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INVESTMENT CONSULTANTS

March 7, 2024

Using Investment Policy Statements as an Investment Tool

It's an Art, Not a Science

Executive Summary

The Investment Policy Statement (IPS) is an essential tool that can improve the investment decision-making process for retirement plans, irrevocable trusts, nonprofit organizations, foundations, endowments, and public funds. The IPS formally encompasses the investing philosophy and decision-making process in writing. The decision-making process requires the investment committee, board members, trustees, or individual investors to agree on their investment philosophy before implementing an investment strategy. Many investors do not realize they are fiduciaries under the law. They do not know what their fiduciary responsibilities include or how to write an Investment Policy Statement. This paper explains what the term fiduciary means and who is included in this definition. Additionally, this paper describes what an Investment Policy Statement is, when it is needed, the components that are included in an Investment Policy Statement, and the steps to writing one. How to use the Investment Policy Statement to document and make decisions and how to maintain the Investment Policy Statement are also included. Additional resources and examples are listed at the end.

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"Investment policy wisely formulated by realistic and well-informed clients with long-term perspective and clearly defined objectives is the foundation upon which portfolios should be constructed and managed over time and through market cycles."

— Charles D. Ellis, *Winning the Loser's Game*

Introduction

The Investment Policy Statement (IPS) is an essential tool that you can use to improve the investment decision-making process. Whether you are a decision-maker for a fiduciary entity or have clients who are fiduciary entities such as retirement plans, irrevocable trusts, nonprofit organizations, foundations, endowments, and public funds, you will find these practical guidelines valuable.

The decision-making process requires the investment committee, board members, trustees, or individual investors to agree on their investment philosophy before implementing an investment strategy. The Investment Policy Statement (IPS) formally encapsulates the investing philosophy and decision-making process in writing.

Charles D. Ellis is an American investment management consultant who founded Greenwich Associates, an international strategy consulting firm focused on financial institutions. He advocates for passive investing through index funds, as his book *Winning the Loser's Game* highlights. Ellis writes, "The principal reason for articulating long-term investment policy explicitly and in writing is to enable the client and portfolio manager to protect the portfolio from ad hoc revisions of sound long-term policy, and to help them hold to long-term policy when short-term exigencies are most distressing, and the policy is most in doubt. (Ellis, 2021, p. 59)."

He also writes, "The high purpose of investment policy, and of the systematic discovery process prerequisite to it, is to establish useful guidelines for investing that are genuinely appropriate to the realities both of your objectives and the realities of the investments and markets." (Ellis, 2021, p. 63)."

Fiduciary Investment Management

How can the investment policy statement be used as a tool to improve your investment decision-making process? Fiduciary Investment Management is an umbrella term that encompasses fiduciary investors—those involved in investment management as fiduciaries. A standard definition of "investment fiduciary" is someone who manages the assets of another person and stands in a special relationship of trust, confidence, and legal responsibility.

"A fiduciary is someone acting in a position of trust on behalf of, or for the benefit of, a third party. More specifically, the courts could include anyone who exercises any discretionary authority or discretionary control regarding fund management, or who exercises any authority or control regarding the management or disposition of fund assets. External service providers often assume a fiduciary duty, especially if they render investment advice regarding fund assets for a fee or other compensation (Cunningham, 1998, p. 2)."

Who Are the Fiduciary Investors?

Some common roles that fiduciary investors hold include:

1. **Investment advisor:** one who manages someone else's money on a comprehensive and continuous basis.
2. **Named trustee:** one who is responsible for managing the assets of the trust, including the option to delegate this responsibility to a professional money manager.
3. **Investment committee member:** one who is a member of a committee who has been delegated the responsibility of managing investment decisions.
4. **Professional (accountant, attorney, or investment consultant):** one who participates in investment decisions.

Using Investment Policy Statements as an Investment Tool

Fi360, a Broadridge Company, has developed a handbook comprised of prudent investment practices. Before this handbook, there was no shared body of knowledge to help fiduciary investors such as trustees, nonprofit board members, trustees of 401(k) plans, and trustees for public pension plans with investment decision-making.

Don Trone co-founded Fi360 and the Center for Fiduciary Studies. He helped develop and was the author of the first edition of the *Prudent Practices*® handbook, first published in 2003. The *Prudent Practices*® handbook is based on current fiduciary law and is edited by the American Institute of Certified Public Accountants. It has been updated and republished several times since 2003.

At the Center for Fiduciary Studies, an experienced investment expert, Done Trone, developed training programs for investment advisors. He is currently the CEO of 3Ethos, which provides training and publications on investment management for the financial services industry. Trone was also the Director of the U.S. Coast Guard Academy Institute for Leadership. He believes that the subjects of investment management and leadership are mutually supportive of one another.

The *Prudent Practices*® handbooks are published in three editions. One handbook is for Investment Managers, one for Investment Stewards, and one for Investment Advisors. Investment Managers are the professionals who pick individual stocks and bonds. Investment Stewards are nonprofit board members, trustees of 401(k) plans, and trustees of personal and charitable trusts. The third group is Investment Advisors, defined as investment management consultants. They oversee the entire investment decision-making process, usually adding most of their value by helping to manage investment risk.

The most current version of *Prudent Practices for Investment Stewards* is available on the Allodium Investment Consultants website https://www.allodium.com/images/pdf/2020-Fi360-Prudent-Practices-for-Investment-Stewards.pdf.

The Investment Policy Statement

What are fiduciary responsibilities related to the Investment Policy Statement? Many legislative acts, such as ERISA, UPIA, and MPERS, have seven standards of care in common. Fi360 coined the term *Uniform Standards of Care* (*Global Fiduciary Precepts*) to denote these seven standards. Their fundamental position is that the *Uniform Standards of Care* (*Global Fiduciary Precepts*) structure the details of a prudent investment process for any fiduciary. Therefore, they equally apply to the investment advisor, the investment committee member, and the trustee.

Global Fiduciary Precepts

1. Know standards, laws, and trust provisions.
2. Diversify assets to specific risk/return profile of client.
3. Prepare investment policy statement.
4. Use “prudent experts” and document due diligence.
5. Control and account for investment expenses.
6. Monitor the activities of “prudent experts.”
7. Avoid conflicts of interest and prohibited transactions.

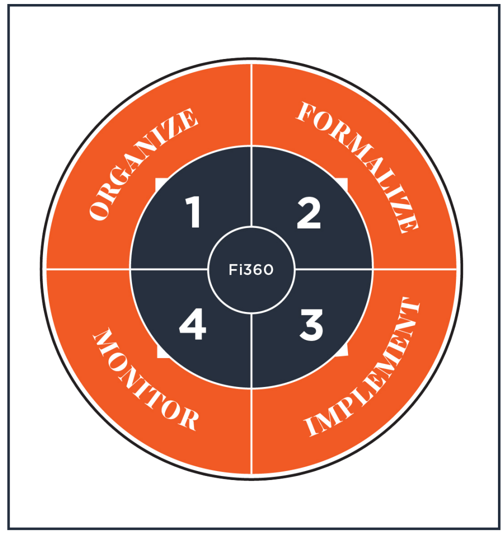
The third global fiduciary precept is preparing and maintaining the investment policy statement. Developing the investment policy statement is a critical function a fiduciary performs. The investment policy statement is like the business plan that guides the activities of those managing the portfolio. The investment policy statement is the formal long-range strategic plan that defines the management of the investment program in a logical and consistent framework. A well-developed investment policy statement should combine the elements of financial planning and investment philosophy and address how to manage each of the other Global Fiduciary Precepts.

Using Investment Policy Statements as an Investment Tool

A primary role of a fiduciary is to manage a prudent investment process, without which the components of an investment plan cannot be defined, implemented, or evaluated. Regarding legal issues, liability is not determined by investment performance but rather by whether a fiduciary approach like the Prudent Investment Practices was followed. It's not whether you win or lose; it's how you play the game. So, if you want to fulfill your fiduciary duties and help your clients understand their fiduciary duties, begin with the prudent process as the starting process for investment decision-making.

The Fiduciary Quality Management System

Fi360 developed the Fiduciary Quality Management System, analogous to the ISO 9001 QMS Continual Improvement Process. The Fiduciary Quality Management System outlines the steps to apply a consistent and repeatable prudent process. It is structured in four parts—Organize, Formalize, Implement and Monitor.



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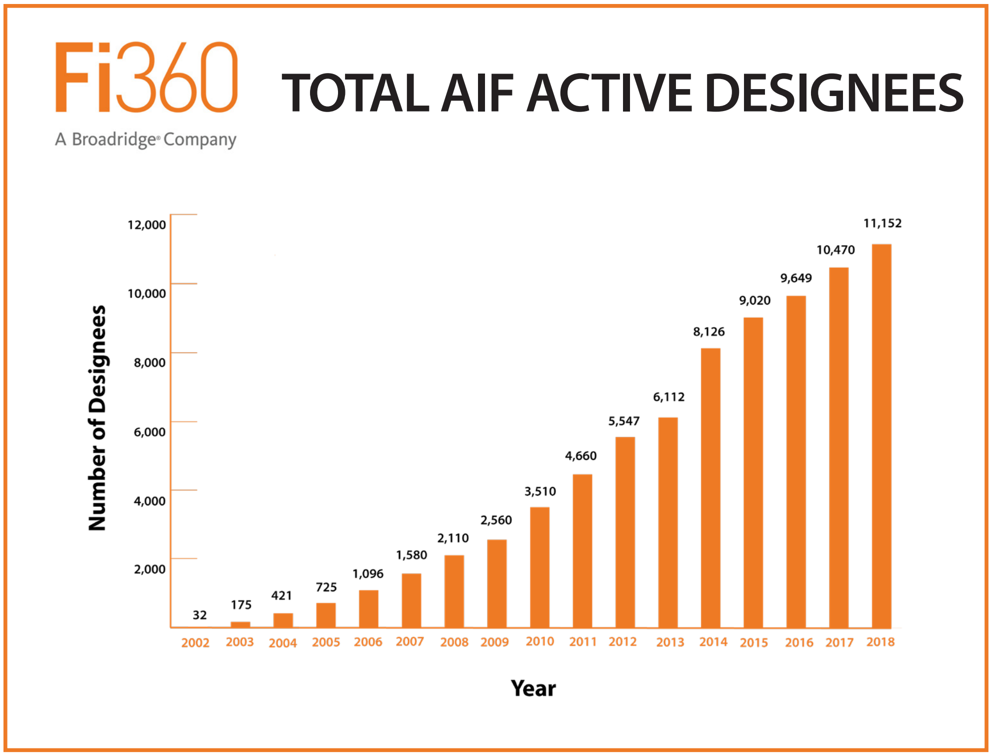
1. *Organize.* The first step in the prudent process is to get organized. Get your arms around all the information. Who are the decision-makers? What are the goals of the organization? What are the facts of the situation in terms of money? Articles of incorporation?
2. *Formalize*. This step is the second one in the process. After you obtain information about the organization, how is an investment strategy or an investment policy formalized? How do you write an Investment Policy Statement that will empower everyone involved in managing the assets or asset allocation?
3. *Implement.* The third step is to implement the strategy that was drafted in the investment policy statement.
4. *Monitor.* The fourth step is to monitor the process on an ongoing basis.

In developing an Investment Policy Statement (IPS) we will focus on the second step of the Fiduciary Quality Management System — *Formalize*.

Fi360 Designations and CEFEX Certification

Fi360 offers a professional designation called an Accredited Investment Fiduciary® Designation (AIF®). Since 2000, over 11,000 individuals have earned the AIF® Designation, including accountants, attorneys, investment brokers, and investment advisors. Fi360 has a "Find a Fiduciary" search function on their website to find Accredited Investment Fiduciary® (AIF®) and Accredited Investment Fiduciary Analyst® (AIFA®) credential holders. Fi360 is a resource for investors who want assistance to draft investment policy statements.

The increasing number of AIF® Designees reflected in the upward trend of the Fi360 graph on the following page shows the credibility of the material produced by Fi360. With over 11,000 AIF® Designees using these materials, this information is beginning to become embedded in the decision-making process of many organizations (Fi360).



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In addition, investment firms are becoming CEFEX certified to prove that they are following fiduciary best practices. CEFEX is an international certification organization for investment advisors, investment stewards, investment managers, record keepers, and third-party administrators. Fi360 and CEFEX are owned by Broadridge Financial Solutions.

CEFEX certification provides independent recognition of a fiduciary or service provider's conformity to all applicable fiduciary practices and criteria. Like ISO Standards, CEFEX certification is intended to streamline due diligence for those seeking the services of organizations that provide or support fiduciary investment services. CEFEX-certified organizations are well-positioned to earn the public's trust. The AIFA® designation is required of all analysts that conduct assessments leading to a CEFEX certification. The AIFA® program provides the requisite knowledge to conduct comprehensive assessments of conformity to the Global Fiduciary Standards of Excellence. A list of all CEFEX-certified firms can be found at CEFEX.org.

Preparing the Investment Policy Statement (IPS)

> "The preparation and maintenance of the Investment Policy Statement (IPS) is the most critical function a fiduciary performs, for a well-written IPS becomes the narrative that defines how all of the investment-related responsibilities will be prudently managed." *How to Write an Investment Policy Statement–Forward* (Trone, 2004, p. 13).

If it isn't in writing, it is a wish, not a plan. You wouldn't start a company without a written business plan. You wouldn't build a deck on your house without a design. Then why do so many institutions fail to record their objectives and strategies in writing when it comes to the oversight of millions of dollars? Your investment policy statement is the document that defines the operation of your fund. It contains written instructions for your money managers.

Although an IPS is not a legally required document, it is a legal document.

> "Although it is not legally required, this document (IPS) is of the utmost importance for all concerned since it makes available a clear indication of investment intent, much like a military commander's mission statement. It should be formalized after full study and reflection, written down in clear language, and agreed to by delegees if outside managers are to be used. Failure to create such a formal statement invites a presumption of imprudence" (Train & Melfe, 1999, p. 80).

Some excerpts from the book, *The Management of Investment Decisions*:

> "For the investment committee, particularly one with a high turnover of members, the IPS (investment policy statement) ensures continuity of the investment strategy and may keep future members from second-guessing the actions of the original members. For foundation and/or endowment committees, the IPS also provides donors the best proof of the organization's stewardship." *The Management of Investment Decisions* (Trone, 1996, p. 11).

> "The investment policy will produce its greatest benefits during periods of adverse market performance. Committee members will be less tempted to alter an otherwise sound program by irrational fears; the investment policy will act as a stabilizer……This is what the substance of good policy review should be all about: the framework that will allow cooler heads and a longer-term outlook to prevail." *The Management of Investment Decisions* (Trone, 1996, p. 12).

> "The IPS (investment policy statement) should be viewed as the business plan and the essential management tool for directing and communicating the activities of the portfolio." *The Management of Investment Decisions* (Trone, 1996, p. 11).

Using Investment Policy Statements as an Investment Tool

Some people argue that they don't want to write an investment policy statement for fear they will not live up to the details they drafted into their IPS. However, one of the most significant reasons for having an investment policy statement is for the benefit of the investment committee, particularly one with a high turnover of members. The IPS ensures the continuity of the investment strategy and may keep future members from second-guessing the actions of the original members.

The IPS also provides donors with substantiation of the organization's stewardship by foundation and endowment committees. A well-written IPS helps get everyone on the same page and reassures large donors looking to support organizations that demonstrate fiscally prudent stewardship. Organizations will find that a well-written IPS is valuable to share with donors.

What is the Investment Policy Statement?

Think of the IPS as the portfolio's business plan, which is likely the most essential management document. It should be reviewed and updated when necessary, or at least once a year, to keep it aligned with the actual process. End investors rely upon the fiduciaries to manage their money effectively.

In essence, the fiduciaries serve as the management team of the portfolio "enterprise." Just as investors in a business expect their management team to have a solid plan to demonstrate an effective business strategy, investors in the fiduciary arrangement are entitled to expect a plan for investment success. The Investment Policy Statement is intended for precisely that purpose.

Following a well-written IPS is the litmus test for how well the fiduciary manages fiduciary duties. It is essential for conforming to a Global Fiduciary Standard of Excellence. One note of caution, the IPS is deemed a "governing document." Therefore, fiduciaries must take care to adhere closely to the investment policies or run the risk of committing a fiduciary breach.

The ultimate test of whether an IPS is effective is whether it provides sufficient detail for a competent third party to implement it without having to supplement it. It should not be so detailed that it requires constant revisions and updates.

Writing an Investment Policy Statement

Many investors need help writing an Investment Policy Statement. Fortunately, you can use a template that provides about 80% of the necessary boilerplate language. One of the most important functions of an investment management consultant is to help you draft your IPS.

Construct the IPS so everyone can read it and understand what the group has agreed to do—whether it's one trustee, two trustees, three trustees, or a nonprofit board with 48 members. Everyone should be on the same page about the organization's investment policy and investment strategy. The IPS is like the business plan for the portfolio.

Benefits of an IPS

A well-crafted Investment Policy Statement offers many benefits. In the event of an audit, litigation, or dispute, the IPS supports a "paper trail." One of the first documents a litigator or auditor may request in a review is the IPS because it outlines how the overall investment strategy should be managed. Another benefit is that an IPS helps negate "Monday morning quarterbacking" or second-guessing of decisions.

There will likely be a turnover of investment committee members and trustees. With an IPS, new decision-makers will understand how the previous decision-makers arrived at their outcomes.

Using Investment Policy Statements as an Investment Tool

An IPS also helps to insulate investment decision-makers from market noise. During periods of over or under-confidence in the capital markets, an IPS helps keep everyone focused on the organization's or entity's long-term goals and objectives. In volatile periods, investment decision-makers are more likely to make the wrong decision at the wrong time if they do not have a well-developed IPS to guide them.

There are many benefits to having an IPS. An IPS reassures contributors and donors; it provides a baseline for monitoring your investments. An IPS offers guidance for implementing the investment strategy and provides continuity for future board members. It also leaves a legacy of institutional decision-making and helps compliance with fiduciary laws.

> "Standardization is one of the reasons why we were so successful during Katrina. We had crews come in from all of the country, but it didn't matter; we had all been trained the same way." *The Guardian*, 2006.

The movie *The Guardian* with Kevin Costner and Ashton Kutcher provides a good anecdote about the similarity between coast guard training and the use of Investment Policy Statements. In the film, they ask, "How do you decide who lives or dies?" During Hurricane Katrina, helicopter rescue pilots came from all over the country to help. There are six positions on the rescue coast guard helicopter. Each of the six roles on the helicopter has a job description with a corresponding checklist. Everyone in the coast guard that works on a rescue helicopter is trained in the same procedures, policies, checklists, and job description.

Rescue teams from all over the country were able to help in Hurricane Katrina, and they didn't have to fly in with their five coworkers. They could show up and step onto a rescue helicopter and immediately perform their role. They could carry out their duties because they had standard checklists, cross-training, and a helicopter mission plan.

An IPS brings a similar kind of standardization of the investment strategy and philosophy as coast guard training. Anyone who gets asked to serve as a fiduciary on an investment committee or as a trustee should be able to read the IPS and understand the investment strategy of the fiduciary entity. In his book *How to Invest Someone Else's Money,* John W. Guy writes, "Investment policies must be simple, forthright, and understandable to a competent stranger" (Guy, 1994, p. 75).

An IPS is the business plan to invest the entity's money. If you don't do investment planning, inefficiencies, missteps, and even imprudent decisions can result. Investing an organization's money depends on a well-written investment policy statement, resulting in more focused results, clearer roles, and more measurable outcomes.

Investment Policy Statement Components

Academic resources are an effective foundation for developing an IPS. An excellent book on the subject is *The Management of Investment Decisions* by Don Trone, William Allbright and Philip Taylor (1996). They define the major components of an IPS in the book.

An investment policy statement has eight major components. Attachments and appendices may be used to capture especially detailed guidance and anything that may change frequently. The main body of the investment policy statement (IPS) sets the overriding plan. The attachments and appendices can provide specific details of how the plan is currently being executed.

The key elements of an effective IPS are:

1. ***Executive Summary***

   Develop a one-page executive summary of the IPS. In this summary, there should be a quick overview of the contents of IPS.

2. ***Purpose and Background***

   The executive summary includes high-level information like the name and tax number of the organization.

   a) *The "story" of the organization*. Include the background "story" of the organization and critical information about the fiduciaries of the fund. Also include information about the purpose of the IPS, the objectives of the portfolio and the legal structure.

      Enter the portfolio size and the expected dollar amount of future contributions and pending disbursements. Also include the fiscal health of the sponsoring entity and tax status—taxable or tax-exempt. In addition, note any restrictions on the distributions of fund assets, legal, donor, or board-directed.

      For example, XYZ Trust, established by Joe Jones in 1950, has a list of FBO beneficiaries and a set of intended actions. It can be a couple of paragraphs explaining the story of the fiduciary entity. Similarly, for foundations or endowments—describe the organization, how it got started, why it has the money, etc. Answer questions such as what is the approximate dollar amount of the portfolio? Does the organization plan to be around in perpetuity, or does it have fiscal health problems? These items go into the purpose and background of the IPS.

   b) *Key information*
      - Name of organization
      - Tax ID number
      - Board of directors
      - Custodian
      - Investment managers
      - Investment consultant
      - Legal counsel
      - Accountant

3. ***Statement of Objectives***

   The objectives should contain the desired interim and end results. In addition, include the present investment asset allocation, expected returns, projected financial requirements, spending policy and cash flow projections. Enter the investment time horizon and risk tolerance level of the portfolio and the committee, as they may differ. Also include the attitudes, expectations, and goals of the committee members or decision makers.

   Examples of general investment objectives:
   - Take a "reasonable and prudent" amount of risk to maximize return at that risk level.
   - Limit risk exposure through prudent diversification.
   - Establish policies based on total return rather than current income.
   - Control the costs of administering the portfolio.
   - Maintain the purchasing power of the fund.

4. ***Guidelines and Investment Policy***

   Establish guidelines to identify the parameters of the investment strategy, such as the diversification or asset allocation decision. The guidelines should outline asset class preferences and expected rates of return by asset class. Document targeted asset allocation guidelines, asset class limits and rebalancing procedures.

Include risk parameters in the guidelines, such as risk tolerance, time horizons, and the expected or desired rate of return of the overall portfolio.

> "Measuring investment risk is the defining aspect of an investment consulting practice." *The Consultant's Math Primer*, Investment Management Consultants Association, (Chapter 4).

Measuring investment risk is one of the defining aspects of an investment management consulting practice. However, if asked, many people can't conceptualize questions like "Do you want to be a growth-oriented investor or an income-oriented investor?" Or "Do you want to be an aggressive or conservative investor?" People are sometimes not sure how to respond to these types of questions. A more effective approach is to show the investment committee various samples of model asset allocation portfolios with expected risk and returns. It gives investors some examples of what their choices are. An analogy for these sample asset allocation models would be going into a restaurant and selecting options from a menu. Going into a restaurant and simply asking for food is not productive. Selecting from specific choices will enhance the interaction with investors so they can better understand risk.

Asset Allocation and Diversification Strategy

The diversification strategy is an integral part of the IPS and arguably the most critical part of the IPS. Most investors, Modern Portfolio Theory, and the court system generally view diversification by asset class as a prudent way to diversify an investment portfolio. Every investor needs to make an asset allocation decision.

Asset Allocation	Lower Limit	Strategic Allocations	Upper Limit
Domestic Large-Cap Equities			
Value	5%	10%	15%
Blend	5%	10%	15%
Growth	5%	10%	15%
Mid-Cap Equities	5%	10%	15%
Small-Cap Equities	5%	10%	15%
International Equities	5%	10%	15%
Intermediate-Term Fixed Income	30%	35%	40%
Cash Equivalents	0%	5%	10%

In the example of a strategic asset allocation for a portfolio in the chart above, the target asset allocation is shown in the middle column. The "guard rails" are the lower and upper limits in the outer columns. The portfolio should be maintained within the boundaries of the agreed-upon lower and upper limits of the asset allocation and specific investment strategy. These guardrails help the investor to keep the portfolio in alignment with the target strategic asset allocation.

5. ***Securities Guidelines***

Define the boundaries of the investment universe. The boundaries outline the playing field for the investment managers. Specific investments which are permitted in the various asset categories, such as cash equivalents, domestic equities and fixed income, international equities and fixed income, and alternative investments should be defined. Include any socially responsible investment preferences. Whether certain investments should be excluded or prohibited should be documented in this section of the IPS.

Example Boundaries for Investment Managers

1. Domestic Equities
    - Diversified by security (not more than 10%)
    - Diversified by economic sector
    - Emphasize quality
    - Liquidity
2. Domestic Fixed Income
    - Bond credit quality rating
    - Diversification by credit quality
    - Diversification by issuer (not more than 10%)
    - Liquidity
3. International Equities
    - Diversified by security (not more than 10%)
    - Diversified by industry
    - Diversified by country
    - Allow foreign currency hedging
    - Prohibit foreign currency speculation
4. International Fixed Income
5. Cash and Cash Equivalents
    - Quality rating
    - Automatic interest-bearing sweep vehicle invested daily

6. Selection of Investment Managers

Include a definite investment manager research methodology and selection process focusing on people, philosophy, process, and performance. Developing a precise manager research methodology is a critical component of the IPS. Eight criteria are used when doing due diligence on researching Investment managers. These commonly used criteria can be found in the *Prudent Practices for Investment Stewards* handbook, published by Fi360.

Eight Due Diligence Criteria

These due diligence criteria can be written into the IPS

1. Performance relative to peer group
2. Performance relative to assumed risk
3. Inception date of product
4. Correlation to peer group
5. Assets within the product
6. Holdings consistent with style
7. Expense ratios or fees
8. Stability of the organization

Other Recommendations when Selecting Investment Managers

1. Choose Registered Investment Advisors—as defined by the Registered Investment Advisors Act of 1940.

2. Review quarterly performance numbers—historical quarterly performance numbers calculated on a time-weighted basis.
3. Obtain evaluation reports by an objective third party—showing the investment risk/return profile of the manager relative to other investment managers of similar investment style.
4. Gather detailed information on the firm—the history of the firm, key personnel, key clients, fee schedule, and support personnel.
5. Ask for clear articulation of the investment strategy to be followed and document that the strategy has been successfully adhered to over time.
6. Look for no outstanding legal judgments—selected firms shall have no outstanding legal judgments or past judgments that may reflect negatively on the firm.

7. Control Procedures

Define control procedures to monitor the portfolio periodically. Control procedures provide a mechanism to monitor the portfolio on an ongoing basis. Numerous parties are involved in the investment management process. Each service provider should have specific duties, requirements, and job responsibilities delineated in this section. For instance, the fiduciary investor has five or six responsibilities. The investment advisor or investment management consultant might have five or six different responsibilities. The investment managers have their list of duties. The custodian has a list of their responsibilities. All the roles and responsibilities of the various participants in the process should be itemized in the IPS with a process to monitor how well these roles and responsibilities are executed.

Establish specific performance criteria and benchmarks for each investment manager. At a minimum, the requirements should include the index by which the manager's performance will be compared. In addition, enter expectations for performance net and gross of fees. When the manager agrees to performance criteria at the start of the engagement, there is less tendency for controversy between the investor and the manager—if the manager must be subsequently fired.

Regularly Scheduled Reviews

The investment management process triggers several reviews and events to schedule periodically—monthly, quarterly, and annually.

1. Monthly: custodian report on current holding.
2. Quarterly: quarterly performance reports prepared by consultant, quarterly review of asset allocation strategy, quarterly review of manager performance versus benchmarks, quarterly review of manager performance versus peer group.
3. Annually: annual revisions to the investment policy statement, annual review of investment expenses.
4. On an as-needed basis: the investment committee should meet if there have been any material changes to hired investment managers and any other event that materially impacts the committee's ability to carry out their fiduciary responsibilities.

8. Signatures

Sign the documents. The IPS is not a contract, but an acknowledgment that everyone involved in developing the policy for this entity, the fiduciary or trustee, will sign this document saying that this is the IPS as of a specific date. The IPS is the document to show anyone who needs to know about the organization's investment policies. Fiduciaries signing the document acknowledge their approval of the investment policy. They will be held accountable for the written investment policy. Once you draft the investment policy, you will need to implement that policy. Review the IPS on an annual basis. It doesn't have to be revised annually but should be reviewed yearly for reasonableness.

Roles and Responsibilities

Roles and Responsibilities of the Fiduciary

The fiduciary, generally called a steward, is always responsible for setting the goals and approving the asset allocation strategy. Stewards should prepare the IPS, diversify the portfolio's assets, and prudently select investment options. In addition, they must control and account for all expenses, incurring only reasonable costs. They must monitor and supervise all service providers and the activities of the overall investment program. They should also avoid prohibited transactions and conflicts of interest.

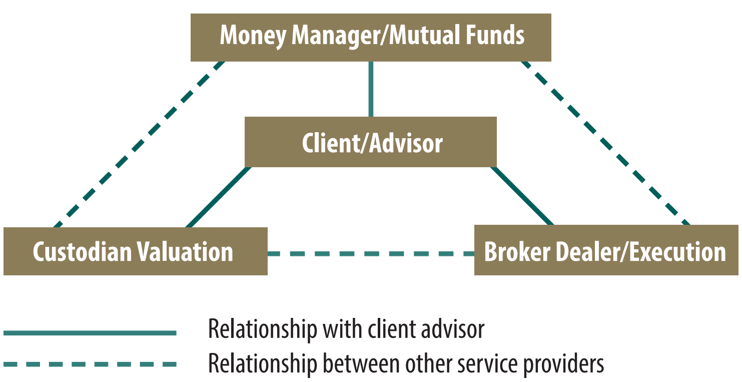
If statutes and trust provisions permit, the fiduciary may delegate certain decisions to professional money managers and trustees as co-fiduciaries. However, even when decisions have been delegated to other professionals, a fiduciary can never fully abdicate the fiduciary responsibilities.

Characteristics of the Successful Fiduciary

Characteristics of a successful fiduciary include the discipline of developing long-term investment policies and taking a personal interest in the capital markets. Being a successful fiduciary doesn't require experience but commitment, courage, and the willingness to get the right things done. New trustees or investment committee members are often concerned about being qualified to perform their duties, citing their lack of Wall Street experience and acumen. They should not worry about this. The duties of an investment committee member are similar to the responsibilities of a general manager. These duties include identifying the goals and objectives, determining the resources to be allocated, preparing a business plan, implementing the business plan, and monitoring the results on an ongoing basis to see if the goals and objectives of the business plan are being met. The most essential characteristic of a successful fiduciary is the ability to get the right things done, otherwise known as effective management. A prudent process facilitates effective management by distinguishing important from unimportant tasks.

Separation of Roles and Responsibilities

The separation of roles is best practice in the industry. Although it is not a fiduciary requirement, larger institutional portfolios of $10 million or more should attempt to ensure that the four parties—money manager, broker, custodian, and investment advisor are all separate and unrelated entities. This approach provides for a system of checks and balances.



Source: © Fi360, a Broadridge Company

This diagram shows the various responsibilities of multiple actors within a fiduciary investment management setting. The investor or client is in the middle, designated as client/advisor. The advisor and the fiduciary client, such as a trustee, work together to develop an Investment Policy Statement that defines the asset allocation model. The advisor helps the fiduciary client to hire independent service providers to implement the investment policy. The custodian holds the money and generates a monthly statement. The investment or money managers for mutual funds include the various asset classes outlined in the IPS. The money managers have a relationship with the broker/dealer doing the execution, as indicated by the dotted line. The money managers execute trades on behalf of the clients directly with the broker/dealers. All the service providers work together, but they are guided by the client and the investment advisor based on the IPS.

Using Investment Policy Statements as an Investment Tool

If one were to examine cases involving breaches of fiduciary responsibility of investments, one would inevitably find that one or more parties were wearing two hats. For instance, consider the Bernard Madoff Ponzi Scheme. In that case, Mr. Madoff wore all the hats, which enabled him to fabricate records and abscond with the money investors deposited. In this example, investing with Madoff would have been impossible if an investor had demanded separation of duties using an independent custodian, independent money managers, and independent broker/dealers. Separating roles is an important fiduciary best practice, not commonly understood by the public. Implementing the division of duties can help prevent investors from getting into financial trouble on Wall Street.

Roles and Responsibilities: Advisor or Investment Management Consultant

Writing an investment policy statement is the heart of investment management consulting. The fiduciary investor can retain an objective third-party investment advisor or investment management consultant to assist in managing the overall investment process. Investment advisors can help investors with their fiduciary responsibilities by guiding them through the disciplined investment process. The investment advisor educates the investor and assists in preparing, implementing, and maintaining the investment policy statement. In addition, the investment advisor conducts asset allocation studies, offers investment options with supporting research, helps implement diversification in asset allocation strategies, coordinates investment manager search processes, and provides ongoing investment manager reporting and evaluation.

The investment management consultant is an investment professional who helps fiduciary investors set and meet their long-term financial goals. There are three essential reasons for hiring an investment management consultant. First, investors may believe that they do not have the knowledge they need or cannot afford to develop that knowledge internally. The second reason is that the investor wants guidance with difficult decisions. The third reason is that investment management consultants provide third-party endorsement or validation of decisions and actions.

The role of the investment management consultant is to work with the fiduciary investor to document their investment policy. The investment management consultant might use an investment policy questionnaire to help investors address the most critical investment policy decisions. The final document is the written investment policy statement.

Role of the Investment Advisor to Help the Client

The advisor (investment management consultant) guides the fiduciary investors through a disciplined and rigorous investment process. The fiduciary investors may often retain an objective, third-party advisor to assist in managing the overall investment process.

The specific duties and responsibilities of the Investment advisor are to:

1. Help to develop a formal Investment Policy Statement.
2. Recommend and implement strategic asset allocation.
1. Perform due diligence research on investment managers.
2. Evaluate the performance of investment managers.
3. Replace investment managers when necessary.
4. Negotiate the cost of the service providers.
5. Implement and monitor portfolio performance.
6. Provide quarterly performance reports and meet with fiduciary investors to review them.
7. Help fiduciary investors to manage the investment decision-making process.

Using Investment Policy Statements as an Investment Tool

Role of the Investment Manager

The investment manager picks individual securities, such as stocks and bonds. Unlike the investment management consultant responsible for managing the investment process, investment managers are responsible for making investment decisions—security selection and price decisions. These securities include mutual funds, exchange-traded funds, index funds, separately managed accounts, private investment funds, limited partnerships, etc. Investment managers can be either active or passive.

The Investment Policy Statement lists seven things that an investment manager must accomplish. Investment managers are fiduciaries; therefore, they are co-fiduciaries relative to the portfolio.

Seven Responsibilities of the Investment Manager

Seven responsibilities of the investment manager include:

1. Manage the assets under their supervision.
2. Exercise complete investment discretion regarding buying, managing, and selling assets.
3. Vote promptly on all proxies and related actions.
4. Communicate all significant changes concerning the managed fund or the firm itself.
5. Effect all transactions subject "to best price and execution."
6. Use the same care, skill, prudence, and due diligence that experienced investment professionals acting in a like capacity would use.
7. If managing a separate account, acknowledge co-fiduciary responsibility.

Role of the Custodian

The role of the custodian is to keep the money safe, providing monthly statements. Duties include:

1. Maintain separate accounts
2. Value the holdings
3. Collect income and dividends
4. Settle all transactions
5. Provide monthly reports

Drafting the Investment Policy Statement

When drafting the investment policy statement, be sure to document everything. Fiduciary law recommends that you document your investment process. Although it is not required to document your investment policy, it is prudent to create this document. Documenting your investment philosophy, strategy and process makes decision-making easier for current and future board members. All decision-makers can read the documents to learn about current investment philosophy and strategy. The investment policy statement is extremely beneficial to investment management consultants and professional investment management firms hired to help manage the investment portfolio.

Document these seven areas to show that you are using a prudent process in your investment decision-making.

Seven Areas to Document When Writing an IPS

When writing an Investment Policy Statement, document the following areas:

1. Your investment processes
2. Your investment policy

3. Your asset allocation decision
4. Your manager selection process
5. Your performance monitoring
6. Your ongoing due diligence
7. Your meeting minutes

Who Drafts the IPS and Why?

The roles responsible for drafting an Investment Policy Statement include:

1. ***Investors –*** institutional (fiduciary) investors planning to fulfill their fiduciary responsibilities and individual investors who want to have a plan and disciplined investment strategy.
2. ***Investment advisors –*** advisors acting as a fiduciary to a fiduciary account with a fiduciary standard of care.
3. ***Investment product providers –*** such as banks and brokerage firms that want to protect themselves from liabilities.

How to Draft an Investment Policy Statement

There are various ways to draft an Investment Policy Statement. Preparing the IPS from scratch is very difficult and not recommended. Copying a sample IPS is also not recommended because it may not be well-written. An effective way to draft an IPS is to start with a template or outline. Templates can be obtained from Fi360 or other credible organizations regarding fiduciary best practices such as academia or MBA programs. Investment firms that have a fiduciary certification often make IPS templates available. Many of these templates are free. Find an IPS template that has a standardized format with boilerplate language.

Eighty percent of the wording on the template is standard. The customizable part of the Investment Policy Statement is the most critical. The investment advisor works with the fiduciary investor to determine what is unique about the entity. Avoid templates written by banks and brokerage firms because they might write investment policy statements in their best interests to protect themselves. The investment policy statement should be drafted from the viewpoint of the fiduciary investor.

Sources of Investment Policy Statement Expertise

Prioritized Sources of Investment Policy Statement Expertise	
Potential Source of Content	**Quality Rating**
Academics: Books and Universities	A
Investment Firms with Fiduciary Certifications	A
Investment Trade Associations with Professional Designations Fi360: AIFA®&AIF®; CFA Institute: CFA; Investments & Wealth Institute: CIMA	A-
Independent, Fee-Only Financial Advisors with Fiduciary Designations: AIFA® & AIF®	B
Industry Trade Associations: Similar Organizations, Membership Resources	B-
Industry Peers: Sharing Investment Policy Statements	C+
Dually-Registered Financial Advisors with Fiduciary Designations: AIFA® & AIF®	C+
Bank and Brokerage Firm Financial Advisors with Fiduciary Designations: AIFA® & AIF®	C
Dually-Registered Financial Advisors with WITHOUT Fiduciary Designations	D
Bank and Brokerage Firm Financial Advisors WITHOUT Fiduciary Designations	D

Using Investment Policy Statements as an Investment Tool

Steps for Drafting an Investment Policy Statement

Begin the process of drafting an Investment Policy Statement with an outline. Allodium Investment Consultants offers a one-page Investment Policy Statement Outline available on the Allodium website. It takes the best practices from the textbook *The Management of Investment Decisions* by Donald Trone, William Allbright, and Philip Taylor and puts it into a one-page document that can be downloaded from here: https://www.allodium.com/resources-2/educational/educational-documents-2.html.

Using a sample Investment Policy Statement with standardized language may be helpful as a starting point. Some categories include defined roles and responsibilities, asset classes, asset allocation percentages, and investment manager due diligence criteria. The Investment Policy Statements can be modified to meet the client's or organization's needs. A sample Investment Policy Statement for a foundation is available on the Allodium website here https://www.allodium.com/resources-2/educational/educational-documents-2.html.

When drafting an Investment Policy Statement, include questions related to the seven investment policy practices outlined in the *Prudent Practices for Investment Stewards* handbook. The most recent version of this handbook is available on the Allodium website https://www.allodium.com/images/pdf/2020-Fi360-Prudent-Practices-for-Investment-Stewards.pdf.

At this stage of the drafting process, the fiduciary must understand the principles of asset allocation. By law and regulation, a prudent expert is expected to understand Modern Portfolio Theory and apply generally accepted investment principles. The fiduciary must also prepare an Investment Policy Statement to guide the remainder of the investment process. In addition, consider whether socially responsible investing will be used in constructing the portfolio.

Possible tension between a disciplined approach to risk management as required by law and socially responsible investing may exist. Drafting the Investment Policy Statement allows fiduciary investors to develop and document clearly delineated values-based investing goals and strategies. Values-based investing is known as socially responsible investing, responsible investing, sustainable investing, ESG investing, and impact investing. See Practice 2.7

Elements of an Investment Policy Statement

Each element of the IPS, such as time horizon, risk level, expected return, and asset class selection, is also represented by the prudent practices from the *Prudent Practices for Investment Stewards* handbook. Each of the prudent practices has several supporting criteria.

- Practice 2.1: Time horizon
- Practice 2.2: Risk level and tolerance
- Practice 2.3: Expected return
- Practice 2.4: Asset class selection
- Practice 2.5: Asset class implementation and monitoring considerations
- Practice 2.6: The IPS
- Practice 2.7: SRI (optional)

Prudent Practice 2.6: The IPS

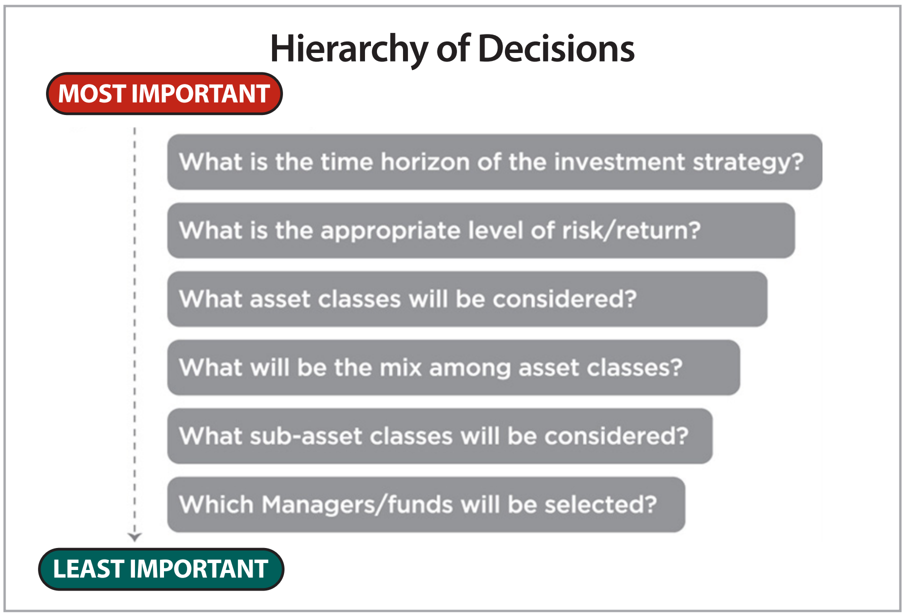
Prudent Practice 2.6 states that the Investment Policy Statement (IPS) should contain sufficient detail to define, implement, and monitor the portfolio's investment strategy. Seven criteria comprise Prudent Practice 2.6. These supporting criteria are the following:

2.6.1 – The investment policy statement identifies the bodies of law governing the portfolio.

2.6.2 – The investment policy statement defines the duties and responsibilities of all parties involved.

2.6.3 – The investment policy statement specifies risk, return, and time horizon parameters.
2.6.4 – The investment policy statement defines diversification and rebalancing guidelines consistent with risk, return, and time horizon parameters.
2.6.5 – The investment policy statement defines due diligence criteria for selecting investment options.
2.6.6 – The investment policy statement defines procedures for controlling and accounting for investment expenses.
2.6.7 – The investment policy statement defines monitoring criteria for investment options and service vendors.

How to Make Investment Decisions



Source: © Fi360, a Broadridge Company

The Fi360 Hierarchy of Decisions diagram can be used to help the fiduciary make decisions. Investors have questions such as "What manager should I select?" or "What funds should I choose?"

The most foundational question is, "What is my time horizon?" Is your time horizon one year, five years, ten years, or twenty years? You begin with the time horizon, then determine the appropriate risk level. Third, which asset classes will you consider? Fourth, what will the mix be among the asset classes? Fifth, which sub-asset classes will you choose, such as small-cap versus large-cap or domestic versus international? You select the managers only after you have determined a targeted asset allocation.

Answer the questions in order and complete all the steps in the process. These questions will help an investment committee discuss the critical questions so they can agree on the investment policy.

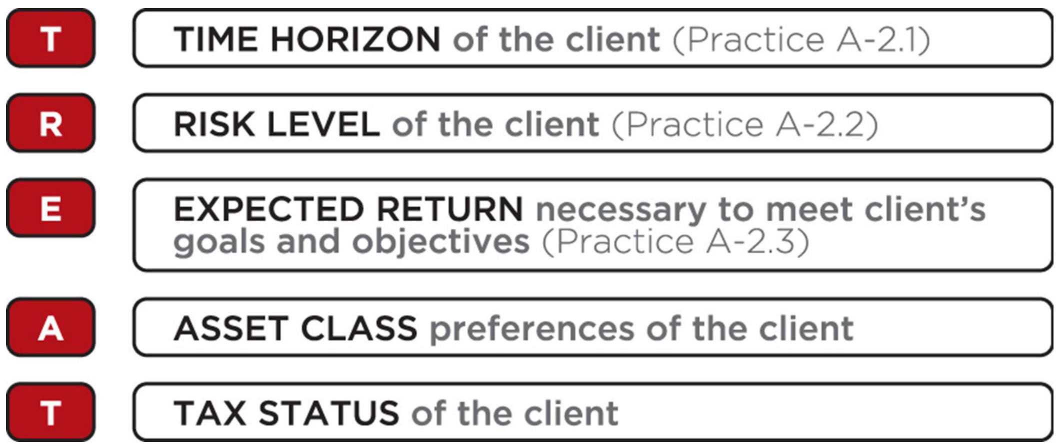
Criteria 2.4.1 calls for "Assets to be appropriately diversified to conform to the portfolio's time horizon and risk/return profile and to reduce non-systemic risk." The strategic asset allocation should be the specific mix of asset classes that meets the portfolio participant's mutually agreed upon risk/return profile. This practice requires the strategic allocation, known as the Policy Portfolio, to be recorded in the IPS.

Another helpful diagram from Fi360 looks at the time horizon, risk level, expected return, asset class and tax status of the client. All these considerations should go into the Investment Policy Statement and strategic asset allocation process.

Using Investment Policy Statements as an Investment Tool

Fi360 uses the acronym "TREAT" to define the specific variables that should be included in the asset allocation decision, demonstrated by the chart.

TREAT Diagram



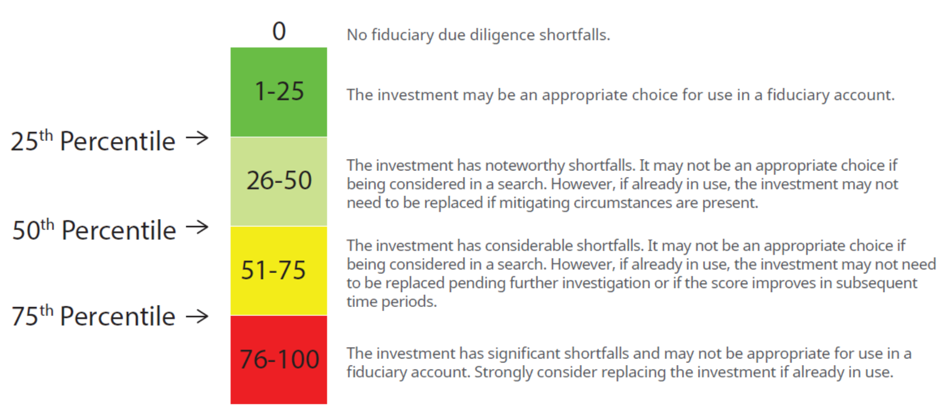
Source: © Fi360, a Broadridge Company

Due Diligence for Investment Options

Fi360 provides a list of due diligence research criteria you can use when searching for, selecting, and monitoring investment managers. These criteria are included in the Fi360 *Prudent Practices for Investment Stewards* handbook. You can find the handbook on the Allodium website https://www.allodium.com/images/pdf/2020-Fi360-Prudent-Practices-for-Investment-Stewards.pdf.

1. Performance relative to peer group.
2. Performance relative to assumed risk.
3. Inception date of product.
4. Correlation to peer group.
5. Assets within the product.
6. Holdings consistent with style.
7. Expense ratios or fees.
8. Stability of the organization.

Fi360 Fiduciary Score



Source: © Fi360, a Broadridge Company

Using the Investment Policy Statement

This section will cover the practical application of using the Investment Policy Statement (IPS) as a tool to improve your investment decision-making process and help you build consensus among all the investment fiduciaries. These guidelines are especially helpful for nonprofit organizations.

Using the IPS: Governance Calendar

Review your Investment Policy Statement and investment decision-making process regularly as part of the fourth step, "Monitor" in the Fiduciary Quality Management System.

Ensure that your IPS still represents the investment policy decisions of the fiduciary investor. Reviewing the investment policy statement might be overwhelming for the investment committee of a large organization. Splitting the review out over the four quarterly meetings may be helpful. This calendar highlights items to discuss and complete each quarter. You can find an Annual Governance Calendar on the Allodium website https://www.allodium.com/images/Educational/Annual-Governance-Calendar.pdf.

Example of an investment committee meeting schedule:

- *Quarterly* meetings to review the portfolio.
- *Annual* meeting to review but not necessarily change the Investment Policy Statement.
- *Interim* meetings to address urgent issues.

ANNUAL GOVERNANCE CALENDAR

Sample Fiduciary Investment Management Governance Plan

Calendar of Recurring Topics

February	• Fourth Quarter Performance Summary • Annual Review of Operating Reserve Portfolio (Time Horizon and Investment Strategy) • Review of Investment Program Expenses-- Investment Managers, Custodian and Consultant • Review of Benchmarks • Review of Governance Calendar for the Next Year • Annual review of Long-Term Reserve Portfolio (Time Horizon and Investment Strategy)
May	• First Quarter Performance Summary • Review Socially Responsible Investment Plan • Annual NACUBO Comparison • Executive Session to Review the Performance of the Investment Consultant
August	• Second Quarter Performance Summary • Review of Historical Gifts Received • Investment Portfolio • Asset Allocation Review • Review of Alternative Investment Managers
November	• Third Quarter Performance Summary • Investment Policy Statement Review • Review Investment Committee Charter and Bylaws • Assessment of Committee’s adherence to Policies and Fiduciary Best Practices

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Using Investment Policy Statements as an Investment Tool

Using the IPS: Annual Review Meetings

Practice SA-4.6: This is a process to periodically review the organization's effectiveness in meeting its fiduciary responsibilities. Some items to discuss at the annual review meeting could include the Investment Stewardship Questionnaire, Investment Stewardship Analysis, and Letter of Understanding. Discuss and develop action items regarding governance, inflows, investment policy, investment management, and financial matters as scheduled on the calendar.

Sample Documents and Topics:

- Fiduciary Acknowledgment Letter—everyone on the investment committee must understand that they are a fiduciary.
- Investment Committee Meeting Minutes
- Investment Policy Statements
- Investment Committee By-Laws
- Investment Fiduciary Checklist

These sample documents can be found on the Allodium website https://www.allodium.com/resources-2/educational/educational-documents-2.html.

Self-Assessment of Fiduciary Excellence (SAFE)

Use the Self-Assessment of Fiduciary Excellence (SAFE) to empower every investment committee member to ask powerful questions about the investment policy. SAFE is a list of 21 questions that can be asked about the investment policy. You can access a free copy of this document in the Educational Resources section of the Allodium website.

Using the IPS: Documenting Decisions

Historical Record of Investment Policy Decisions

Record all your major investment policy decisions and the significant changes to your investment policy over time. Provide this historical record to all fiduciary decision-makers at the Annual Review Meeting. Also, provide this information to all new investment committee members so they can understand the history of policy decisions. You can attach this document to the Investment Policy Statement as an appendix.

Using Investment Policy Statements as an Investment Tool

A sample excerpt of a historical record:

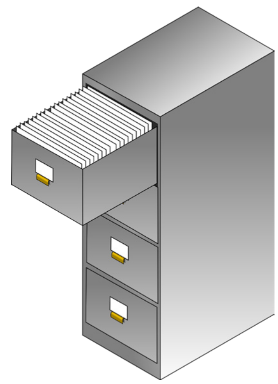
08/28/2014	Modified asset allocation policy slightly to bring down the cost of the managers. We moved 3% from Managed Futures and added it to Diversified Alternatives. We also made slight adjustments to hedged equity and equities. We are now targeting approximately 55% in domestic stock and 45% in international stock.

Fiduciary File

You should create a fiduciary file (see Practice 1.2 and Criterion 1.2.3 of Fi360's Prudent Practices) for your entity. Maintain all documents related to the investment management process in a central location called the "fiduciary file." This file is the definitive source of information regarding the investment decision-making process.

The fiduciary file should include:

- Applicable trust documents
- Custodial and/or brokerage statements
- Investment performance reports
- Service agreements with investment management vendors
- The Investment policy statement and committee minutes
- Most recent asset allocation and/or asset liability studies
- Due diligence files on funds and other investment managers
- Monitoring procedures for funds and other investment managers



Using the IPS: Governance

All areas within the nonprofit should use the Investment Policy Statement. Train everyone on how to use the Investment Policy Statement. Include training for the board of directors, finance committee, investment committee, staff, and development committee. The charitable nonprofit can use the Investment Policy Statement to prove investment stewardship.

Proving Investment Stewardship

The "Investment Stewardship Ratio" scoring system, based on a scale of 1 to 10, is used by some management consultants during an annual review to determine how the investor fares in each of the following seven areas:

- Governance — who makes decisions?
- Cash Inflows — gift acceptance procedures
- Investment Policy — investment objectives defined
- Investment Management — research, rebalancing
- Financial — balance sheet, cash reserves, taxes
- Administration — accounting, legal, staff
- Cash Outflows — spending policy

Behavioral Governance

"You cannot rise above a level to which you have not been trained."
— 3Ethos

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Using Investment Policy Statements as an Investment Tool

The military makes a significant commitment to training. During extreme duress, you cannot rise beyond the level you have been trained. During the first nine days of Hurricane Katrina (August/September 2005), the U.S. Coast Guard rescued 24,500 people. The Coast Guard is the only organization or agency that responded with this magnitude. Standard procedures and a well-defined ethos are the secrets to the Coast Guard's success.

The *Behavioral Governance Framework* is the foundation for uniform decision-making. Use it to substantiate a fiduciary, governance, project management, or professional standard of care.

Behavioral Governance is the third leg of the Behavioral Sciences stool. A unique feature of Behavioral Governance is that it has a universal decision-making process that can be used in any industry sector or domain. Use the Behavioral Governance Framework to lead a team, division, department, company, investment committee or board of directors.

Advantages of the Behavioral Governance include:

- Staying current on new regulations, trends, technologies and offerings.
- Having a network of professionals with which to share ideas and processes.
- Reaching out to others when more information or specialty expertise is needed.
- Being able to communicate complex ideas in simple ways.

Five Ways to Engage and Inspire Lay Fiduciaries

Governance is your ability to manage the details of a prudent decision-making process. Don Trone of 3Ethos has developed five ways to inspire lay fiduciaries.

1. Be authentic: simplify your communications; complexity is an inhibitor to forming trust.
2. Be aligned: look for an understanding of all their needs, not simply their goals and objectives.
3. Be attentive: look for opportunities to depart from the agenda to nurture a leadership and stewardship discussion.
4. Be adaptive: know how to transition from a leadership role to a stewardship role. When a lay fiduciary shows a desire to lead, become a steward of that person's leadership role.
5. Be accountable: ask how you can better serve key decision-makers at the end of each meeting.

Using the IPS: Legal Entities

	Legislation and Oversight				
	ERISA	**UPIA**	**UPMIFA**	**UMPERSA**	**IAA**
Type of Plan or Portfolio	• Corporate Retirement • Defined Contribution • Defined Benefit • Taft-Hartley • Employee Welfare	Private Trusts	Foundation/ Endowment	Public Retirement	Activities of Registered Investment Advisers and Investment Advisor Reps, including advice to retail investors. Applies in addition to any other Act.
Oversight	DOL, IRS, PBGC	State Attorney General	State Attorney General	State Attorney General	SEC or State Securities Administration

This chart summarizes the significant sources of fiduciary legislation, the types of fiduciary portfolios they apply to, and the entity that oversees and enforces responsibility. In some cases, more than one organization has oversight.

Using Investment Policy Statements as an Investment Tool

Corporate-qualified retirement plans come under ERISA, a federal law with primary oversight from the Department of Labor. Due to the tax implications, the Internal Revenue Service oversees some aspects of these plans. The quasi-government organization, the Pension Benefit Guarantee Corporation, also has skin in the game for defined benefit plans.

Taft-Hartley plans are a unique subset of ERISA. They have several additional requirements because multiple employers are responsible for contributions instead of a single employer for the typical defined benefit plan.

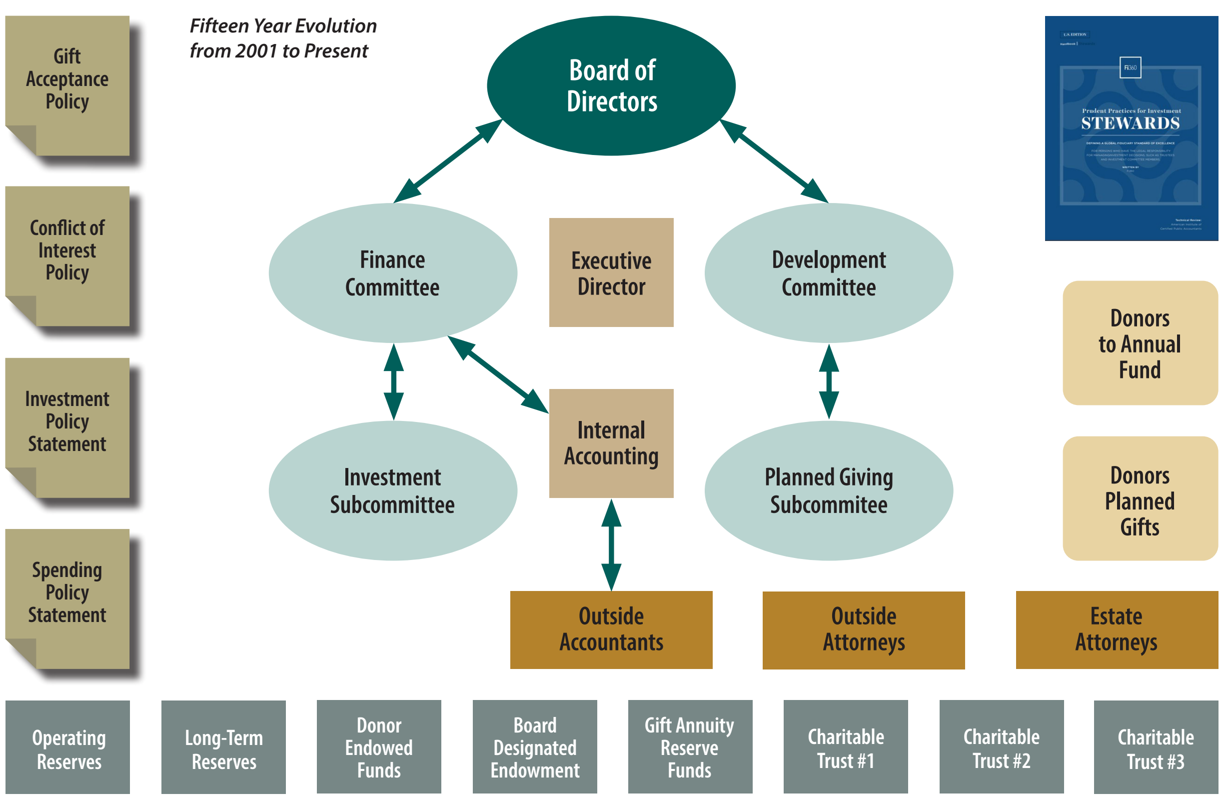
State laws regulate private trusts, and most states have adopted UPIA, a model law introduced in 1994. The Attorney General in each state has legal standing to investigate whether there are fiduciary breaches.

Foundations and endowments also come under state laws now guided by UPMIFA, a uniform law introduced in 2006 to replace UMIFA. Most states have adopted UPMIFA. Substantively, UPMIFA has most of the same fiduciary practices as those codified under UPIA. The State Attorney General has oversight responsibility.

Public retirement plans come under state law. Although UMPERSA was introduced in 1997, only Maryland and Wyoming have adopted it. For the other states, you need to investigate and familiarize yourself with the governing law of that state. Again, the State Attorney General has legal oversight responsibility for public employee retirement system plans.

Finally, the Investment Advisers Act of 1940 is an essential legislation governing investment advisors' activities. The Adviser's Act is unique because the word fiduciary is not directly referenced in the Act. Despite this, the Act is fiduciary legislation backed by strong case law and regulatory rulemaking. The Securities and Exchange Commission and state securities administrators have oversight responsibility for investment advisors.

Nonprofit Governance, Strategy, Policy & Procedure



Using Investment Policy Statements as an Investment Tool

Using the IPS: Promoting Investment Stewardship in Charitable Organizations

The investment policy statement is vital to many different groups within a nonprofit organization. Regarding investment stewardship, John Griswold, Executive Director of Commonfund Institute, writes, "After the hiring of a chief executive, the most important function of a board is maintaining the financial equilibrium of the institution, including management of its long-term funds and oversight of its operating funds, revenues and expenses."

To promote your investment stewardship:

1. Listen to your donors
2. Adopt fiduciary best practices
3. Avoid conflicts of interest
4. Know your people (and their roles)
5. Develop investment stewardship fact sheet

Charitable organizations have a significant opportunity to use their investment policy statement to prove their investment stewardship. Transparency builds confidence in the board of directors of an organization and may inspire larger gifts.

- Transparency
- Full disclosure: posting their essential information and documents:
    - Income tax returns
    - Names of board members
    - Names of investment committee members
    - Investment policy statement

Creating an Investment Stewardship Fact Sheet

Create an "Investment Stewardship Fact Sheet" to explain your investment stewardship. Create the fact sheet collaboratively with the CFO, finance committee, investment committee, accounting staff, external investment advisors, custodians and trustees. Use the document for donor communications, phone calls, letters, meetings and the website.

Using the IPS: Building Board Consensus

A well-written investment policy statement will help your organization establish board consensus. Share a copy of the IPS with every new board member in their initial "Welcome to the Board" packet. Share a copy of the IPS with every new finance and investment committee member at their first committee meeting.

Recruit process-oriented board members. Review the IPS at annual review meetings and submit it to the board for approval. By distributing the IPS, you will educate your board on fiduciary standards. Consider a "fiduciary review." Define the investment advice providers.

Develop a one-page IPS for use as a donor development tool. Clarify how planned gifts are to be received and managed. Communicate quarterly performance to all parties. Work to define and establish a governance framework. Develop goals as you draft the IPS. Without an Investment Policy Statement containing a governance framework with bylaws, investment decision-making process and goals, the organization lacks direction. A sample case study illustrates this point.

Using Investment Policy Statements as an Investment Tool

Nonprofit Case Study Example

Challenge: A nonprofit organization had $2 million invested in short-term certificates of deposit at a local bank earning modest returns. The committee members were interested in a portfolio that could be invested for a longer time horizon to provide greater returns over time. They did not have any investment decision-making processes in place or an investment policy statement (IPS) to oversee the portfolio.

After several meetings with the investment committee members, their advisor learned about their investment objectives, risk tolerance and time horizon for the portfolio. The first and most critical step was to help them draft an investment policy statement (IPS). In addition to assisting the committee in developing the IPS, their advisor provided a governance framework for the investment committee that included member bylaws, an annual governance calendar and a gift acceptance policy.

Result: The investment committee members now have an investment policy statement customized to their situation, and they have a better understanding of their fiduciary responsibilities. The IPS clearly defined how the funds could be invested, how the investments would be monitored, and how each fiduciary's role and duties should be executed in the future. Their advisor's continued assistance through quarterly review meetings has helped the investment committee members to stay on track and feel secure that they were making sound investment decisions for their organization and meeting their fiduciary responsibilities.

Summary

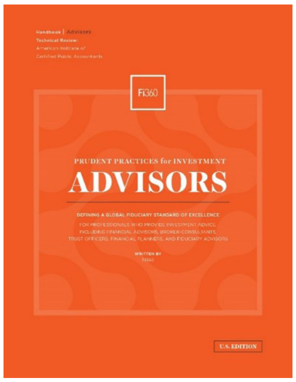
Many investors, investment committee members, board members or other nonprofit leaders do not realize they may be fiduciaries under the law. They may not fully understand their investment philosophy or decision-making responsibilities. Fortunately, they are not alone. Tools exist to help them. These tools include formulating a formal Investment Policy Statement and implementing the Fiduciary Quality Management System developed by Fi360. This paper outlines the components within these tools, including the roles and responsibilities, the necessary steps to draft the IPS, and instructions for how to use the IPS. Resources such as an annual governance calendar, specific directions for documenting decisions, guidelines for building board consensus and other practical tips are also included.

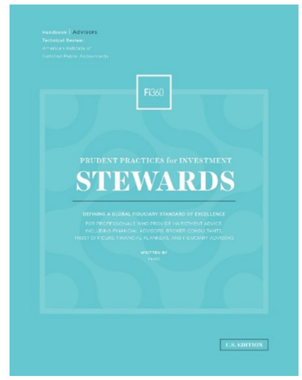
Using Investment Policy Statements as an Investment Tool

Educational Handouts and Resources

Fi360 resources and Prudent Practices handbooks: www.fi360.com
CEFEX resources: https://www.cefex.org/
Allodium: https://www.allodium.com/resources/educational/fi360-documents.html

2020 PIP Handbooks





Source: © Fi360, a Broadridge Company

1. *The Prudent Practices:*
   - 2020 *Prudent Practices for Investment Stewards* handbook
   - 2019 *Prudent Practices for Investment Advisors* handbook
   - 2013 *Prudent Practices for Investment Managers* handbook
   - 2021 Self-Assessment of Fiduciary Excellence for Investment Stewards (SAFE)
   - 2017 Periodic Table of Global Fiduciary Practices for Investment Stewards
   - 2012 Fiduciary Placemat

2. *The Fiduciary Score:*
   - Two Page Fiduciary Score Methodology
   - Eight Page Fiduciary Score Methodology
   - MacrRisk Research Report Evaluating the Value Added by the Fi360 Fiduciary Score
   - 2017 CFPI Analysis of the Fi360 Fiduciary Score: "Red is STOP, Green is GO"
   - The Value of the Fi360 Toolkit for Clients of Advisors

3. *Investment Committee:*
   - Bylaws for the Formation of an Investment Committee
   - Fiduciary Acknowledgment Letter and Response
   - 2016 Periodic Investment Review Checklist

4. *Hiring Investment Advisors:*
   - The Benefits of Choosing an AIF Designee for Individual Investors
   - The Benefits of Choosing an AIF Designee for Investment Stewards
   - Questions a Steward Should Ask
   - How Clients Benefit from Their Advisor's CEFEX Certification
   - The Road to Fiduciary Security Begins with a CEFEX Certified Advisor

5. *Sample Investment Policy Statements:*
   - 2013 Fi360 Sample Investment Policy Statement for a Personal Trust
   - 2013 Fi360 Sample Investment Policy Statement for an Individual
   - 2013 Fi360 Sample Investment Policy Statement for a Foundation
   - 2008 Fi360 Sample Investment Policy Statement for a Personal Trust
   - 2007 Fi360 Sample Investment Policy Statement for an Individual IRA Account
   - 2005 Fi360 Sample Investment Policy Statement for a Foundation
   - 2005 Fi360 Sample Investment Policy Statement for a 401k Plan
   - 2003 Fi360 Sample Investment Policy Statement for a Foundation
   - 2002 Fi360 Sample Investment Policy Statement for a Defined Contribution Retirement Plan
   - 2002 Fi360 Sample Investment Policy Statement for a Defined Benefit Plan
   - 2002 Fi360 Sample Investment Policy Statement for an Individual Investor
   - 2002 Fi360 Sample Investment Policy Statement for a Foundation

Allodium Educational Resource Sample Documents:

1. *Investment Policy Statements:*
   - Sample Investment Policy Statement Outline
   - 2011 Sample Family Foundation Investment Policy Statement
   - 2010 Sample Anchor Foundation Investment Policy Statement

2. *Fiduciary Management:*
   - Fiduciary Audit File Checklist
   - Historical Record of Investment Policy Decisions
   - Annual Governance Calendar

3. *Allodium White Papers:*
   - An Evidence-Based Approach to Sustainable Investing
   - The ABCs of Behavioral Biases
   - Food for Thought: Reducing the Risk of Black Swans
   - Evidence-Based Investment Insights
   - The Viability of the Value Premium
   - Trustee Intelligence: The Role of the Investment Management Consultant
   - Accelerating Impact Investing for Foundations and Endowments: Aligning Your Leadership and Stewardship with Your Fiduciary Responsibilities
   - 15 Ways to Enhance Donor Trust by Improving Your Investment Stewardship

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