy has been adopted to fairly apportion endowment income between current and future generations of Smith College students. An additional goal of this policy is to minimize the temptation to relieve all budgetary pressures by simply taking additional monies from the endowment. The approved spending rate formula is designed to provide a relatively predictable and growing stream of revenues to the operating budget.

Each year the spending rate per share will normally increase by a 4% annual inflator. This income per share valuation times the number of shares will be tested each year to be sure that it is within a collar of 4% and 6% of the ending market value of the pooled endowment as of December 31 of that year. The board may decide to increase or decrease the annual inflator (4%) in order to remain within the bounds. The board will review and approve the spending rate each year.

The finance committee of the board of trustees periodically reviews the endowment spending rate policy. The committee last conducted such a review in 2011-12. These reviews focus on smoothing the effect of market volatility on the operating budget, minimizing the likelihood of substantial loss in endowment value, and achieving intergenerational equity. The college continues to monitor market conditions, particularly in light of increased volatility, and their impacts on the endowment's ability to support operations and maintain intergenerational equity.

Over the past ten years (through fiscal year 2014-15), the college's endowment spending rate averaged 4.8% and ranged from a low of 4.3% in 2006-07 to a high of 5.7% in 2009-10. The spending rate has exceeded 5.0% in four of the past ten years, most recently in 2012-13. With the recent softening in capital markets, the college expects next year's spending rate to exceed 5.0%.

Table 4. Spending Rate Over the Past Ten Years
with endowment market returns, net endowment growth and year-end market value

	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006
Spending rate	4.4%	4.8%	5.1%	4.8%	5.3%	5.7%	5.0%	4.4%	4.3%	4.6%
Endowment market return	6.7%	16.5%	14.3%	2.2%	19.1%	16.3%	-16.7%	4.3%	23.2%	14.2%
Net growth	1.5%	12.7%	10.5%	-1.6%	15.2%	13.4%	-19.7%	0.4%	17.7%	11.7%
Year-end market value (billions)	\$1.78	\$1.76	\$1.56	\$1.41	\$1.43	\$1.24	\$1.10	\$1.37	\$1.36	\$1.16

As indicated in Table 4, Smith’s endowment totaled \$1.78 billion as of June 30, 2015. Over the last ten years, the endowment increased by \$746 million, or 5.6% annually. This increase reflects the contribution of new gifts, transfers and appreciation minus endowment spending to support operations and management expenses. Gifts and transfers have accounted for \$172 million of the overall growth, or the equivalent of 1.6% of the beginning-of-year market value annually.

Spending Endowment Principal (Question 7)

Because Smith is incorporated in Massachusetts, the management of the college’s endowment is governed by the Uniform Prudent Management of Institutional Funds Act (UPMIFA). The college’s independent auditors have affirmed its interpretation of the Massachusetts-enacted version of UPMIFA as allowing the college to continue to prudently spend from a restricted endowed fund during times when its current value is less than the original gift value. The college then preserves the restricted principal value with unrestricted funds.

Financial Aid and the Endowment (Question 9)

Smith educates women of promise for lives of distinction. The college seeks to attract and enroll talented women with the potential to succeed in a rigorous academic program -- without regard to their ability to pay. Smith meets the full demonstrated financial need of all enrolled students, using a widely standard methodology to determine a student and family’s ability to pay for a college education.

Smith has a well-established position of leadership in providing financial aid, as evidenced by the proportion of students receiving federal Pell grants (21% of the student body in 2014-15); the proportion of students receiving need-based aid (60%); and financial aid spending as a percentage of tuition, room and board revenue (40%).

Smith spent \$60.3 million on institutional grant aid for undergraduates in 2014-15. Institutional aid excludes pass-through grants from federal and state government sources, such as Pell Grants. Approximately 97% of undergraduate institutional grant aid at Smith is awarded solely on the basis of demonstrated need, with the remaining 3% allocated as merit-only aid. The STRIDE program,

which pairs entering students with faculty members to conduct research, is one example of merit aid at Smith.

Smith's endowment makes it possible for the college to enroll students from across the income spectrum through this level of financial aid. Endowments restricted (either by the donor or by the college) for undergraduate financial aid covered \$26.6 million, or 44%, of the total spent on institutional grants. The remaining \$33.7 million was funded by a combination of general operating revenues, unrestricted endowment income and gifts.

Undergraduate grant aid increased by an annualized rate of 4.7% between 2005-06 and 2014-15. This is higher than the 4.4% rate of growth for comprehensive fees. As a result, the college's discount rate (institutional grant expense/gross comprehensive fee revenue) for undergraduates increased from 37% to 40% over the past decade. The college provided aid to nearly 65% of undergraduate students in 2014-15, of which approximately 60% was need-based aid. In 2014-15 the average institutional grant among undergraduate students with need-based grants was \$35,500.

Income from the endowment, combined with annual giving, provides a significant benefit for every student at Smith College, whether or not the student is receiving financial aid. In 2014-15, the cost incurred by the college to educate an undergraduate student was nearly \$80,000 and the total comprehensive fee charge was \$59,674. This means that a student who is not eligible for financial aid received a 25% discount against the cost to educate. Due to the generosity of donors and through the benefit of strong investment returns over time, the college is able to provide the highest quality educational experience for all of its students.

Rejecting Endowed Gifts Due to Restriction (Question 10)

The college has a gift acceptance policy that governs the receipt of funds from donors. The policy stipulates as follows:

Smith College reserves the right not to accept a proposed gift for reasons including, but not limited to, the following:

- *The gift or gift transaction involves an illegality.*
- *The gift or gift transaction in some manner conflicts with Smith policies or with Smith's mission.*
- *The benefit of the gift is outweighed by the potential of negative publicity for Smith that would result from the transaction.*
- *The gift or gift transaction inhibits Smith from seeking donations from other donors.*
- *The benefit of the gift is insufficient to offset the extent of administrative and/or legal effort involved.*
- *The donor, or other prohibited party, wishes to exert control over how the donated funds are used beyond the gift agreement.*

In addition, all new or updated fund agreements include a contingency clause providing the board of trustees the power to adjust fund agreements should they become impractical to administer in the future.

While the college has rejected gifts due to donor restrictions, it does not specifically track these occurrences so no specific cases can be provided. One example might be that where a donor wants to support a named individual for Smith tuition or, more commonly, summer non-degree program tuition. The college lets the potential donor know that under IRS guidelines this does not qualify as a charitable gift. The individual can pay the tuition, but it is not recorded as a gift and no receipt is issued. The donor is also informed that she or he can change the restriction to more broadly apply to a program rather than providing something that benefits a specific individual.

Real Property (Question 11)

Smith College has no direct investment real estate exposure in its endowment.

With more than 110 residential, academic and administrative buildings comprising more than three million gross square feet of space on 147 acres at its main campus and 256 acres at its MacLeish Field Station, the majority of the college's real estate holdings directly support its core mission.

Table 5. Gross Building Square Footage of Smith College

broken out by building type.

Building Type	Gross Square Footage (millions)
Academic	1.4
Student Residences	1.1
Administrative	0.6
Athletic	0.3
Rental Properties	0.2
Total	3.6

The majority of the college's institutional real estate holdings are within the city of Northampton, Massachusetts, with smaller holdings in the towns of Whately and Conway, Massachusetts. While much of the campus is tax exempt, Smith pays more than \$500,000 in real estate taxes annually for properties that are not in academic use, making it Northampton's largest real estate taxpayer by a significant margin. The college also makes other payments to the city that were negotiated through development agreements or other memoranda of understanding. These amounts totaled \$58,000 in 2012-13, \$72,000 in 2013-14, and \$96,000 in 2014-15.

Outside of the circumstances noted above, Smith College does not make payments in lieu of taxes because, as a charitable institution, the college is tax-exempt. The college does, nonetheless, make major voluntary contributions to the local community. One example: In 2014-15, Smith provided free college-level courses to 122 Northampton High School students (a benefit that has been in place since 1965) and grants to 12 local college students, enabling them to attend Smith at half tuition. Combined, these benefits totaled more than \$2.2 million.

Donations

Named Endowed Fund Minimums (Question 12)

The minimums to establish named endowed funds, including those that fund scholarships at Smith, are set by the board of trustees. Minimum fund levels for endowments to support scholarships range from \$250,000 to \$1.0 million, depending on the type of scholarship the donor is funding. Minimums are also established for other types of endowments, including those that support the faculty or specific programs.

If a donor is interested in reaching the fund minimum over time, a written statement of intent must be completed at the time of the initial gift. In general, Smith does not accept new endowments where broader fundraising is required to reach the fund minimum. In the rare case when such a fund is approved, the fund agreement must include a date certain for reaching the minimum and a contingency clause indicating how the fund will be utilized if the endowed fund minimum is not reached (spent out for the restriction indicated, or transferred to another fund, etc.).

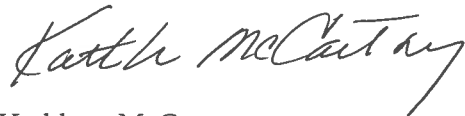
Conflicts of Interest (Question 13)

All Smith trustees and officers are fiduciaries of the college and are expected to avoid conflicts and the appearance of conflicts between their personal interests, the interests of the college and each other. Trustees and officers are required to file financial disclosure statements every year detailing corporate and other ownership interests as well as board membership by the trustee or officer and her or his family members. Trustees and officers have affirmative obligation to update the financial disclosure statements as they become aware of changes in their financial situation. A trustee or officer who believes that she or he or any member of her or his family may have a conflict of interest or may appear to have a conflict of interest with respect to any particular transaction shall promptly and fully disclose the conflict to the president and the chair of the board of trustees who shall take appropriate action.

Conclusion

Smith College's endowment was established nearly 150 years ago with one woman's generous bequest. It has grown through the significant generosity of other donors and the college's long-term investment focus and strong returns, coupled with responsible spending. Looking to the future, Smith will continue to apply scrupulous endowment management practices to ensure that the college can provide an essential societal good—excellent higher education for women—for generations to come.

Sincerely,



Kathleen McCartney
President
Smith College