

# The Discipline to Succeed

## Assembling a Robust Investment Policy Statement for Endowments and Foundations

Economic conditions, securities markets, people and philosophies tend to be in a perpetual state of flux. Constant change can undermine commitment to a long-term investment plan; however, when an organization has a comprehensive Investment Policy Statement that sets forth long-term strategic direction, investment guidelines, and accountability standards, the course is well established and, over time, goals are more likely to be achieved.

Having a well-drafted Investment Policy Statement gives organizations the discipline to face the uncertainties of challenging investment environments. Removing emotion from the equation positively correlates with better results for the investment portfolio, leaving the organization better positioned to fulfill its mission.

### Executive Summary

An Investment Policy Statement (IPS) is an investment management document drafted by a client, often with the help of an investment advisor or consultant. The document serves as a strategic guide in the management of the client assets specified in the IPS and outlines the fiduciary responsibilities of those groups and individuals involved in the oversight of the assets.

Documentation of the client's objectives and constraints are critical in determining the Strategic Asset Allocation (SAA) that may best help achieve the client's long-term investment goals. Portfolio parameters may also be established which identify suitable investment styles and vehicles to employ in the portfolio, as well as tactical asset allocation ranges that managers may utilize in order to take advantage of market dislocations. Risk management control procedures, performance, and client service/reporting requirements may also be outlined.

The entire process of developing the IPS should be an educational experience for the client, as it entails a detailed discussion of how investment decisions are made, who is responsible for each aspect of this process, and clearly lays out expectations.

The development process has value to the investment advisor as well, as it allows the adviser to get to know the client better, and ultimately, the IPS provides clarity around guidance for investment decision making.

We recommend that the IPS be reviewed at least annually and as a response to material changes in a organization's circumstances or capital market assumptions. The IPS is meant to be a portable document that can be easily understood by anyone involved in the investment process. It is important that parties involved in the oversight of assets acknowledge they have reviewed and acknowledge the clients most recent IPS.

In this piece, we focus on nonprofit organizations, particularly foundations and endowments.

### The Components of an Investment Policy Statement

To help organizations develop a robust Investment Policy Statement (IPS), below we have outlined the sections commonly included. In this paper, we will try to explain the "what" and "why" of each section, as well as noting any special considerations.

#### Part One: Governance

Governance largely defines three elements: a) the purpose and scope of the IPS, b) the definition of duties for parties outlined in the IPS, and c) the investment philosophy. The purpose and scope often serves as a table of contents or summary of what the IPS will include and will also identify the specific assets governed by the IPS. The definition of duties identifies possible key stakeholders, those individuals or groups with fiduciary responsibilities, and may outline how they are accountable toward the assets governed by the IPS. Finally, the investment philosophy outlines the board's preferences and expectations for the investment process, the investment advisors, and other general considerations.



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## Common Investment Policy Statement Sections

### I. Governance

a. Purpose & Scope

b. Definition of Duties

c. Investment Philosophy

### II. Objectives & Constraints

a. Statement of Goals

b. Spending Rule

c. Return Objectives

d. Risk Tolerance

e. Time Horizon

f. Liquidity Requirements

g. Unique Circumstances

### III. Portfolio Parameters

a. Asset Allocation

b. Benchmarks

c. Selection and Retention

d. Types of Securities

e. Portfolio Rebalancing

### IV. Risk Management

a. Control Procedures

b. Performance Objectives

### V. Client Service

a. Communications

b. Reporting

### VI. Acknowledgement of IPS

**Purpose and Scope** – This section should clearly state the general goals and objectives of the organization and of the investment policy statement. Providing a clear understanding of the purpose of the funds can help the Investment Advisor to meet your organization's investing objectives.

This section may further detail what assets are covered by the Investment Policy Statement: specifically, which assets should comply with the strategic asset allocation set forth within the document.

**Definition of Duties** – The definition of duties outlines the roles and responsibilities of boards and staff. Some of the more important responsibilities to identify individuals or groups accountable for include:

- Developing and executing Investment Policy
- Development and affirmation of capital market assumptions inputs
- Preparation and review of Investment Performance & Risk management reports
- Annual review and updates to Investment Policy Statement
- Selecting and removing consultants and investment advisors

It is necessary for the Investment Policy Statement (IPS) to enumerate clearly the responsibilities and expectations of all parties involved. Some of the main parties and responsibilities may include:

- I. Board of Directors/Trustees** – This section lists what responsibilities come under the Board of Directors. Typically, such responsibilities include fiduciary responsibility for the investment portfolio and general responsibility for maintaining and reviewing the IPS for accuracy and relevancy. Ultimately, the Board is accountable to care for and protect the assets as established by the guidelines of the IPS.
- II. Investment Committee** – This section identifies the Investment Committee's responsibilities, which typically include hiring and firing Consultants and/or Investment advisors, reviewing fund performance, providing oversight and coordination of assets while in the Investment advisor(s)' care, and implementing the Investment Policy Statement in a timely and accurate manner. If there is no Investment Committee, these responsibilities fall to the Board of Directors.



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**III. Asset Management Firm** – An asset management provider is responsible for guiding the Board of Directors and/or Investment Committee in all areas of investing that relate to the assets being managed. These include, but are not limited to, recommendations for and review of the Investment Policy Statement, asset allocation, ongoing investment manager selection (internal or external), portfolio review, and performance assessment. In addition, it is important to determine whether fiduciary responsibility is shared.

**IV. Investment Advisor** – The investment advisor executes the IPS. The Investment Committee should specify exactly what the Investment Advisor is being hired to do in addition to the level of discretion and authority the Investment Advisor has over the portfolio. Whether tasked with maintaining a diversified portfolio or a implementing a single strategy, the Investment Advisor is responsible for investing within the confines of the IPS. In some cases, a Consultant may also serve as an Investment Advisor.

**V. Custodian** – The custodian is in charge of safeguarding specific financial assets. Toward this end, responsibilities might include, controlling access, settling trades efficiently, collecting investment income and principal, and/or collecting and disseminating investment portfolio performance.

**Investment Philosophy** – It is important to establish expectations at the onset of any endeavor. Without expectations, it is impossible to measure success or the attainment of goals. This section should outline the expectations of the board for both the parts and the whole of the investment assets, covering the process, expected behavior, and the definition of success. A few topics we recommend to discuss include:

- The need for and benefits of diversification across asset classes
- Expectations of active managers and passive managers
- How risk management is defined, executed, and reviewed
- The inclusion or exclusion of alternative investments

These expectations and beliefs may be specific to your organization. By defining them, your organization will be properly able to measure success.

## Part Two: Objectives and Constraints

An investor's long-term strategic asset allocation (SAA) is the culmination of two work sets: a) capital market expectations, and b) objectives and constraints. An investment advisor may work with an investment strategist to produce the former, but the latter requires input from your organization.

When defining objectives and constraints, we recommend certain categories be addressed: statement of goals, return objective, risk tolerance, time horizon, liquidity requirements, and unique circumstances. In this part, we will address what we believe may be appropriate to consider when defining these factors.

**Statement of Goals** – For institutional investors, especially endowments and foundations, investment objectives are generally to provide a permanent asset base of funding specific activities or at a minimum meeting required spending rules. There is also a necessity to preserve real purchasing power and cover investment expenses.

Furthermore, the investment objectives should be sufficiently specific to be meaningful, but adequately flexible to be practicable. These objectives are designed to establish an attitude and philosophy that will guide the investment advisors toward the desired policies and performance.

**Spending Rule** – This section is applicable to investment programs that are intended to fund a distribution. We recommend that the Board and the Investment Committee adopt a spending rule, by defining the amount of Fund distributions, to instill discipline into the budgeting and financial management process. A spending rule will assist the Board and Investment Committee in determining the Fund's required rate of return and risk tolerance objectives, which in turn may lead to less volatile distributions from year-to-year and improve the visibility of distributions. When it comes to determining the target distribution, there are generally three main spending rules to consider:



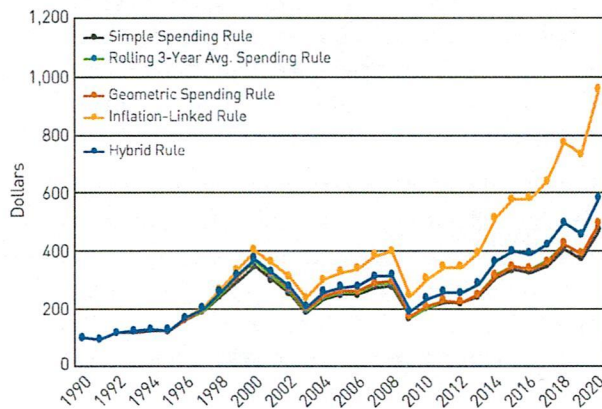
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- Simple Spending Rule: Spending is equal to the specified spending rate multiplied by the beginning period market value.
- Rolling 3-Year Average Spending Rule: Spending is equal to the spending rate multiplied by an average of the three previous years' market values. This method reduces the volatility of required distributions from year to year.
- Geometric Spending Rule: Spending in the current period is equal to a) Previous year's

distribution adjusted for inflation times a smoothing rate (used to further reduce volatility, i.e., 0.7); plus b) the beginning market value of the portfolio times the spending rate and the residual of the smoothing rate (i.e.,  $0.3 = 1 - 0.7$ ).

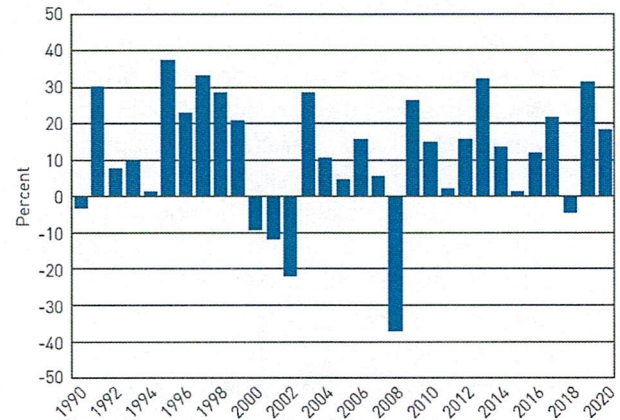
The charts<sup>1</sup> below are to illustrate the how the Rolling Three Year Average and Geometric Average Spending Rule smooth out the payments from year to year. An important point is that in years of consecutive market

Chart 1  
**Portfolio Value (\$Millions)**  
As of 12/31/20



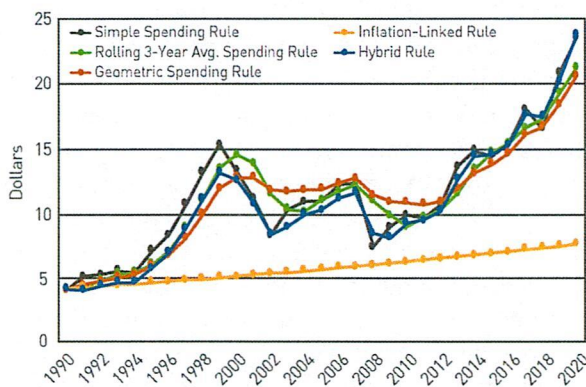
Source: FactSet® Research Systems Inc.

Chart 2  
**S&P 500 Annual Return**  
As of 12/31/20



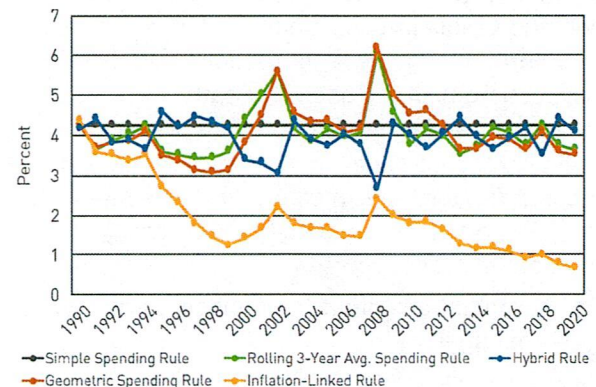
Source: FactSet®

Chart 3  
**Annual Spending (\$Millions)**  
As of 12/31/20



Source: FactSet®

Chart 4  
**Spending as % of Beginning Portfolio Value**  
As of 12/31/20



Source: FactSet®

<sup>1</sup> Assumes \$100 million portfolio invested 100% in S&P 500® at beginning of 1989 and follows the three different spending rules. In the hypothetical example, which is meant solely to illustrate the differences in the spending values over time, the spending rate is 5%. For the Geometric return, the annual inflation rate = 2%, and the smoothing rate = 70%.



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declines, the annual spending of an institution may be higher than the simple spending rule because of the weight placed on higher portfolio values.

There are pros and cons to all three methods.

The simple spending rule is easy to understand, but can lead to volatile distributions. The rolling 3-year average spending rule can reduce the volatility of distributions, but might lead to an outsized distribution in years where the market value has declined significantly. The geometric spending rule can be complicated to calculate, but reduces the volatility of distributions even further and, with a smoothing rule, can reduce the impact of a significant market decline on the annual distribution. The differences between these three rules is especially apparent in 2003 and 2009, on both the annual spending and spending as a percentage of beginning portfolio value (as seen in the charts above).

**Return Objective** – The investment objective and return requirements should clearly define what the organization is hoping to accomplish over a full market cycle and/or multiple market cycles. It is also sometimes important for the spending policy to be considered when setting a return target. Precisely outlining the organization's needs for growth and liquidity helps the investment advisor determine and execute a strategy to achieve the objective(s).

Spending Rule	< 4.25 of Market Value → 1.0425
Inflation	< 2% over the Long Term → 1.0200
Fees	< 0.50% of Market Value → 1.0050
Return Objective	= $[(1.0425) * (1.02) * (1.005)] - 1 = 6.6867\%$

Thus, for the example, the return objective would be [rounded to] 6.69%. By solving for the return objective this way, the organization will have an absolute benchmark for measuring the success of the investment program at meeting its distributions while preserving real purchasing power.

**Risk Tolerance** – Endowments and foundations can generally tolerate more risk relative to other institutions such as pension funds, insurance companies, and hospitals. This is because the investment management can focus solely on the assets of the endowment or foundation and the spending needs, while pension plans, insurance companies, and hospitals have liabilities that must be taken into consideration.

Unlike required return, which an organization can solve for quantitatively, evaluating risk tolerance is one area that may be difficult to assess. This difficulty is exacerbated by the need to aggregate the risk preferences of many board members.

A key principle of determining the risk tolerance for an organization involves assessing “willingness vs. ability.” Even if every member of the board is willing to reach out as far as possible on the risk scale, the appropriate level of risk may not exceed the ability of the fund given a proper assessment of the funds constraints. With this in mind, the risk tolerance section should speak clearly to the acceptable level of risk in as granular a level of detail as necessary, while remaining within prudent levels of practicality.

An example of a risk tolerance statement is as follows:

*“It is understood that an endowment or foundation must generally be more aggressive on the risk tolerance scale in order to meet return requirements; however, the Investment Advisor(s) are expected to seek to minimize risk against the return objective.”*

**Time Horizon** – Your organization should state in this document whether or not the time horizon is perpetual. A perpetual time horizon that provides a permanent source of funding is likely to be the case for most endowments and foundations. This indefinite time horizon is one of the reasons risk tolerance can be higher for endowments and foundations than for institutions that are more liability centric.

**Liquidity Requirements** – With endowments and foundations, liquidity requirements are normally low, but will ultimately vary by institution. Generally, the risk tolerance of a portfolio decreases as the uncertainty around spending and liquidity requirements increase.

**Unique Circumstances** – In this section, an organization can list any special objectives, constraints, rules around abnormal distributions (i.e., for emergency purposes), or any other policies that could affect the investment program. An example of this is socially responsible investing (SRI): here the organization would list any preferences, such as following the US Conference of Catholic Bishops (USCCB), that they expect the investment advisor and/or investment manager(s) to follow. This section can also include whether or not the investment program is allowed to invest in



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alternative assets, in addition to any policies around the approval process (i.e., if the board needs to approve each alternative investment).

## Part Three: Portfolio Parameters

This section of the Investment Policy Statement (IPS) should lay out the investment process: the strategic asset allocation and benchmarks, rules for manager selection and retention, the types of securities allowed, and rules for portfolio rebalancing.

### Strategic Asset Allocation and Benchmarks –

We recommend that the target asset allocation reflect both the organization's long-term strategic view and the stated goals for the designated funds. How specific the asset allocation guidelines are will vary by organization. Some organizations may prefer broad parameters, setting targets for equities, fixed income and cash. Other organizations may be more precise, segmenting the major asset classes into smaller categories such as large cap, mid cap, and small cap equity. This section of the IPS may also set restrictions on how much or how little an investment advisor may deviate from the allocation target for a given asset class or category; with that said, restrictions should be considered carefully given that there are potential benefits to allowing investment advisors to tactically allocate assets on the basis of prevailing market opportunities and conditions. While narrow ranges may overly restrict asset managers, too much latitude may allow asset allocation to deviate from the overall investment objective.

We also recommend using this section to establish the benchmarks for measuring the relative performance of each asset and sub-asset class. Further, we recommend establishing an absolute benchmark, or hurdle rate, which serves as a measure of success in meeting the overall goals of the investment program. Investment returns below the absolute benchmark would imply the program is failing to meet its objective, above this number would imply that it is meeting its objective.

### Selection and Retention Criteria for Investments –

Managers should be given discretion to manage the funds entrusted in accordance with the style for which they are employed, provided that they comply with the restrictions and limitations set forth in the IPS. Important criteria for selection may include:

the investment style and discipline of the proposed manager; past performance, considered relative to other benchmarks and other strategies having the same investment objective; historical volatility and down-side risk management; the size of the organization as measured by the amount of assets under management with respect to the investment style under consideration; length of the manager's track record; and the experience of the organization as measured by the tenure of the professionals with respect to the investment style under consideration.

**Types of Securities Allowed –** While risk and volatility are present with all types of investments, it should be stated that high levels of relative risk are to be avoided in every asset class. Diversification by asset class, sector, industry and issuer limits, maturity limits and, to the extent possible, management style can be used to reduce risk. We recommend that this section also clearly outline investments that are prohibited, as well as any other restrictions such as types of securities, weighting limits, quality standards, or liquidity requirements. Further, if mutual funds are utilized, their investment objectives should be consistent with the investment guidelines set forth in the IPS.

Exclusions and limitations can help reduce risk, but they also reduce the investment opportunities available to managers. With that said, a list of prohibited investments can proactively prevent the inclusion of security types that the board/investment committee is not familiar with and/or does not desire, as an example for Socially Responsible Investing purposes, to include in the portfolio.

**Portfolio Rebalancing –** The purpose of rebalancing is to maintain the asset allocation within the ranges set around the strategic baseline. This section may specify how often the portfolio is rebalanced, in addition to how much discretion the investment advisor(s) have in managing asset class weight drift from the targets established in the strategic asset allocation. We recommend outlining the procedure that the investment advisor should follow for remedying weight drift outside of the ranges. In certain circumstances it may make sense for the weights to remain outside of the targeted ranges for a period of time. In these cases, the IPS should provide a procedure by which the Board/ Committee would approve these temporary deviations from the policy.



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## Part Four: Risk Management

This part may cover both the operating and investment risks of the investment program. We recommend that the control procedures section discuss the schedule of reviewing the portfolio for both performance and compliance. Performance objectives should define how “success” for the investment program will be measured.

**Control Procedures** – In this section, the Investment Committee may reiterate its performance expectations in addition to establishing a schedule to review the portfolio and performance with the investment advisor(s). This section can also make clear what performance periods are important to the organization: while performance may be best measured over full market cycles, as it may more accurately reflect progress toward the organization’s stated goals, analysis of shorter time periods may help explain the impact that certain investments are having on the portfolio.

Furthermore, it is important to herein state the focus of the reviews, including topics such as: investment advisor(s)’ adherence to the policy guidelines; comparison of results to the benchmark(s); material changes in the Investment Advisor(s)’ organizations, such as philosophical or personnel changes. Along the same lines, it may be stated here the circumstances for which termination of an investment advisor will be considered, such as: deviation from the IPS guidelines; deviation [substantially] from investment disciplines and process; or when the client’s representatives have any material problem or concern regarding the investment advisor(s).

**Performance Objectives** – The fund’s investment performance should be reviewed regularly, such as on an annual basis; however, the emphasis with regard to performance should be focused on results achieved over a full market cycle (typically a three-to-five year period). Furthermore, overall policy and investment objectives should be reviewed on at least an annual basis and adjusted, if necessary, after consultation with the appropriate parties.

We recommend that advisor and manager performance be measured against policy objectives and for consistency with the total return objectives, evaluated on a net-of-fees basis. With regard to

benchmarking, the overall portfolio should be measured against an appropriate, often blended, index that measures both the return and risk profile of the portfolio. This blend should be based on the strategic allocation, incorporating the target levels of equity, fixed income, and/or alternative assets comprising the portfolio.

## Part Five: Client Service

This section may include what your organization expects from the investment advisor(s) and/or consultant with respect to communications and reporting. This section may also address the frequency of in-person meetings and the method(s) of communication. Clearly establishing these expectations at the onset can help a board to better manage the investment program and lead to better interactions between the organization and those assigned to manage the organization’s assets.

**Communications** – As earlier discussed, it is important that the investment advisor(s) provide performance evaluations on a regular basis. This section may require that the managers provide regular accounting of transactions, portfolio holdings, yields, current market values, summary of cash flows, and calculations of the portfolio’s total rate of return.

It is additionally important that a reasonable, baseline frequency of communication be established, such as on the basis of “as market conditions and the portfolio warrant,” to ensure full transparency. Along these lines, it may be stated that significant changes within the investment advisor(s)’ operations or personnel, and the anticipated impact on the portfolio(s), should be brought to the attention of the committee.

**Reporting** – Setting out the expectations for reporting can facilitate transparency and access between the client, investment advisor(s), and all other relevant parties. With this in mind, a schedule for reports containing portfolio activity and asset holdings, in addition to tactical and strategic updates, may be established at the onset of the relationship. The language may also further specify that the investment advisor(s) are responsible for frequent and open communication with regard to all significant matters pertaining to the investment of assets.



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With regard to the schedule of reporting and account reviews, it is important that the schedule is framed around reasonable and appropriate timing. End of quarter and end of year reports take time to produce: reviews and reports scheduled soon after a period's end will necessarily lack some of the details and clarity that reports scheduled later on can provide. We recommend balancing the need for urgency with the level of detail desired, accounting for the fact the two are sometimes mutually exclusive.

## Part Six: Acknowledgement

The last part of the IPS should document the organization's recognition of the importance of following the guidelines, rules, and best practices incorporated within the document. A sample acknowledgment would be as follows:

*We, the undersigned, recognize the importance of adhering to the mission and strategies detailed in this policy and agree to work to fulfill the objectives stated herein, within the guidelines and restrictions, to the best of our ability.*

Thus the acknowledgment signifies all parties as having read the investment policy statement and states the mutual intention to follow both the letter and the spirit of the document.

## Conclusion

In summary, the points to address include naming those with fiduciary responsibilities, documenting objectives and constraints, outlining a strategic asset allocation, defining how success is measured, and setting standards and a schedule around performance reviews.

Every Investment Policy Statement should address the preceding points in some detail. When addressing each point, the organization should be certain to set forth not only "what," but also "why." Once a draft of the statement is complete, the entire document should be carefully reviewed to identify and resolve inconsistencies. When all points are consistent and the organization's leadership is in agreement, they should adopt the final document.

Thus, the IPS may serve as the blueprint for institutional investment programs. In addition, it may serve as a foundation for the organization's overall governance structure and ensure that all fiduciaries are fulfilling their responsibilities and obligations. At PNC, we believe that a document created with such a level of care will result in an investment experience that is fully integrated and aligned with the needs and objectives of the overall organization, thus increasing the likelihood and probability of success over the long term.

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## Sample Investment Policy Statement

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### Endowments & Foundations

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**[Name of Endowment or Foundation]**

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Investment Policy Statement

[Adopted \_\_\_\_\_]

The managed assets of [Name of Organization] ("Organization") will consist of an [name of fund type here] (the "Fund"). It is the intention of the [BOARD OF DIRECTORS/TRUSTEES] (the "Board") that the Investment Committee of the Organization (the "Investment Committee") ensure that the Fund will be managed toward [\_\_\_\_\_, while simultaneously meeting the objectives set forth in this Investment Policy Statement.

The Investment Committee is charged with oversight of the management of the Fund in a manner which builds upon the existing assets and furthers growth of the Organization without exposing the assets to excessive risk. The primary objective of the Investment Committee should be [\_\_\_\_\_, with secondary goals of [\_\_\_\_\_] and [\_\_\_\_\_].<sup>1</sup>

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<sup>1</sup> Your Organization's goals should be tailored by the Board and Investment Committee to reflect the unique circumstances of the Organization. A few goals you may consider include: preservation of purchasing power; growth & income; and preservation of capital.



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## Governance

This Investment Policy Statement ("IPS") serves as a strategic guide in the planning and implementation of an investment program for the Organization and governs the investments associated with [describe specific assets in the Fund].

### I. Purpose and Scope

This IPS should establish a clear delineation of the expectations of the Board with respect to the Investment Committee's and the Investment Advisor(s)' oversight and management of the Fund.

This IPS is intended to:

- Define the investment assets to be governed by the IPS and allocation of duties among the Board, Investment Committee and the Investment Advisor(s) with respect to such assets;
- Establish reasonable objectives for return and risk expectations, incorporating the following constraints: current time horizon; liquidity constraints; and any other unique circumstances regarding the Fund;
- Establish the appropriate target allocation and the parameters around restricted security types and asset classes;
- Establish an appropriate portfolio benchmark for the evaluation of investment performance and risk management;
- Establish expectations for investment and money managers, securities guidelines, and for the monitoring of the selected managers;
- Provide a basis for risk management and the evaluation of the investment performance of the Fund's assets at the manager level;
- Encourage effective communication between all parties involved in the oversight, management and operations of the Fund(s).
- Establish the Board's and the Investment Committee's expectations regarding reports to be delivered by the Investment Advisor(s) and the frequency of meetings with the Investment Advisor(s).

Further, this IPS is intended to provide investment objectives that are sufficiently specific to be meaningful, but adequately flexible to be practicable. The objectives in this IPS are designed to establish an attitude and philosophy to guide the Board and the Investment Committee toward the desired policies and performance in oversight of the Organization's assets.

### II. Definition of Duties

POSITION	GENERAL RESPONSIBILITY	SPECIFIC TASKS
Board of Directors	Oversees corporate policy and investment process	<ul style="list-style-type: none"><li>➤ Appoints Investment Committee</li><li>➤ Authorizes and approves changes to the Investment Policy Statement</li></ul>
Investment Committee	Coordinates investment activities, institutional direction, and strategic initiatives	<ul style="list-style-type: none"><li>➤ Oversees management of the investment portfolio</li><li>➤ Coordinates periodic asset allocation review</li><li>➤ Reviews and recommends revisions to the IPS</li><li>➤ Reviews Fund transactions and holdings</li><li>➤ Reports investment results to the Board on a quarterly basis</li><li>➤ Retains/dismisses custodians and Investment Advisor(s)</li></ul>



## II. Definition of Duties (continued)

POSITION	GENERAL RESPONSIBILITY	SPECIFIC TASKS
<b>Investment Advisor(s)</b>	Supports the Board and Investment Committee in the development and execution of investment strategy	<ul style="list-style-type: none"> <li>➤ Complies with the investment policy, guidelines, and restrictions</li> <li>➤ Constructs / revises the investment policy and guidelines</li> <li>➤ Recommends asset classes and asset allocation ranges / targets</li> <li>➤ Seeks return within acceptable risk parameters</li> <li>➤ Provides capital markets / asset class information as needed</li> <li>➤ Rebalances the Fund, as appropriate</li> <li>➤ Generates desired performance reports</li> <li>➤ Supports Investment Committee requests</li> <li>➤ Retains / dismisses investment and money managers for the Fund</li> </ul>
<b>Custodian Bank</b>	Safeguards specified financial assets	<ul style="list-style-type: none"> <li>➤ Controls access to assets</li> <li>➤ Settles trades efficiently</li> <li>➤ Collects investment income and principal</li> <li>➤ Collects and disseminates fund statements</li> <li>➤ Provides book of record, audit, and tax information</li> </ul>

The Investment Committee will be responsible for adopting a recommendation for the Fund's investment strategy and overall Fund management, as set forth in this IPS. The Investment Advisor(s) will be responsible for the recommendation of an investment strategy, and, once adopted, the management and implementation of the selected strategy.

The Board and Investment Committee recognize that this IPS requires periodic reexamination and, if necessary, revision, if it is to continue to effectively produce the intended strategic results. If it is determined that this IPS needs to be amended, it is the mutual responsibility of the Investment Advisor(s) and the Investment Committee to initiate written communication to effect such change.

## III. Investment Goals & Philosophy

The Organization has periodically reviewed and confirmed its investment goals and philosophy, which are set forth below:<sup>2</sup>

- Clear and systematic decision making processes deliver more consistent performance over time;
- The bias of the investable assets is toward being substantially fully invested over time;
- That equity investments will provide greater long-term returns than fixed income investments, although with greater short-term volatility;
- That it is prudent to diversify the Fund across the major asset classes;
- That investment managers with active mandates can reduce portfolio risk and potentially add value through security selection strategies;

<sup>2</sup> The goals and philosophy of each Organization are dependent upon that Organization's particular circumstances. The above list is provided only as an example of some goals / philosophies you may want to consider adopting. You should carefully consider your Organization's attributes, goals and circumstances and develop a tailored list of goals and your philosophy for the Organization.



- That passive management can be appropriate in certain asset classes, and that a portion of the Fund may be invested in passive mandates;
- That it may be appropriate to select more than one investment manager in any one asset or sub-asset class, provided that such managers can offer asset class or style diversification;
- That investments in alternative assets, such as hedge funds and private equity in both traditional (illiquid) and liquid vehicles, may provide diversification and a competitive risk-adjusted return; and,
- That it is prudent to consider the Organization's tax status (including the applicability of UBIT).

## Objectives and Constraints

This Investment Policy Statement ("IPS") serves as a strategic guide in the planning and implementation of an investment program for the Organization and governs the investments associated with [describe specific assets in the Fund].

### IV. Statement of Goals

The Board's and Investment Committee's investment objective should be focused on support for:

- [\_\_\_\_\_]
- [\_\_\_\_\_]
- [\_\_\_\_\_]

This will be achieved through a [\_\_\_\_\_] spending/distribution policy adjusted for inflation and management expenses.

### V. Spending Rules – ENDOWMENTS ONLY

The Board and the Investment Committee should adopt a spending rule, by defining the amount of Fund distributions, to instill discipline into the budgeting and financial management process. A spending rule will assist the Board and Investment Committee in determining the Fund's required rate of return and risk tolerance objectives, which in turn may lead to less volatile distributions from year-to-year, and improve the visibility of distributions.

#### **[Choose one]**

#### **[Simple Spending Rule]**

The long-term annual spending and distributions from the Fund are targeted to average \_\_\_\_\_ (xx%) of the beginning period market value of the Fund. However, spending and distributions may occasionally exceed this amount as necessary as determined by [\_\_\_\_\_].

#### **[Rolling Three-Year Average Spending Rule]**

While the long-term annual spending and distributions from the Fund are targeted to average \_\_\_\_\_ (xx%) of a moving 12-quarter market value average of the Fund, spending and distributions in any one fiscal year may range between a minimum of \_\_\_\_\_ percent (xx%) and a maximum of \_\_\_\_\_ percent (xx%). However, spending and distributions may occasionally exceed this amount as necessary as determined by [\_\_\_\_\_].



### ***[Geometric Spending Rule]***

The long-term annual spending and distributions from the Fund are targeted to average \_\_\_\_\_ (xx%). Spending in the current period is equal to a) Previous year's distribution adjusted for inflation times a smoothing rate of [\_\_\_\_\_]; plus b) the beginning market value of the portfolio times the spending rate and the residual of the smoothing rate [\_\_\_\_\_]. However, spending and distributions may occasionally exceed this amount as necessary as determined by [\_\_\_\_\_].

## **VI. Return Objectives**

The long-term return objective is to preserve the real value of the Fund assets while supporting the spending policy and management expenses.

### ***[Private Foundation]***

The Fund will need to achieve a minimum compounded (nominal) return objective of [\_\_\_\_], which includes a required 5% annual distribution, investment management fees, overhead expenses, and inflation, based on the rolling 3-year average asset value of the portfolio.

### ***[Endowment]***

The portfolio will be required to fund a long-term, inflation-adjusted annual spending rate of [\_\_\_\_], consistent with the spending rule defined above, in order to maintain the purchasing power of the principal over the long-term.

## **VII. Risk Tolerance**

The Investment Committee is expected to cause the Fund to be diversified in order to minimize the risk of large losses and to manage volatility of asset classes and investment styles. The Investment Advisor(s) are expected to invest Fund assets in accordance with the standard of care set forth in the investment management agreement between such Investment Advisor(s) and the Fund and to seek reasonable diversification where possible.

The Organization recognizes that, over the long term, the risk of owning equities has been and is expected to continue to be rewarded with a relatively greater return than what has been historically available from fixed income investments. The role of fixed income investments is to reduce the volatility of the overall portfolio, while providing a predictable stream of income. The Organization expects the Investment Committee to follow these accepted investment principals in oversight of the assets of the Fund.

It is understood that an endowment or foundation must generally be more aggressive on the risk tolerance scale in order to meet return requirements, however, the Investment Advisor(s) are expected to seek to minimize risk against the return objective.

## **VIII. Time Horizon**

Except with regard to portions of the Fund explicitly set aside to fund specific projects, the time horizon for the investment assets will be assumed to be perpetual.



## IX. Liquidity Requirements

Generally, the Board expects that the Investment Committee will determine the Organization's anticipated spending needs and the amount that should be held in a cash reserve and excluded from investable assets. The Investment Committee has determined that [ ] months of cash should be held in reserve for distribution or emergency purposes and will instruct the Investment Advisor(s) accordingly.

## X. Unique Circumstances

[Client Specific]

## Portfolio Parameters

## XI. Strategic Asset Allocation and Benchmarks

The Investment Committee believes that the most significant decision to affect the ability of the Fund to meet its objectives is asset allocation. In the event there are two or more Investment Advisors, this Section XI shall be implemented and monitored by the Investment Committee with respect to the Fund as a whole, and by each Investment Advisor with respect to the portion of assets of the Fund being managed by that Investment Advisor (each a "Portfolio"). With that in mind, and based on the investment objectives and risk tolerances stated herein, the following asset mix targets and ranges are considered appropriate:

Asset Class	Minimum	Target	Maximum	Evaluative Index
U.S. Equity				
Large Cap				
Mid Cap				
Small Cap				
REITs				
Non-U.S. Equity				
Developed				
Emerging				
Global				
U.S. Fixed Income				
Short				
Intermediate				
Long				
High Yield				
Non-U.S. Fixed Income				
Developed				
Emerging				
Global				
Alternatives				
Hedge Funds				
Private Equity				
Private Debt				
Private Real Estate				
Natural Resources				
Cash or Cash Equivalents				



It is the responsibility of the Investment Advisor(s) to monitor asset allocations and to make adjustments in their Portfolios, as necessary, to achieve on-going allocation consistency with the guidelines for the Portfolio set forth in this IPS. It is the responsibility of the Investment Committee to monitor asset target allocations with respect to the Fund as a whole to maintain compliance with the objectives set forth in this IPS.

## **XII. Selection and Retention Criteria for Investments**

The Investment Committee will appoint Investment Advisor(s) following a systematic search for those with demonstrated skill in the discipline desired. Investment Advisor(s) will have discretion to manage their respective Portfolios in accordance with the style for which they are employed, subject to the restrictions and limitations in this IPS.

Investment funds and managers will be chosen and retained by the Investment Advisor(s) using criteria including, but not limited to, the following:

- The investment style and discipline of the proposed Investment Manager
- Past performance, considered relative to benchmarks having the same investment objective – consideration shall be given to both rankings over various time frames and consistency of performance
- The historical volatility and down-side risk of each proposed investment
- The size of the organization as measured by the amount of assets under management with respect to the investment style under consideration
- Experience of the organization as measured by the tenure of the professionals with respect to the investment style under consideration

The Investment Advisor(s) will monitor managers for consistent investment process, performance, and risk including but not limited to key man and operational risks.

With regard to managers with active mandates, their selection and retention within the portfolio will be predicated on whether or not they fulfill the purpose for which they were selected. If the purpose is:

- risk management, the manager will be evaluated as to how well downside protection is provided and at what cost to upside participation;
- security selection, the manager will be evaluated relative to an appropriate benchmark.

The Investment Advisor(s) will monitor active managers and mandates to determine whether or not value is added relative to the intention or to a passive mandate. If the Investment Advisor(s) determine that it is not, a passive investment vehicle will be selected for that part of the allocation.

## **XIII. Types of Securities**

The Board and Investment Committee recognize that risk and volatility is present with all types of investments and, in performing their respective fiduciary duties for the Organization, they should avoid high levels of relative risk in every asset class. To this end, the Investment Committee should ensure that the Fund manages risk appropriately through diversification by asset class, sector, industry and issuer limits, maturity limits and, to the extent possible, management style. If mutual funds are utilized, their investment objectives should be consistent with this IPS.



### Restricted Investments:

The limitations and restrictions in this section shall be implemented and monitored by the Investment Committee with respect to the Fund as a whole and by each Investment Advisor with respect to their Portfolio. With the exception of being within pooled investment vehicles, direct exposure to the following strategies and types of securities is prohibited:

- oil and gas wells;
- interest only securities;
- warrants;
- principal only securities;
- margin trading; and,
- inverse floating rate securities.

## XIV. Portfolio Rebalancing

The purpose of the rebalancing is to help control risk and maintain asset allocation within the ranges set forth in this IPS. The Investment Committee will be responsible for keeping the Fund as a whole, and Investment Advisor(s) will be responsible for keeping their Portfolio, within the established tolerance levels around the targeted strategic asset allocation. While it is at the Investment Advisor(s) discretion as to the frequency with which they rebalance their Portfolio to the targeted levels, it is understood that asset weight drift that exceeds the tolerance thresholds will be promptly corrected.

## Risk Management

## XV. Control Procedures

### Review and Evaluation of Investment Objectives

The achievement of the investment objectives in this IPS shall be reviewed at least on an annual basis by the Investment Committee. This review will focus on the continued feasibility of achieving the objectives and the continued appropriateness of this IPS. It is not expected that this IPS will change frequently. In particular, short-term changes in the financial markets should not require an adjustment in the IPS.

### Review and Evaluation of Investment Advisor(s):<sup>3</sup>

The Investment Committee will meet periodically with the Investment Advisor(s) or their representative(s). Additionally, with or without the Investment Advisor(s), the appropriate committees will review investment results on an established basis.

These reviews will focus on:

- The Investment Advisor(s)' adherence to this IPS;
- Comparison of the Investment Advisor(s)' results to the benchmark established for their Portfolio;
- Material changes in the Investment Advisor(s)' investment philosophy or changes in personnel managing the Fund.

<sup>3</sup> The Review and Evaluation criteria for Investment Advisor(s) should be carefully reviewed and considered by the Board and the Investment Committee. The list above contains examples of criteria, but each Organization should consider its unique circumstances and goals and tailor this criteria to meet your specific needs.



Termination of an Investment Advisor should be considered under the following circumstances:

- Deviation from this IPS.
- Deviation substantially from the Investment Advisor(s)' investment disciplines and process.
- Identification of by [ ] of a material problem or concern regarding the Investment Advisor.

## **XVI. Performance Objectives**

The Fund's and each Portfolio's investment performance will be reviewed on a quarterly basis, with long-term emphasis placed on results achieved over a full market cycle (typically three-to-five year period). This IPS will be reviewed annually and adjusted, if necessary, after consultation with the Investment Committee. Investment Advisor progress will be measured against this IPS and for consistency with the total return objectives for the Advisor's Portfolio; performance will be reflected net of management fees.

With regard to performance benchmarking, the Fund and each Portfolio will be measured against a blended index of the component parts used to measure the equity, fixed income, and alternative asset allocations, as/if applicable. This blend will be weighted by the targeted strategic allocation proposed for the Fund and each Portfolio, as outlined in this IPS.

## **Client Service**

## **XVII. Communication**

The Investment Advisor(s) are responsible for frequent and open communication with the Investment Committee on all material matters pertaining to the investment of the Fund.

The Investment Advisor(s) will promptly notify [ ] of changes in market conditions which may materially impact the Fund. [ ] will notify the Investment Advisor(s) promptly of any changes in the Fund or this IPS.

## **XVIII. Reporting**

The Investment Advisor(s) will provide comparative performance evaluation reports on a quarterly basis. In addition, the Custodian will provide quarter-end regular accounting of transactions, Fund holdings, yields, current market values, summary of cash flows, and calculations of the Fund's total rate of return.

The Investment Advisor(s) and/or Custodian will forward to [ ], as they become available, monthly reports containing Fund activity and asset holdings at book and market values. Quarterly, the Investment Advisor(s) should submit tactical and strategic updates regarding the Fund's management for performance evaluation purposes.



## Acknowledgment of IPS

### XIX. Adoption of Investment Policy Statement

The [Name of Organization] certifies that this Investment Policy Statement was adopted by the Organization's Investment Committee on [\_\_\_\_\_].

[Organization]

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_

By: \_\_\_\_\_

Name: \_\_\_\_\_

Title: \_\_\_\_\_



## Acknowledgement By Investment Managers

The Investment Manager named below acknowledges receipt of the [Name of Organization] Investment Policy Statement, dated [\_\_\_\_\_]. In the event any of the terms of the Investment Policy Statement conflict with the terms and conditions of an investment management agreement or custody agreement entered into between the Organization and the Investment Manager the terms of the investment management or custody agreement shall govern.

[NAME OF INVESTMENT MANAGER]

\_\_\_\_\_  
Date

\_\_\_\_\_  
Signature

[Create a separate acknowledgement page for each Investment Manager]

“ The Investment Policy Statement depicted is for illustrative purposes only. PNC believes in crafting a customized IPS designed to meet each client’s unique needs. To learn more, please contact your PNC Representative. ”

For definitions of indexes used in this publication, please refer to [pnc.com/indexdefinitions](http://pnc.com/indexdefinitions).

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