THE REGULATORY FUNDAMENTALS GROUP LLC

The Importance of the Endowment Valuation Process

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ABOUT RFG

RFG helps endowment investment offices and other clients develop cost-effective, enterprise-focused solutions to identify, and stay current with, the complex laws, regulations and transaction terms that impact their day-to-day operations. RFG represents clients which have more than $100 billion in assets under management, including a consortium of the nation's leading endowment investment offices.

To learn more, please visit RegFG.com or call 212-537-4058 x 1.

Introduction

Including difficult to value assets in an investment portfolio requires careful consideration as to how the investor will value the assets. This, in turn, may require an appreciation of how third-party investment managers produce interim valuations.

Why? Several reasons are noted below.

Important Valuation Factors

- **Requirements of Stakeholders**
- **Asset Allocations**
- **Manager Allocations**
- **Incentive Compensation**
- **Fiduciary Duties**

- **Requirements of Stakeholders.** Most endowments face requirements, both internal and external, to make periodic reports to stakeholders. The stakeholders may include an organization's own board and investment committee, public entities that exercise oversight, and even lenders if an organization has outstanding debt instruments (as values of assets are included directly and indirectly in representations and covenants). Each of these stakeholders is likely to expect that interim valuations are undertaken with sufficient rigor and consistency to satisfy applicable financial reporting standards. Some may explicitly require reporting in accordance with generally accepted accounting principles or another standard. Importantly, a fair valuation should be done on the same basis each time an investor reports; otherwise, boards and other stakeholders may be confused as to the basis of the information they are receiving. Of course, a document prepared solely for internal management purposes and which clearly indicates that it is not prepared based on fair value may be acceptable for some internal purposes.

- **Asset Allocations.** Asset allocations cannot be made on a meaningful basis unless all assets in a portfolio are valued in a consistent manner. If some portion of the portfolio is held at an arbitrary value (such as cost), then the allocations will also run the risk of being arbitrary or not achieving their intended purpose.

- **Manager Allocations.** Sometimes an organization is given the opportunity to place additional funds with a manager. However, if the existing assets are not valued on a consistent, rigorous basis, the decision may be a difficult one to make. It is not atypical for a private equity fund to offer investors the chance to invest in a new fund before the results of a prior fund have crystalized.

- **Incentive Compensation**. Some organizations may provide incentive compensation to staff or advisers based on returns. Without an appropriate valuation methodology, the calculation of the compensation may be thrown into doubt.

- **Fiduciary Duties.** It may be difficult to establish that a fiduciary has satisfied its duties without being able to demonstrate that the fiduciary understands the investments being made and has an ability to monitor them. Understanding valuation may be central to this process.

RFG conducts a yearly survey of endowment practices that addresses valuation and other issues of importance to investment office staff. To participate in an upcoming survey, contact Information@RegFG.com.

Conclusion

Charitable organizations need to properly value their investment assets in order to satisfy fiduciary duties and prepare appropriate financial reports.

If you are interested in a further discussion of these issues, please reach out to us:

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The following page provides information about how RFG supports your peers.

RFG REGULATION. SIMPLIFIED.

Regulatory Risk Management for Endowments and Foundations

Did you know that your investment activities are subject to multiple U.S. and foreign regulations?

Are You Comfortable That…

- Your compliance program is in line with peer group standards?
- You have fully satisfied all federal filing and reporting requirements?
- Managers you allocate to have kept up-to-date with applicable regulatory requirements?

If Not, Here is Your Solution

Join a consortium of your peers, the leading U.S. endowments and foundations, already using RFG Pathfinder®, and receive:

- **A baseline** of regulatory requirements.
- **Weekly thought leadership alerts** that provide insights on developments and future trends.
- **Peer-to-peer communications** through webinars and conferences, which allow you to share questions and knowledge.

Here's What Clients Say About RFG's Definitive Resource for Investment Offices

- "We have **gotten a lot** out of our partnership with RFG, and we think others can too."
- "As a new client, so far, **you have exceeded expectations**."
- "The forum you provide is **HUGELY beneficial**…"
- "Your work on reporting requirements has been **outstanding**."
- "The summaries you prepared on the Congressional inquiry…were circulated to our CFO and others in the organization…**they were just what we needed**."

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