



THE COMMUNITY FOUNDATION

Rochester Area Community Foundation

Investment Policy

Investment Policy Statement

The purpose of this investment policy is to establish a formal framework in which to manage the investment assets of Rochester Area Community Foundation.

The Board of Directors of Rochester Area Community Foundation (the Community Foundation) has the fiduciary responsibility to establish the parameters under which the assets of the Community Foundation are managed. These parameters include risk levels, asset allocation, diversification guidelines, credit quality, and the selection of investment managers and/or consultants who will most effectively implement the investment plan. The Board of Directors has delegated its oversight to the Investment Committee of Rochester Area Community Foundation. It is the role of the Investment Committee to provide oversight and stewardship of the assets entrusted to the Community Foundation by its benefactors. The Board of Directors and Investment Committee recognize that sound investment practices and procedural prudence are the keys to fulfillment of their fiduciary responsibility.

These policies outline the following:

- Investment Philosophy and Mission
- Asset Allocation
- Diversification Requirements
- Credit Quality
- Manager Selection and Review
- Statement of Spending Policy

1. Investment Philosophy and Mission

The Board of Directors and Staff of the Community Foundation strive to exercise good stewardship of the assets entrusted to the Community Foundation. To this end, the Community Foundation limits its portfolio to funds for specific purposes. These investments are made in accord with the following principles:

- A. **Mission of the Community Foundation** – Investments are made in accordance with the mission of the Community Foundation, to support its grantmaking, and insure the long-term viability of the organization.
- B. **Prudence** – In accordance with the concept of the Prudent Investor, the financial policy is based on a flexible balanced fund approach to accomplish the goals of the Community Foundation and yield an appropriate return given the level of risk undertaken. The Community Foundation will use a total rate of return approach to its spending policy as defined by the Board of Directors.

2. Fundamental Concepts

The Board of Directors stresses an investment policy which seeks to grow the assets of the Community Foundation over time, preserve the purchasing power of the assets, control risk, and provide for the spending needs as specified by the spending policy of the Community Foundation and its donors. The Board and the Investment Committee recognize that:

- A. Inflation erodes the purchasing power of assets in a foundation and changes in expectations can affect investment returns;
- B. Economic growth of the U.S. is likely to continue;
- C. Any investment requires the assumption of risk.

Therefore, equities of companies offering growth potential and possessing the financial resources to fund growth will be an integral part of the overall investment portfolio. Accordingly, the Investment Committee believes that the goals of capital appreciation, protection against inflation, and generation of sufficient income and returns for funding the spending policy of the portfolio can best be achieved by structuring a flexible, balanced fund approach.

These policies shall cover the following investment programs:

- I. Charitable Endowment Funds**
- II. Expenditure Funds**
- III. Charitable Investor FundSM**
- IV. Charitable Checking AccountSM**
- V. Pooled Life Income Funds**
- VI. Charitable Gift Annuity Funds**

Investment Policy

1. Asset Allocation

Given the above stated goals, the Community Foundation portfolio shall be managed as follows:

- A. Nominally, the equity pool of the portfolio should be invested in common equities including domestic as well as international or non-domestic equities. No single asset shall comprise more than 5% of the overall equity portfolio at any time. Equities should be diversified by economic sector and in multiple industries to assure diversified exposure to various sectors of the economy.

Within the equity portfolio the Investment Committee will consider diversification by style and market capitalization.

- B. Nominally, the fixed income pool of the portfolio should be invested in fixed income securities as described below:
 - 1. Investment Grade (as measured by a nationally recognized rating service such as Moody's or Standard & Poors), marketable corporate notes or bonds including convertible bonds.
N.B. Use of non-investment grade securities requires the express prior written approval of the Investment Committee.
 - 2. U.S. Government treasury or agency notes or bonds
 - 3. High quality, short term money market instruments, certificates of deposit - generally A1/P1 and Auction Rate Preferred issues with investment grade ratings.
 - 4. High quality mortgage backed securities.
- C. Tax-exempt issues are not appropriate for the portfolio by virtue of its tax-exempt status.
- D. Individual manager or fund liquidity should be limited to residual cash and income received. In general money market positions should be 5% or less.
- E. Managers may not employ leverage, margin, short sales or buy/sell uncovered options without the express prior written permission of the Investment Committee.

- F. Assets will be re-balanced by the staff to meet the asset allocation requirements as directed by the Investment Committee. General operational instructions shall be given to the staff by the Investment Committee and are attached to this policy as an addendum.

2. Implementation

Generally, the investment portfolio will be managed by independent investment managers with full discretion subject to the objectives and constraints imposed in this investment policy. The fixed income portion of the portfolio may be managed by investment advisors or laddered by maturity in a buy/hold strategy directed by the Investment Committee.

The investment managers shall meet with the Investment Committee as required by the Investment Committee to review their portfolio, its holdings, transactions and investment performance. Securities will, whenever possible, be held in a custodial arrangement with a reputable firm with the approval of the Investment Committee. Monthly custodial statements shall be sent to the financial officer of the Community Foundation and will constitute the official valuation statement of the portfolio. Each manager is required to submit periodic reports as determined by the Investment Committee and the staff.

Certain Community Foundation investments may be part of a co-mingled fund or limited partnership. In such cases, securities may not be held by an independent custodian. The Investment Committee should favor investment managers who operate in a manner which would allow the Community Foundation's securities to be held by an independent custodian.

The investment policy shall be reviewed at least once a year in order to assure consistency in attaining the goals and viability of the program.

3. Due Diligence for Selecting Investment Managers

In order to accomplish the goals and objectives of the Community Foundation, it is important that the Investment Committee engage qualified and competent investment professionals to manage the assets. The Investment Committee will consider the following factors when selecting managers:

- **Performance Adherence to Stated Investment Style** - The manager has a clearly articulated investment strategy and demonstrated discipline.
- **Performance Against Peers** - Time-weighted actual quarterly results, over the long-term, outperforms peer group median.

- **Performance relative to assumed risk** - Evaluated using statistical measures such as Sharpe Ratio, Alpha, and Standard deviation of returns.
- **Performance of Key Decision Makers** - Same portfolio manager (or portfolio management team) for 2/3 years, at least \$100 million under management.
- **Performance of Organization on Expense Control** - Expense ratio, fees, execution, and reasonable soft-dollar arrangements.
- **Performance of Overall Organization** - Stability, absence of regulatory problems, ability to handle growth.

It shall be the Investment Committee's responsibility to interview managers (firms) who have at least three years experience and track record and who have demonstrated skill in managing equities, fixed income, or balanced portfolios. Recognizing that many good firms do not subscribe to AIMR (Association for Investment Management and Research) standards, the Investment Committee should strive to select managers that are AIMR compliant and composite returns should be audited.

Each manager is to be given a copy of the investment policy statement and must agree to its terms unless there is a separate written agreement approved by the Investment Committee. Each manager should compare its returns to an index, which is appropriate to its investment style, as agreed to by the Investment Committee and the respective investment manager.

- The Community Foundation uses the Wilshire 5000 for its overall equity domestic benchmark. In addition, each equity manager will be instructed to use an unmanaged benchmark associated with its market capitalization and style specialty as a basis of comparison. Peer group returns should also be considered when evaluating managers.
- International Equity Managers shall use one or more Morgan Stanley EAFE Indices as their basis for comparison.
- US fixed income managers should use the Lehman Aggregate Bond Index as their basis of comparison. If the Community Foundation utilizes a U. S. fixed income manager with a strategy that results in a significantly different duration than the Lehman Aggregate Bond Index, the Investment Committee may utilize a different index for that manager.
- Balanced managers should use a blended index based on the asset allocation direction given by the Investment Committee.

4. Evaluation and Termination of Managers

Managers will be evaluated on rolling 3 and 5 year periods based on their performance against their benchmark, client service and communications, adherence to the terms of the investment policy, continuity of key professionals and ownership structure, style discipline, and spending policy requirements.

The Investment Committee should use reports and data that enable comparison of performance to the appropriate benchmarks and peer managers by style. These reports should be provided to the Investment Committee on a quarterly basis, and should be reported to the Board as required. Should the Investment Committee so determine, it may engage the services of a consultant to provide comparative data for the Investment Committee's consideration.

Managers that do not meet the expectations of the Community Foundation and the Investment Committee shall be given fair notice. It is important to recognize that there may be periods of underperformance by good managers. The Investment Committee must endeavor to monitor performance issues over the rolling 3 and 5 year periods to determine if a manager should be terminated.

In the case of hiring a new manager to replace a terminated manager, or the need to add an additional manager, the Investment Committee, acting as a whole or members thereof acting as an ad hoc committee, will interview and evaluate potential new managers. The Investment Committee may utilize the services of an outside consultant in the search process. Hiring a new manager will require the approval of the full Investment Committee. These actions should then be communicated to the Board of Directors.

I. Charitable Endowment Funds

The Community Foundation's endowment funds are managed with a long-term horizon using the total rate of return approach. The assets are invested in the equity and fixed income pools of the Community Foundation using an asset allocation of 70% equities as defined by the equity pool's strategic sector allocation, and 30% fixed income as defined by the fixed income pool. As a result, the policies that apply to the asset pools as defined in Section 1 of this document also apply to the endowed assets of the Community Foundation.

The Board of Directors and the Investment Committee believe that this asset allocation will maintain the purchasing power and future grantmaking capability of the endowment funds over the long term.

The level of income available for grant making is set at five percent (5%) of the rolling twenty-quarter average market value of the Charitable Endowment Funds. The rolling average spending rule or level adjusts for unusual short term market fluctuations, thereby giving predictability to future distributions. The Community Foundation's administrative fee structure for endowment funds is not a part of this investment policy.

II. Expenditure Funds

The Community Foundation will hold funds awaiting distribution or disbursement in an expenditure fund (the Fund). Since these monies will be spent within a short period of time, the investment objective shall be to produce current income and have low expected variability of principal. The Fund is expected to earn competitive yields or returns available in the money market or short term fixed income market. Since the Community Foundation uses a total rate of return approach, changes in Net Asset Value (NAV) can have an adverse short-term effect on the operating budget of the Community Foundation.

This Fund shall use institutional money market fund(s), short term fixed income funds, short term U.S. Government treasury or agency securities and/or Auction Rate Preferred Stock. For the purposes of this policy, short term will be defined as having a final maturity of three years or less.

The fund or funds used shall be of high average credit quality. Returns should be compared to an appropriate universe of similar funds such as the Donahue Domestic Money Market index. The staff will seek to earn competitive money market returns without exposing the Fund to unnecessary or inappropriate risks.

No mutual fund shall hold more than 10% of its assets in any one issuer or single obligor, except obligations of the U.S. Government or any agency thereof. In

addition, for any given fund, the Community Foundation's holdings shall not exceed 10% of the total assets of that fund.

III. Charitable Checking AccountSM

The Community Foundation holds certain contributions in the Charitable Checking AccountSM (the Fund) until the donor directs distribution. Since these monies are expected to be spent within a short period of time, the investment objective calls for low risk or low expected variability of principal.

This Fund shall use institutional money market fund(s), short term fixed income funds, short term U.S. Government treasury or agency securities and/or Auction Rate Preferred Stock. For the purposes of this policy, short term will be defined as having a final maturity of three years or less.

The fund or funds used shall be of high average credit quality. Returns should be compared to an appropriate universe of similar funds such as the Donahue Domestic Money Market index. The staff will seek to earn competitive money market returns without exposing the Fund to unnecessary or inappropriate risks.

No mutual fund shall hold more than 10% of its assets in any one issuer or single obligor, except obligations of the U.S. Government or any agency thereof. In addition, for any given fund, the Community Foundation's holdings shall not exceed 10% of the total assets of that fund.

IV. Charitable Investor FundSM

The Charitable Investor FundSM (the Fund) allows the Community Foundation to consider the asset allocation request of the donor, such that the investment allocation will complement the charitable purposes and expected duration of the Fund. Both income and principal may be distributed for charitable purposes. The investments are pooled with the Community Foundation's endowment portfolio. They are divided between the equity pool and the fixed income pool in varying asset allocation tracks selected for aggressive, long-term, balanced, moderate or conservative growth.

Each allocation track includes a five percent (5%) cash position for grantmaking liquidity. Since these accounts utilize the Community Foundation's asset pools, the general provisions of the Community Foundation's Investment Policy shall govern these accounts.

V. Pooled Life Income Fund

Contributions are pooled with other donations and invested for maximum current income and preservation of principal. Quarterly payments of income earned are made to the beneficiaries. After the lifetime of the beneficiaries, the remainder is paid to the Community Foundation for charitable purposes. The Community Foundation pays all administrative and investment management expenses so that the entire yield is paid to the beneficiaries. The trustee, Bank of America, invests the fund as follows: 80% in fixed income securities and 20% in a diversified portfolio of equities, with re-balancing to that asset allocation every quarter. A variety of common trust funds and mutual funds are utilized in the investment program.

The Investment Committee shall have oversight of the Trustee Bank's investment program and shall consider Bank of America's management in the context of the Community Foundation's policies on investment manager selection and monitoring (Sections 3 and 4).

VI. Charitable Gift Annuity Funds

Contributions of cash or publicly traded securities are exchanged for a lifetime stream of income guaranteed by the Community Foundation. The New York State Department of Insurance regulates charitable gift annuities including certain mandated reserve calculations and investment requirements. The Investment Committee has concluded that the annuities represent a long-term liability that should be matched with a long-term asset allocation. The asset allocation is 70% in a diversified portfolio of equities and 30% in fixed income securities. The Community Foundation has contracted with Bank of America Planned Giving Services for administration and investment management within the New York State regulations.

ADDENDUM

I. Operating Guidelines

Investment Authority is delegated to the Vice President and Chief Operating Officer and in his/her absence, to the President and Executive Director within the following guidelines:

1. All endowment and Charitable Investor FundSM contributions will be added to the fixed income pool.
2. The fixed income pool account will be re-balanced using State Street Global Advisors Passive Bond Market Index Fund.
3. The maximum cash in the fixed income pool account will not exceed five percent (5%) of such pool.
4. The equity pool account will be re-balanced using indexed mutual funds from State Street Global Advisors.
5. The maximum cash in the equity pool account will be no more than one percent (1%) of the total equity pool including all equity managers.
6. Staff will run the asset re-balancing software as needed but at least monthly, move, and invest funds as needed within the above guidelines. If there is a significant shift in the asset allocation, staff will contact the Chair of the Investment Committee for additional directions.
7. Results of re-balancing and interim decisions are to be communicated to the Investment Committee at the next regularly scheduled meeting.

II. Current Investment Managers

The endowment funds of the Community Foundation are managed by fourteen professional money managers under the direction of the Investment Committee. Those managers include American Funds, Ashford Capital Management, Clover Capital Management, Columbia Management Advisors, Frank Russell Funds through AM&M Planners, HSBC Bank USA, Genesee Valley Trust Company, Gryphon International Value Fund, JP Morgan Chase, Manning & Napier, Mazama Capital Management, PIMCO Total Return Fund, Sanderson International Value Fund, and State Street Global Advisors.

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