

# **Episcopal Diocese of Rochester**

## ***Endowment Funds***

### **INVESTMENT POLICY STATEMENT**

#### **Statement of Principles & Policy**

**Amended February 24<sup>th</sup>, 2018**

### **Purpose of Investment Policy Statement:**

- ❖ Establishes the Investment Committee's **expectations, objectives and guidelines** in the investment of the Portfolio's assets.
- ❖ Creates the framework for a **well-diversified asset mix** that can be expected to generate acceptable long-term returns at a level of risk suitable to the Investment Committee, including:
  - describing an appropriate risk posture for the investment of the Portfolio
  - specifying the target asset allocation policy
  - establishing investment guidelines regarding the selection of investment managers, permissible securities and diversification of assets
  - specifying the criteria for evaluating the performance of the Portfolio's assets
- ❖ **Defines the responsibilities** of the Investment Committee, Advisor and Investment Manager(s).
- ❖ **Encourages effective communication** between the Investment Advisor and the Investment Committee.
- ❖ Meet the fiduciary obligations of the Investment Committee with respect to the management and investment of the Portfolio, consistent with applicable state law under New York Prudent Management of Institutional Funds Act ("NYPMIFA").

*This policy is intended to be a summary of an investment philosophy and the procedures that provide guidance for the Investment Committee. The investment policies described in this document should be dynamic. These policies should reflect the Investment Committee's current status and philosophy regarding the investment of the Portfolio. These policies will be reviewed and revised periodically to ensure they adequately reflect any changes related to the Portfolio, to the Investment Committee or the capital markets.*

### **Guiding Principals**

Management of the Portfolio will follow the general investment guidelines set forth below:

1. Investments shall be made solely in the interests of the Episcopal Diocese of Rochester, consistent with the duty of loyalty required by law.
2. The Portfolio shall be invested with the care an ordinarily prudent person in a like position would exercise under similar circumstances. In particular in managing and investing the Portfolio, the following factors, if relevant, must be considered: general economic conditions; the possible effect of inflation or deflation; the expected tax consequences, if any, of investment decisions or strategies; the role that each investment or course of action plays within the overall investment assets of the Portfolio; the expected total return from income and the appreciation of investments; other resources of the EDOR; the needs of EDOR and the Portfolio to make distributions and to preserve capital; and an asset's special relationship or special value, if any, to the purposes of the Portfolio.

3. Investment of the assets shall be so diversified as to minimize the risk of large losses, unless the Investment Committee prudently determines that, because of special circumstances, the purposes of the Portfolio are to be better served without diversification. The Investment Committee shall review a decision not to diversify as frequently as circumstances require, but at least annually.

4. The Investment Committee may employ investment professionals, such as an Investment Advisor, Investment Manager(s), Custodian(s) and additional specialists as may be required to attain the objectives set forth in this IPS. Any person who has special skills or expertise, or is selected in reliance upon that person's representation that the person has special skills or expertise, has a duty to use those skills or that expertise in managing and investing the Portfolio.

### **Investor Philosophy:**

Diocesan investment portfolios exist to support the current and future mission and ministry of the Episcopal Diocese of Rochester and in certain circumstances the current and future mission of its congregations and other related groups. This management on behalf of parishes recognizes that, although some congregations are 501c-3 corporations, the Canons of the church require that all assets of all congregations, missions and chapels be held in Trust for the Diocese. Faithful and responsible stewardship requires that the Diocesan investments be managed in a manner that will enable the diocese to meet both its short- and long-term objectives.

The Diocesan Trustees have the ultimate fiduciary responsibility to establish guidelines for the management of the Diocese's funds. They are also responsible for establishing a spending policy, which will provide operating income for the work of the diocese and for certain parishes, congregations, chapels, related organizations and missions. Members of the Trustees, staff of the Diocese and Investment Review Committee may not be sued, individually, when their work on behalf of the diocese is done in the capacity of the position they hold to the best of their ability. The Diocese will maintain liability insurance to cover those working on behalf of the Diocese, whether paid or volunteer.

### **Scope of Investment Policy:**

The Diocese will, from time to time, make direct investments in church and clergy related loans and mortgages. These assets are not included in nor subject to, the guidelines as set forth in this document.

### **Investment Objectives**

The investment objective for the assets under this policy is to achieve sum of inflation as measured by the CPI + 5-7%

The investment objectives addressed in this statement represent the portfolio's overall investment objectives. **The Investment Committee's objective for this investment portfolio is primary**

**emphasis on moderate capital growth with some focus on income, while avoiding excessive risk.** Most revenue for operations will come from the planned investment sales based upon a concept of total return and according to the approved annual budget need as determined by the Diocese.

The Investor feels that grants **to be made in the future are as important as grants made today.** This is consistent with the philosophy that this Endowment is to exist in perpetuity, and therefore, should provide for grant making in perpetuity. To attain this goal, the overriding objective is to **maintain purchasing power.** That is, net of spending, the objective is to grow the aggregate portfolio value at the rate of inflation over the investment horizon.

### **Risk Tolerance**

Investment theory and historical capital market return data suggest that, over long periods of time, there is a relationship between the level of investment risk assumed and the level of return that can be expected. In general, in order to attain higher returns one must accept higher risk (e.g. volatility of return).

Given this relationship between risk and return, a fundamental step in determining the investment policy for the Portfolio is the determination of the amount of risk the Trustees can tolerate.

The Investment Committee, as directed by the Trustees, desires long-term investment performance sufficient to meet the objectives. The Investment Committee and the Trustees understand that to achieve such performance the portfolio may experience periods of decline. The Investment Committee further understands that in a severe market, the potential recovery period could be extensive.

The Investment Committee understands that the managed assets must also be invested so that funds are available to meet the needs of congregations and the Diocese and provide sufficient liquidity to allow reasonable withdrawal by congregations of unrestricted funds.

Although the Investment Committee prefers to limit the portfolio's volatility, they are comfortable with fluctuations in their portfolio, and the possibility of declines in value, in order to seek to grow their portfolio over time.

Goal is to allow for risk (as measured by standard deviation) consistent with that of the composite benchmark plus or minus 5% on an average basis.

### **Time Horizon**

While it is the intent for these funds to continue on in perpetuity, the Episcopal Diocese of Rochester's objectives for this portfolio are currently anticipated to continue without significant modification for a period of: **5 years**

## Asset Allocation

After reviewing the long-term performance and risk characteristics of various asset classes and balancing the risk and rewards of market behavior, the following asset classes were selected to achieve the objectives of Episcopal Diocese of Rochester's portfolio. (Please note that other direct investments made by the diocese are not included).

<b>Asset Class</b>	<b>Minimum</b>	<b>Maximum</b>	<b>Target</b>
<b>Domestic Equity</b>	<b>35%</b>	<b>65%</b>	<b>53%</b>
<i>Large Cap</i>	25%	50%	35%
<i>Value</i>	12.5%	25%	17.5%
<i>Growth</i>	12.5%	25%	17.5%
<i>Small/Mid Cap</i>	10%	25%	18%
<i>Value</i>	5%	12.5%	9%
<i>Growth</i>	5%	12.5%	9%
<b>International Equity</b>	<b>10%</b>	<b>30%</b>	<b>17%</b>
<i>Developed Markets</i>	7%	18%	10%
<i>Emerging Markets</i>	3%	12%	7%
<b>Fixed Income</b>	<b>15%</b>	<b>25%</b>	<b>20%</b>
<b>Alternative Investments-</b>	<b>0%</b>	<b>15%</b>	<b>10%</b>
<i>Hedge Fund of Funds</i>			
<i>Real Estate Investments</i>			
<i>Commodities</i>			
<b>Cash &amp; Equivalents-</b>	<b>0%</b>	<b>10%</b>	<b>0%</b>

### ***Portfolio Returns and Volatility:***

The Trustees' willingness to accept risk and their expectation for investment growth have a direct bearing on the rate of return objective for this portfolio.

It should be recognized that the portfolio will invest in a variety of securities and that the actual weighting of these securities can and will vary. It is also important to note that future returns of the securities with the portfolio and the portfolio itself can be expected to vary from the historical returns.

### ***Updated Allocations:***

Over time, it may be desirable to amend the basic allocation guidelines, which can only be done by a majority of Trustees voting either by proxy or in person. When such changes are made, updates will be considered part of this Investment Policy Statement.

***Rebalancing Procedures:***

From time to time, market conditions may cause the Portfolio's investment in various asset classes to vary from the approved allocation.

This portfolio will be rebalanced periodically as follows:

Portfolio is rebalanced at least quarterly, to maintain the portfolio's position within the minimum and maximum limits. Annually, the Diocese will establish the spending for the period and that schedule will be provided to the advisor to raise funds, under the discretionary powers granted to them, as they see fit.

Tactical rebalancing to position the portfolio to benefit from the current market environment may be employed at any time within the constraints of this investment policy.

***Adjustment in the Target Allocation:***

Modifications to the approved allocation may be needed from time to time for a variety of reasons. When such a change to the approved allocation needs to occur, it shall only be made with the concurrence recommendation of the Investment Committee and the approval of the Trustees, which may be electronically gathered.

***Investment Philosophy***

*The basic tenets under which this Policy will be managed include the following:*

**Modern Portfolio Theory** will be the philosophical foundation for how the portfolio will be structured and how subsequent decisions will be made. The underlying concepts of Modern Portfolio Theory include:

- Investors are risk averse. The only acceptable risk is that which is adequately compensated by potential portfolio returns.
- Markets are efficient. It is virtually impossible to anticipate the future direction of the market as a whole or of any individual security. It is, therefore, unlikely that any portfolio will succeed in consistently "beating the market".
- The design of the portfolio as a whole is more important than the selection of any particular security within the portfolio. The appropriate allocation of capital among asset classes (stocks, bonds, cash, etc.) will have far more influence on long-term portfolio results than the selection of individual securities. Investing for the long term (preferably longer than ten years) becomes critical to investment success because it allows the long-term characteristics of the asset classes to surface.
- For a given risk level, an optimal combination of asset classes will seek to maximize returns. Diversification helps reduce investment volatility. The proportional mix of asset classes determines the long-term risk and return characteristics of the portfolio as a whole.
- Portfolio risk may be decreased by increasing diversification of the portfolio and by lowering the correlation of market behavior among the asset classes selected.

## Spending Policy

Where applicable, distributions are made using the total return method. Under the total return method, distributions consist of interest, dividends and realized and unrealized gains. In its determination to appropriate or accumulate, the Investment Committee shall act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, and shall consider, if relevant, the following factors: the duration and preservation of the Fund; the purposes the Fund; general economic conditions; the possible effect of inflation or deflation; the expected total return from income and the appreciation of investments; other resources of the organization; where appropriate and circumstances would otherwise warrant, alternatives to expenditure of the Fund, giving due consideration to the effect that such alternatives may have on the organization, and the investment policy of the organization for each determination to appropriate for expenditure, the organization shall keep a contemporaneous record describing the consideration that was given by the Investment Committee to each of the factors enumerated above.

The spending policy target is 5% (of the trailing 5-year average, of the audited year-end market value of endowment assets); while maintaining the purchasing power of these investments. That is, net of spending, the objective is to grow the value of the portfolio at the rate of inflation over the investment horizon.

## Diversification and Investment Constraints

### *Allowable Investments/Transactions:*

#### Assets Classes

Money Market Funds  
 U.S. Total Tax-Free Bonds  
 U.S. Total Taxable Bonds  
 U.S. Corporate Bonds  
 U.S. High Yield Bonds  
 Convertible Securities  
 Non-U.S. Bonds  
 U.S. Equities - Large-Cap Companies  
 U.S. Equities- Mid-Cap Companies  
 U.S. Equities- Small-Cap Companies  
 World Stocks (Ex. U.S.) Developed and  
 Emerging Market Countries

Real Estate Securities/REITS  
 Hedge Funds  
 Commodities/ Managed Futures

#### Investment Types

Individual Stocks or Bonds  
 Open-ended Mutual Funds  
 Closed-end Mutual Funds  
 Exchange Traded Funds/Index Funds  
 Managed Separate Accounts  
 Investment Partnerships

## Liquidity

Endowment's liquidity requirements are:

- ❖ Cash is used to fund the monthly draws and the Advisor may use discretion as to the amount being held within the portfolio to meet the draw requirements or as an investment decision.

- ❖ The maximum allowable allocation of the aggregate portfolio to non-liquid securities is 15%.

### **Alternative Investments**

#### ***Objective:***

Investment in alternatives may be considered by this organization within the context of an overall investment plan. The objective of such investments will be to seek to diversify the portfolio, complementing traditional equity and fixed-income investments and improving the overall performance consistency and/or risk characteristics of the portfolio. It is acknowledged that there is no guarantee that this objective will be realized.

#### ***Transparency and Liquidity:***

Alternative investments will be audited and generally transparent. For instance, funds may be more appropriate for the Diocese. It is acknowledged that these investments may be less transparent than traditional investments and that liquidity in such investments may be limited, but the Trustees seek to use guidance from auditors in determining which investments would be appropriate for this portfolio.

### **Selection/Retention Criteria for Investments**

#### ***Investment Management Selection:***

Investment managers shall be chosen using the following criteria, but not limited to:

- ❖ Past performance, considered relative to other investments having the same investment objective. Consideration shall be given to both performance rankings over various time frames and consistency of performance
- ❖ Costs relative to other funds with like objectives and investment styles
- ❖ The manager's adherence to investment style and size objectives
- ❖ Size of the proposed fund
- ❖ Length of time the fund/manager has been in existence and length of time it has been under the direction of the current manager(s) and whether or not there have been material changes in the manager's organization and personnel
- ❖ The historical volatility and downside risk of each proposed investment
- ❖ How well each proposed investment complements other assets in the portfolio
- ❖ The current economic environment
- ❖ The likelihood of future investment success, relative to other opportunities



## Investment Monitoring and Control Procedures

### **Benchmarks:**

The following benchmarks will be used to evaluate performance:

#### **Total Fund-Broad Market**

53% Russell 3000 Index/ 20% Bloomberg Barclays U.S. Aggregate Bond Index / 17% MSCI ACWI ex-US/5% FTSE Nareit Index/5% HFRI FOF Index

#### **Individual Investment-Asset Class**

#### **Index**

Domestic Large Cap Value	Russell 1000 Value
Domestic All Cap Value	Russell 3000 Value
Domestic Large Cap Growth	Russell 1000 Growth
Domestic Small Cap Value	Russell 2000 Value
Domestic Small Cap Growth	Russell 2000 Growth
REITS	FTSE Nareit Index
International Developed Equity	MSCI ACWI ex-US
Emerging Market Equity	MSCI EM (gross)
Fixed Income	Bloomberg Barclays U.S. Aggregate Bond Index
Hedge Fund of Funds	HFRI Fund of Funds Index
Commodities/Managed Futures	GS Commodity Index
Cash & Equivalents	90 Day T-Bills

### **Reports:**

- ❖ The investment custodian shall provide The Diocese with monthly statements for each account held by Episcopal Diocese of Rochester and subject to this Investment Policy Statement.
- ❖ The Custodian or another organization selected by the Diocese shall provide to the Diocese on a timely schedule, the unitization for all investors in the Diocesan Endowment program, including but not limited to congregations, parishes, missions and other organizations and funds. This reporting shall be provided monthly, within 15 calendar days of each month end period, and reviewed quarterly at a meeting of the Investment Review Committee.
- ❖ If the Diocese engages an Advisor, the Advisor shall provide Investment Committee the following management reports on a periodic basis but at least quarterly:
  - Performance results of comparative benchmarks over varying time periods and against industry peer groups
  - Review of current asset allocation versus policy guidelines
  - Any recommendations for changes of the above

## **Duties and Responsibilities**

### **The Advisor:**

If the Diocese engages an advisor, the Advisor shall be a Registered Investment Advisor and shall act as the investment advisor to the Chief Financial Officer and the Investment Committee and upon their recommendation the Trustees until the Trustees decide otherwise.

Advisor shall be responsible for:

- ❖ Assisting in the development and periodic review of investment policy.
- ❖ Designing and implementing an appropriate asset allocation plan consistent with the investment objectives, time horizon, risk profile, guidelines and constraints outlined in this statement.
- ❖ Advising the Investment Committee about the selection of and the allocation of asset categories.
- ❖ Identifying specific assets and investment managers within each asset category.
- ❖ Reporting any substantial qualitative changes to investment management organization; which would include, but not limited to lead personnel changes, organizational changes, large increase/ decrease in assets under management, etc.
- ❖ Providing "due diligence", or research, on the Investment Manager(s)
- ❖ Monitoring the performance of all selected assets the advisor consults to.
- ❖ Recommending changes to this investment policy statement.
- ❖ Periodically reviewing the suitability of the investments for the Investment Committee.
- ❖ Being available to meet with the Investment Committee at least four times each year.
- ❖ Being available at such other times within reason at the Investment Committee's request.
- ❖ Preparing and presenting appropriate reports.
- ❖ Advisor is granted discretionary authority to invest in a manner consistent with this investment policy statement.
- ❖ Advisor shall have no authority to withdraw funds from Episcopal Diocese of Rochester's accounts, except to cover payment of previously agreed to fees or at Investor's specific direction.
- ❖ Advisor may not change Episcopal Diocese of Rochester's investment policy, including the targeted asset allocation, without the Trustees' prior approval.
- ❖ Advisor understands that the contact with the Episcopal Diocese of Rochester shall be through the CFO of the Diocese.

***The Investment Committee:***

Investment Committee shall be responsible for:

- ❖ The oversight of the Portfolio on behalf of the Trustees of the Diocese.
- ❖ The Committee will at all times include at least one of the currently elected Trustees. Others may be appointed by the Bishop to fill needs of the committee.
- ❖ Defining, subject to approval of the Trustees, the investment objectives and policies of the Portfolio.
- ❖ Directing, subject to approval by the Trustees, the Advisor to make changes in investment policy and to oversee the Advisor's recommendations with regards to policy, guidelines, and objectives on a timely basis.
- ❖ Provide Advisor with all relevant information on Episcopal Diocese of Rochester's financial condition, risk tolerance and shall notify Advisor promptly of any changes to this information.
- ❖ Understanding the investments in the Portfolio.
- ❖ Exercising all rights, including voting rights, as acquired through the purchase of securities, but which may be delegated to the Church Pension Fund, as appropriate.

***The Investment Manager(s):***

Each Investment Manager will have full discretion to make all investment decisions for assets placed under its jurisdiction, while observing and operating within all policies, guidelines, constraints, and philosophies as outlined in this statement. Specific responsibilities of the Investment Manager(s) include:

- ❖ Discretionary investment management including decisions to buy, sell, or hold individual securities, and to alter asset allocation within the guidelines established in this statement.
- ❖ Communicating any major changes to economic outlook, investment strategy, or any other factors, which affect implementation of investment process, or the investment objective progress of the Fund's investment management.
- ❖ Informing the Advisor regarding any qualitative change to investment management organization: Examples include changes in portfolio management personnel, ownership structure, investment policy, etc.

***The Parishes:***

Individual Parish Vestries shall be responsible for:

- ❖ Acting as Fiduciary for their parish invested funds
- ❖ Developing and maintaining a documented spending policy

**Frequency of IPS Review**

The Investment Committee recognizes that all investments go through cycles and therefore there will be periods of time in which the investment objectives are not met or when specific managers fail to meet their expected performance expectations. The Investment Committee accepts the principle that, in the absence of specific circumstances requiring immediate action and subject to a review of managers in their space, patience and a longer-term perspective will be employed when evaluating investment performance.

The Advisor shall meet with the CFO of the Diocese as needed between meetings of the Investment Review Committee and with the Trustees annually to review and update this policy.

**Adoption**

At a meeting of the Diocesan Trustees on the date below, this policy was approved by a majority of its members. Adopted by the below signed:

Date: February 24th, 2018

Leslie W. Kernan, Jr., Esq.

Vice Chair of the Diocesan Trustees

  
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