Sample Investment Policy for Nonprofits Having Endowment Funds

The New York Prudent Management of Institutional Funds Act ("NYPMIFA") requires the adoption of an "investment policy" by all corporations subject to its provisions.[1] This draft sample investment policy is intended for consideration by a nonprofit that (i) holds cash equivalents (such as bank deposits) as well as longer-term investments including endowment funds and (ii) delegates or permits delegation of authority to invest or manage its assets to committees, officers, employees or external agents.[2]

The provisions in red are required by NYPMIFA. Nonprofits should keep in mind that modifications to this draft sample policy may be appropriate in light of the organization's circumstances and the investment policy adopted by the organization should reflect policies and procedures to which the organization can readily adhere. However, care should be taken to ensure that the NYPMIFA-mandated provisions are included in the organization's policy.

The draft sample policy is not intended as investment advice, and, except with respect to NYPMIFA, it does not contain any references to, or information regarding, state, federal, regulatory or other requirements that may be applicable to the nonprofit. Legal counsel should be consulted concerning any other provisions that may need to be included. The New York Attorney General has not approved or reviewed this draft sample policy.

Investment Policy

for

[Full Name of Nonprofit] ("the Corporation")

Adopted [Insert Date]

Purpose

The purpose of this policy is to set forth the standards and guidelines governing the investment and management of the Corporation's financial assets. A separate appendix sets forth standards and guidance for the expenditure of the Corporation's endowment funds.[3] This policy is intended to be in accordance with the New York Prudent Management of Institutional Funds Act ("NYPMIFA").

Financial Assets of the Corporation

The Corporation's financial assets consist of (a) funds intended to be used to cover its short-term operating and program expenses (the "Operating & Program Fund"), (b) reserve funds, which are funds to be held in reserve to support the Corporation's future operations, serve as a resource during economic downturns or provide an additional source of income to support and further the Corporation's mission (the "Reserve Funds"), (c) funds which have been restricted by the donor or the Corporation's Board of Directors (the "Board of Directors" or the "Board") for a specific purpose, but which do not have a restriction as to the timing of their expenditure (the "Restricted Funds"), and (d) funds received by the Corporation pursuant to a gift instrument[4] that are not wholly expendable by the Corporation on a current basis (the "Endowment Funds" and together with the “Operating & Program Fund,” the “Reserve Funds” and the "Restricted Funds," the “Funds”).[5]

Financial assets subject to a specific donor restriction as to the investment, management, use or expenditure of such assets shall be invested, managed, used and spent in accordance with the donor's restriction.

Investment and Management Objectives and Guidelines

Operating & Program Fund: The Operating & Program Fund shall be invested with the objective of preserving its assets to cover operating expenses and realizing earnings in a way that allows for immediate liquidity to meet the Corporation's ongoing programmatic and operational needs. Operating & Program Fund assets may be maintained in the checking account that the Corporation uses for day-to-day operations and may be invested in other cash-equivalent investments, such as savings accounts, money market accounts, certificates of deposit with maturities appropriate for expected needs, Treasury bills and other investments that are relatively easy to liquidate. The Corporation’s professional staff from time to time will review the allocation (or the methodology of allocation) of Operating & Program Fund assets between the Corporation’s checking account and its other cash-equivalent investments, determining the appropriate allocation based on the Corporation’s cash-flow needs, and regularly report such allocation to the Board. The Board may direct that changes be made to such allocation and will also consider from time to time whether the Corporation's Operating & Program Fund assets are sufficient to allow for the designation of a portion of such assets to the Reserve Funds.

Reserve Funds: The Reserve Funds shall be invested with the objective of preserving the long-term real purchasing power of the Funds' assets while realizing appropriate investment income. Reserve Funds' assets may be invested in certificates of deposit, Treasury bills, mutual funds, exchange traded funds, equities [ADD LIMITATIONS, SUCH AS “traded on a U.S. public exchange” OR EXCLUSIONS, SUCH AS “(excluding [List exclusions such as “stock not publicly traded on a U.S exchange,” “preferred stock,” “convertible securities,” etc.])”], fixed income securities and, as to an appropriate portion, cash equivalent investments.[6] The asset allocation of each of the Reserve Funds shall be determined from time to time by the Board of Directors, in consultation with any managers or advisors if desired (unless it delegates such task to an external manager), which allocation shall reflect a proper balance of such Fund's investment objective, any risk tolerance standard and the need for liquidity.

Restricted Funds: The Restricted Funds shall be invested with the objective of preserving and enhancing the purchasing power of the Funds' assets while ensuring that liquidity requirements can be met. Restricted Funds' assets may be invested in certificates of deposit, Treasury bills, mutual funds, exchange traded funds, equities [ADD LIMITATIONS, SUCH AS “traded on a U.S. public exchange” OR EXCLUSIONS, SUCH AS “(excluding [List exclusions such as “stock not publicly traded on a U.S exchange,” “preferred stock,” “convertible securities,” etc.])”], fixed income securities and, as to an appropriate portion, cash equivalent investments. The asset allocation of each of the Restricted Funds shall be determined from time to time by the Board of Directors, in consultation with any managers or advisors if desired (unless it delegates such task to an external manager), which allocation shall reflect a proper balance of such Fund's investment objective, any risk tolerance standard and the need for liquidity.

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Endowment Funds: The Endowment Funds shall be invested with the objective of preserving the long-term real purchasing power of the Funds' assets while realizing appropriate investment income. Enowment Fund assets may be invested in certificates of deposit, Treasury bills, commercial paper, bankers acceptances, repurchase agreements, mutual funds, exchange traded funds, equities (including common stock, preferred stock, convertible securities and other equities, whether traded on an exchange or not publicly traded), fixed income securities, real estate, commodities, natural-resource related stock, hedge funds, derivatives, alternate investment vehicles and, as to an appropriate portion, cash equivalent investments. The asset allocation of each of the Endowment Funds shall be determined from time to time by the Board of Directors, in consultation with any managers or advisors if desired (unless the Board delegates such task to an external manager), which allocation shall reflect a proper balance of such Fund's investment objective, any risk tolerance standard and the need for liquidity.

Diversification

Investments of each Fund will be diversified to limit the risk of loss resulting from the concentration of assets in a specific type of investment, specific maturity, specific issuer or sector unless the Board prudently determines that, because of special circumstances, the purposes of the Fund are better served without diversification. The Board shall review the diversification strategy periodically, provided, however, that it shall review any decision to not diversify as frequently as circumstances require but, at a minimum, annually.

Responsibilities of the Board of Directors in Managing and Investing the Corporation's Financial Assets

In managing the financial assets of the Corporation, the Board of Directors will act in good faith and with the care an ordinarily prudent person in like position would exercise under similar circumstances. When making investment and management decisions, the Board shall consider the Corporation's purposes, as well as the purposes of the specific Funds.

In making decisions regarding management and investment of the Corporation’s financial assets, the Board of Directors, as required by applicable law, shall consider the following factors, if relevant:

(1) general economic conditions;
(2) the possible effect of inflation or deflation;
(3) the expected tax consequences, if any, of investment decisions or strategies;
(4) the role that each investment or course of action plays within the overall investment portfolio of the specific Fund;
(5) the expected total return from income and the appreciation of its investments;
(6) other resources of the Corporation;
(7) the needs of the Corporation and the specific Fund to make distributions and to preserve capital; and
(8) an asset's special relationship or special value, if any, to the purposes of the Corporation.

The Board of Directors shall not make management and investment decisions regarding an individual asset in isolation but rather in the context of the specific Fund's portfolio of investments as a whole and as part of an overall investment strategy having risk and return

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objectives reasonably suited to the Fund and the Corporation. The Board shall make reasonable efforts to verify facts relevant to the management and investment of the Funds and may incur only costs that are appropriate and reasonable in relation to the assets, the purpose of the Corporation and the skills available to the Corporation.

Within a reasonable time after the Corporation's receipt of a gift of property or other financial assets, the Board shall make and carry out decisions regarding retaining or disposing of the property, or the rebalancing of the Fund or Funds applicable to such gift in order to ensure compliance with the purposes, terms, and distribution requirements of the Corporation (including the diversification requirements and other aspects of this policy) as necessary to meet other circumstances of the Corporation and the requirements of applicable law, subject to any restrictions imposed by the terms of the gift.

The Board may delegate one or more of its responsibilities with respect to the management and investment of the Corporation's financial assets to a committee of the Board or an officer or employee of the Corporation. Any such committee or individual to whom such responsibility is delegated shall report to the Board on a regular basis and shall be subject to direction by the Board. If such responsibilities are delegated to a committee or individual, the rights and obligations set forth in this policy applicable to the Board (other than the right to amend this policy) shall also apply to such committee or individual, subject to the right of the Board to review and revise any decision of such committee or individual, and reports required under this policy to be made to the Board may instead be made to the committee or individual, which or who shall in turn report to the Board on a regular basis.

Delegation of Management and Investment Authority to an External Agent

To the extent it considers prudent, the Board may delegate management and investment decisions to one or more external agents, such as a bank, investment advisor, investment manager or custodian, except where prohibited by the terms of a gift instrument. The Board will act in good faith and with the care an ordinarily prudent person in like position would exercise under similar circumstances in (i) selecting, continuing or terminating any external agent (including assessing the agent's independence, including any conflicts of interest such agent has or may have;[7] (ii) establishing the scope and terms of the delegation, including the compensation to be paid; and (iii) monitoring the agent's performance and compliance with the scope and terms of the delegation. The Board, in making the decision as to whether to delegate such functions to a specific external agent, shall conduct such due diligence as the Board deems appropriate, such as reviewing information regarding the external agent's experience, personnel, track record and proposed compensation as compared to appropriate peers. Any external agent to which management and investment authority is delegated owes a duty to the Corporation to exercise reasonable care, skill and caution to comply with the scope and terms of the delegation.

Any external agents shall provide the Board with reports on investment performance on a quarterly basis, at a minimum, and more frequently if so requested by the Board. The Board will assess at least annually the performance and independence of any external agent, including any conflicts of interest it may have. Any actual or potential conflicts of interest involving a member of the Board or officer or key employee of the Corporation with respect to the external agent must be disclosed and resolved pursuant to the Corporation's conflict of interest policy and any conflicts of interest the agent may have involving service to the

Corporation (e.g., investment in deposits of a bank owned by the agent's brother) must also be disclosed to the Corporation. Any contract between the Corporation and an external agent involving delegation of investment authority shall be terminable by the Corporation at any time, without penalty, upon no more than 60 days' notice.

The Board of Directors will also review from time to time the Corporation's arrangements with any investment managers, investment advisors, custodians and the banks and other entities with which the Corporation maintains its financial assets to ensure that the costs and fees associated with each such arrangement are appropriate and reasonable in relation to the assets, the Corporation's purposes and the skills available to the Corporation.

The Corporation will seek to ensure that any investment managers retained by the Corporation invest the Corporation's investment assets in accordance with this policy and any specific guidelines for the investment manager established by the Board of Directors, which may include return and risk expectations, asset allocations and investment strategies (including allowed and prohibited investments). Specific guidelines established for investment managers will be reviewed from time to time by the Board of Directors and revised as necessary. Decisions as to the selection of individual investments, security size and quality, number of industries and holdings shall be left to the broad discretion of the investment manager, within the limits set forth in this policy and any specific guidelines established by the Board, and subject to the prudence standards under NYPMIFA.

Spending from Endowment Funds

Decisions with respect to spending from the Corporation's endowment funds shall be made in accordance with the Endowment Spending Policy set forth in Appendix A of this policy.

Review of Investment Policy

The Board will review this policy, and shall amend the policy, from time to time as necessary to reflect developments affecting the Corporation's finances and activities.

Additional Provisions That Might Be Considered for Inclusion

If the board of directors wishes to include in the organization's policy more detailed guidance, such guidance could address items such as, but not limited to:

- Investment philosophies, asset allocation guidelines, prohibited investments, and risk and return expectations for the Reserve, Restricted and Endowment Funds;
- Specific caps intended to promote diversification of the nonprofit's investment portfolio, such as caps on the market value of the portfolio that may be invested in any one industry, in the securities of any one company or in any asset class;
- Responsibilities of board committees, officers and/or staff if your board of directors has delegated management and investment authority to such internal delegates;
- Responsibilities of investment managers and custodians if your board of directors has delegated management and investment authority to such external agents;
- Guidance on the basic standards, rules and requirements that must be reflected in any specific guidelines established for investment managers;
- Whether restrictions should be imposed on the types of permitted investments for non-financial reasons (e.g., prohibitions on investments in certain industries, such as tobacco);

- Criteria for selecting and evaluating investment managers; or
- Criteria/benchmarks that will be used to evaluate the investment performance of the Reserve, Restricted and Endowment Funds.

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[1] NYPMIFA applies to all corporations incorporated under the New York Not-for-Profit Corporation Law or the New York Religious Corporations Law and to all education corporations as defined in Section 216-a(1) of the New York Education Law. Therefore, public charities, private foundations, social welfare organizations, trade associations, social clubs and all other entities incorporated under these laws will be governed by NYPMIFA.
[2] Also available on the Nonprofit Coordinating Committee of New York's website are (i) two draft sample investment policies appropriate for consideration by a nonprofit with some longer-term investments but no endowment funds (one of the two sample policies allows for delegation of investment management authority to external agents and the other policy does not) and (ii) a draft sample investment policy appropriate for consideration by a nonprofit that holds only cash equivalents and does not have either longer-term investments or endowment funds.
[3] NYPMIFA does not require nonprofits to have an endowment spending policy. Accordingly, in lieu of creating a separate endowment spending policy, a nonprofit could place its policies and procedures governing the appropriation of endowment funds for expenditure directly in the nonprofit's investment policy. The nonprofit should ensure, however, that NYPMIFA's rules for appropriating endowment funds for expenditure are memorialized in a document that is shared with and approved by the Board and guides the Board's decisions with respect to such appropriation. The purpose provision of this policy should be revised accordingly if there is no separate spending policy.
[4] In the context of an endowment fund, a gift instrument may be (i) a gift agreement between the donor and the Corporation creating or contributing to an endowment fund; (ii) the Corporation's solicitation materials in which the Corporation represents that funds received from the solicitation will be endowed funds; (iii) minutes of a Board of Directors meeting at which a donor's gift of endowed funds is announced; or (iv) any other record under which a fund is granted, transferred or conveyed to the Corporation containing a directive from the donor that makes the fund an endowment. Funds that are not restricted as to expenditure under the terms of a gift instrument but have been so restricted by action of the Corporation's Board of Directors (the "Board of Directors" or the "Board") are not endowment funds.
[5] NYPMIFA's rules governing the investment and management of a nonprofit's financial assets apply to the nonprofit's operating funds, as well as its reserve, restricted and endowed funds. (All such funds are referred to as "institutional funds" in NYPMIFA.)
[6] This list, as well as the list of Restricted Fund assets and list of Endowment Fund assets set forth below, is not intended to be an exclusive list of the classes of investment assets in which the specific fund may be invested. In light of a nonprofit's particular circumstances, its board of directors may wish to expand the list of permissible investment assets for a specific fund and/or eliminate one or more of the suggested classes of investments or types of investments within a class.
[7] For example, the nonprofit's Board should consider whether any director, officer or key employee has any business or personal relationships with the external agent that the Board might reasonably expect to interfere with the Board's ability to properly monitor or assess the external agent's performance or receive independent investment advice from the external agent.

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Endowment Spending Policy
For
[Full Name of Nonprofit] (the "Corporation")

I. Purpose

The purpose of this Endowment Spending Policy is to set forth the standards and guidelines governing spending from the endowment funds of the Corporation.

An endowment fund is any fund, or a part of a fund, that, under the terms of the gift instrument,[1] is not wholly expendable by the Corporation on a current basis. Funds that are not restricted as to expenditure under the terms of a gift instrument but have been so restricted by action of the Corporation's Board of Directors (the "Board of Directors" or the "Board") are not endowment funds.

II. Appropriating Endowment Funds for Expenditure

All spending from each of the Corporation's endowment funds will comply with any donor restrictions on spending imposed on such fund and with the New York Prudent Management of Institutional Funds Act ("NYPMIFA"). In creating an endowment fund, the donor also may have restricted the purpose or purposes for which funds from the endowment may be spent. All decisions regarding expenditures from an endowment fund restricted as to purpose must comply with such purpose restrictions. Expenditures from endowment funds that are not restricted as to purpose may be used for any purposes of the Corporation.

Decisions to appropriate funds from each endowment for expenditure[2] or to accumulate such funds shall be made only by the Board of Directors. The Board may authorize a committee of the Board to assist the Board in carrying out its responsibilities with respect to the expenditure of the Corporation's endowment funds. Such committee may be authorized to make recommendations to the Board of Directors regarding the expenditure of the Corporation's endowment funds but the final decision as to such matters shall be made by the Board.[3] The Board committee, in making a recommendation to appropriate funds from each endowment for expenditure or to accumulate such funds, and the Board of Directors, in making a decision to appropriate funds from each endowment for expenditure or to accumulate such funds, must act in good faith with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, and must (a) consider the uses, benefits, purposes and duration for which the endowment fund was established and (b) consider each of the following factors, if relevant:

(1) the duration and preservation of the endowment fund;
(2) the purposes of the Corporation and the endowment fund;
(3) general economic conditions;
(4) the possible effect of inflation or deflation;
(5) the expected total return from income and the appreciation of investments;
(6) other resources of the Corporation;
(7) where appropriate and circumstances would otherwise warrant, alternatives to expenditure of the endowment fund, giving due consideration to the effect that such alternatives may have on the Corporation; and
(8) the Corporation's investment policy.

In accordance with NYPMIFA, decisions to appropriate endowment funds will be made on a fund-by-fund basis and in accordance with any specific directives on spending that the donor has imposed. Should the number of the Corporation's endowment funds become large enough that making annual appropriation decisions on a fund-by-fund basis becomes unduly burdensome or cumbersome, the Board of Directors or a Board committee so authorized by the Board, may classify the Corporation's endowment funds into groups of similarly situated funds for the purpose of allowing the Board, in accordance with the prudence standard set forth above, to determine each year an appropriate spending rate that should be applied to each such group of similarly situated funds. The factors that the Board or Board committee may consider in determining classes of similarly situated funds include: (i) the purposes of the funds as stated in the gift instruments; (ii) spending restrictions imposed by donors in the gift instruments; (iii) the durations of the funds; (iv) whether the funds are invested similarly; (v) the financial conditions of the funds; and (vi) such other factors as the Board or Board committee determines are relevant under the circumstances.

The Board of Directors or the Board committee shall review from time to time the classes of similarly situated funds and the composition of each such group to ensure that such funds are properly classified.

Specific donor directives on spending may preclude classification of an endowment fund into any class of similarly situated funds. When making an appropriation recommendation or decision from an endowment fund that includes such specific donor directives on spending, the Board committee, in making its recommendation, and the Board of Directors, in making its decision, shall consider the endowment fund separately and appropriations from such endowment fund will be made in accordance with any specific directives on spending that the donor has imposed.

III. Documenting Spending Deliberations

The Board committee, if any, and the Board of Directors each shall keep a contemporaneous record of its decisions regarding the appropriation of endowment funds for expenditure, describing the nature and extent of the consideration that the committee or Board gave to each of the eight factors listed in Section II above.

Under NYPMIFA, unless permitted by the donor in the gift instrument, an annual distribution from an endowment fund created on or after September 17, 2010 in an amount exceeding seven (7) percent of the fair market value of the fund, calculated based on market values determined at least quarterly and averaged over a period of at least the last twenty quarters ending with the last quarter of the fiscal year preceding the distribution (or for the number of quarters in existence for endowments more recently created), will create a rebuttable presumption that such distribution was imprudent. Accordingly, should the Board committee recommend and/or the Board of Directors decide, after acting in accordance with NYPMIFA's prudence standard as set forth above, that making an annual distribution in excess of seven (7) percent from such endowment fund is prudent, the Board committee and the Board each shall ensure that the contemporaneous written record documenting its recommendation or decision includes a detailed statement of the basis upon which the Board committee and/or Board determined that such annual distribution was prudent.

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[1] In the context of an endowment fund, a gift instrument may be (i) a gift agreement between the donor and the Corporation creating or contributing to an endowment fund; (ii) the Corporation's solicitation materials in which the Corporation represents that funds received from the solicitation will be endowed funds; (iii) minutes of a Board of Directors meeting at which a donor's gift of endowed funds is announced; or (iv) any other record under which a fund is granted, transferred or conveyed to the Corporation containing a directive from the donor that makes the fund an endowment.

[2] Under NYPMIFA, the assets in the Corporation's endowment fund may not be spent until they are "appropriated for expenditure" by the Corporation. Although the term is not defined in NYPMIFA, an appropriation is generally understood to mean a decision by the board of directors to release a portion of an endowment from the donor-imposed restriction on spending, thus authorizing it to be spent in accordance with the terms of the gift instrument. Funds appropriated for expenditure need not be spent immediately; they may be appropriated on one date and spent at a later date or over time.

[3] There is some uncertainty whether the decision to appropriate endowment funds for expenditure or to accumulate such funds can be delegated to a board committee, such as the executive committee or finance committee. NYPMIFA specifically authorizes the delegation of board investment-related responsibilities to board committees and outsiders but is silent on whether the appropriation decision can be delegated. Section 712 of the N-PCL, however, specifically allows delegation of most board duties to board committees and, accordingly, could be seen as providing the board with the power to delegate the appropriation decision to a board committee. We understand that the Charities Bureau is intending to issue guidance on this issue. Until such guidance is issued, it may be best to ensure that the final decision with respect to any appropriation or accumulation of endowment funds is made by the board of directors.