Board Governance Policy

BG II-03 Investment Policy for College Endowment Funds

Policy Category :	Finance		
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PURPOSE

This Policy provides guidelines within which the College's Endowment Funds are to be effectively maintained, managed and enhanced. The Board of Governors of Algonquin College has responsibility for approving the investment policies of the College and for monitoring the performance of the Endowment Funds' investments relative to established benchmarks.

The Algonquin College Endowment Funds have the following objectives:

- to provide a steady flow of income, in perpetuity, to meet expenditure requirements as defined in section 3 of this policy. Ideally the income stream should grow each year in order to maintain the purchasing power of the Endowment Funds being disbursed; and

- to increase the market value of the Endowment Funds so that capital, in real terms, is maintained. This is achieved by increasing the balance held in the Endowment Funds by an annual amount that offsets the inflationary erosion of this Funds.

To meet the above objectives, the College invests its Endowment Funds in a diversified portfolio of Canadian and Global equities and Canadian and US Fixed Income instruments.

Endowment Funds are invested in accordance with this policy, unless otherwise bound by contract or by donor specifications.

POLICY

1. GENERAL GUIDELINES

1.1. Endowment Funds are to be held by the College in perpetuity, with the primary objective for the portfolio to achieve a rate of return sufficient to meet their annual obligations as defined in section 3 of this policy and grow at a rate greater than inflation to ensure maintenance of their value.

1.2. An asset mix policy of 65% in Equities and 35% in Fixed Income will provide an investment strategy that will balance the competing needs of a stable income stream and long term growth of the Endowment Funds.

1.3. External investment counsel will manage the Endowment Funds. The Investment Counsel will report to the Finance and Administrative Services Department of the College on the performance of the Endowment Funds no less frequently than quarterly. The performance of the Endowment Funds will be reported at least annually to the Board of Governors of the College.

1.4. All investment activities must be conducted in accordance with the Code of Ethics and Standard of Professional Conduct adopted by the CFA Institute.

1.5. It is intended that this policy comply with all relevant government legislation and regulations. Investment of Endowment Funds must comply with the Ontario Colleges of Applied Arts and Technology Act, 2002 and specifically the Banking and Investments Minister's Binding Policy Directive with reference to the Trustee Act.

1.6. Assets held in the Endowment Funds will be classified and accounted for at fair value (Per CPA Canada Handbook PS 3450).

2. ASSET MIX POLICY AND ITS PRACTICAL IMPLICATIONS

2.1. The table below lists the asset classes that may be used and it presents the total fund asset mix policies, referred to as the Benchmark, together with the maximum and minimum exposures for each asset class, based on market value.

	Benchmark	Range
Cash or Cash Equivalents	3%	0-20%
Fixed Income	35%	25-45%
Canadian Equities	22%	12-32%
Global Equities	40%	30-50%

2.2. If investments in an asset class fall outside the minimum or maximum exposure as per section 2.1, the College must ensure that the asset mix is adjusted to be compliant within 90 days after the non-compliance is reported.

2.3. If more than one investment counsel is employed, each will be given an asset mix (which may differ from one investment counsel to another), such that the aggregate of the delegated asset mixes will be the mix defined above for the total Endowment Funds.

2.4. The asset mix above should be the one followed by the Endowment Funds, in the absence of any opinion on the part of investment counsel that any asset class offers particularly favorable opportunities at any time. If such opinions are approved, the Endowment Funds should deviate approximately from the asset mix policy, within limits to be prescribed to each investment counsel.

3. **EXPENDITURE RATE**

3.1. The College maintains separate general ledger accounts for all sources of Endowment Funds.

3.2. An expenditure rate set by the Board of Governors (currently 5%) of the Endowment Funds' Book Value at the end of the previous fiscal year shall be applied as follows:

- 4% to all Endowments listed at that date; and
- 1% to cover a portion of fundraising costs.

3.3. The difference between the total Endowment Funds' rate of return and the expenditure rate will be reinvested. This is intended to preserve the real value of the Endowment Funds over time. In the event that there is a significant accumulated surplus in the Endowment Funds, the Board of Governors may elect to use a portion of surplus funds to either increase current listed Endowments or increase donations (eg. through a donor matching program) to the Endowment Funds.

3.4. Notwithstanding the above, where required by donor specification, the expenditure rate will be in accordance with the specific goals of the program or donor.

3.5. The expenditure rate will be reviewed by the Board of Governors of the College every five years for appropriateness.

4. INVESTMENT PERFORMANCE BENCHMARKS

4.1. Given the asset mix policy of the Endowment Funds, the return of the Endowment Funds will be measured against the sum of the benchmarks for each asset class multiplied by the performance of the indices as follows:

Canadian Equities	S&P/TSX Composite Index
Global Equities	MSCI World (ex Canada) Index
Fixed Income	FTSE TMX Canada Universe Bond Index
Cash & Cash Equivalents	FTSE TMX Canada 30 day T-Bill Index

4.2. Professional investment counsel have been selected in the expectation that their combined judgments will, over time, enable the Endowment Funds to earn a return in excess of the neutral return specified above, after payment of transaction costs and investment management fees.

4.3. Accordingly, the most important performance benchmark against which the Endowment Funds' actual performance will be compared is the neutral return specified above.

4.4. Over a 5-year rolling average of the Fund's market value, a target rate of return of 5.6% is required to fund the expenditures including a 2% factor for inflation.

4.5. While the total performance of the Endowment Funds is the main consideration, the Finance and Administrative Services Department will also monitor the performance of each money manager's ability to make sound judgment calls and investment decisions for the performance of the Endowment Funds.

5. REVIEW PROCEDURES

5.1. The Finance and Administrative Services Department of the College shall review the performance of each investment counsel against the relevant benchmarks and objectives on a quarterly basis, with a view to measuring progress towards the relevant investment objectives.

5.2. The Finance and Administrative Services Department of the College shall meet with each investment counsel at least annually to discuss their performance and investment strategy.

6. VOTING RIGHTS

6.1. When Endowment Funds investments are made, voting rights may be acquired. The exercise of these voting rights is delegated to the Investment Counsel, with the instruction that they should be cast in favour of any proposals which, in the opinion of the Investment Counsel, secure or enhance the investment value of the relevant security, and against any proposals which, in the opinion of the Investment Counsel, expose to risk or reduce the investment value of the relevant security.

6.2. If the Investment Counsel or any of their officers has any pecuniary interest, direct or indirect, in any matter on which the Endowment Funds has a right to vote, the Investment counsel shall bring this to the attention of the Finance and Administrative Services Department, who is given discretion to,

6.2.1. instruct the Investment Counsel to exercise the voting right in line with the principles described in section 6.1 above, on the grounds that the relevant pecuniary interest is not material; or

6.2.2. instruct the Investment Counsel how to cast the Endowment Funds' vote, having considered the principles described in section 6.1 above.

7. PERMITTED INVESTMENTS

7.1. In general and subject to the restrictions noted below, the Endowment Funds may be invested in any of the investment instruments listed below:

7.1.1. Equities

This asset class is defined as being made up of common shares, mutual funds, convertible bonds, convertible and/or preferred shares and index funds. Derivative holdings (option contracts) may not be purchased under any circumstance. Equity instruments representing individual corporations or equity related indices must be listed on New York, American, National Association of Securities Dealers Automated Quotes (NASDAQ), Chicago or Toronto.

7.1.2. Fixed Income

This asset class may include bonds (Canada and the United States), debentures, GICs, strip bonds and investment grade corporate debt instruments as listed below:

7.1.2.1. Provincial bonds and provincial guaranteed bonds, must have a minimum credit rating of BBB (as rated by the Dominion Bond Rating Service).

7.1.2.2. Residual or strip coupon instruments representing direct debt obligations to the Government of Canada or a Province of Canada must have a minimum credit rating of BBB.

7.1.2.3. Corporate bonds or debentures, when purchased, must have a minimum credit rating of BBB with the limitation that holdings of such bonds may not exceed 50% of the market value of the bond portion of the portfolio.

7.1.3. Cash or Cash Equivalent

7.1.3.1. This asset class is defined as being made up of cash deposits, money market securities, Canada Savings Bonds, GICs, bonds with maturity of one year or less, Government of Canada Treasury Bills, bankers' acceptances and term deposits. Money market securities must be rated R-1 or/and may include mutual fund money market instruments offered by Canadian Mutual Fund Companies.

7.2. If an investment is reported to be below the standards required in sections 7.1.2 or 7.1.3 above, then the College is to sell the investment within 90 days after the day the non-compliance is reported.

7.3. The portfolio should hold a prudently diversified exposure to the intended market.

7.4. Investments may be made in the above asset classes either directly, or by holding units of a pooled, segregated or mutual fund investing in one or more of the asset classes.

MONITORING

8. RISK MANAGEMENT POLICY FOR ENDOWMENT FUNDS

The following risk statement is part of an overall risk policy framework to be adopted by Algonquin College's Endowment Funds to manage and control all known risks that could have an effect on these assets. The Algonquin College Endowment Funds ("Endowment Funds") is exposed to risks that are knowingly assumed and are necessary to implement its long-term investment objectives. While certain risks are unavoidable (for example market risk), other risks (or even subsets of the broader market risk) can be managed through proper planning, monitoring and implementation of various controls outlined in the Algkonquin College Endowment Funds Statement of Investment Policies and Goals ("Investment Policy Statement").

The investment plan of the Endowment Funds as well as the Funds itself are exposed to the following risk factors:

- The assets of the Endowment Funds are not sufficient to support its related liabilities and commitments;
- The expected needs of Algonquin College (i.e. what the Endowment Funds are expected to finance) outpace the growth of the assets that are needed to fund these needs;
- The assets of the Endowment Funds do not behave as expected and fail to deliver their expected long-term return objective. **This is the primary focus of this risk policy statement**. This risk statement does not address internal risks such as governance or strategic risks.

8.1. *Risk Policy*

8.1.1. Asset Return Risk

This is the primary risk and encompasses the possible risk that the return needed to grow the Endowment Funds and support the College's mission is not produced due to unexpected behaviour (i.e. higher than the knowingly assumed risk) of the investment vehicles chosen.

The specific risks that may cause assets to not behave as expected can be placed into three categories:

8.1.1.1. Asset Class Return Risk

This is the risk that the long-term expectations of any asset class turns out to be significantly different than expected due to unforeseen market, economic or political factors. These deviations from expectations may result from changes in expected returns, changes in volatilities or changes in asset class correlations or behaviours in relation to other asset classes. For example, the Great Credit Crisis of 2008 altered market correlation expectations between asset classes and challenged the previous norm; namely, almost all asset classes became highly correlated at the height of the crisis.

8.1.1.2. Risk Mitigation Strategy

College management meets at least annually with the appointed investment manager to review long-term return objectives for approved asset classes. Additionally, on a minimum five-year cycle, the College management seeks input from the existing portfolio manager on existing asset class allocations. The purpose of this review is to examine the appropriateness of approved asset classes, while considering new asset classes for inclusion or exclusion in managing the Endowment Funds.

Market risk is controlled through proper diversification across various asset classes. Expected allocations and control ranges are outlined in the Investment Policy Statement and are reviewed with the investment manager on annual basis.

8.1.2. Inherent Investment Risks

All investments are subject to one or more types of inherent risk. It is necessary and expected for the Endowment Funds to assume some level of risk to achieve needed returns and to meet its statutory obligations under the Ontario Trustee Act. For example, some inherent risk present in common investments include:

8.1.2.1. Capital Risk: The risk of losing part of the original investment.

8.1.2.2. Credit Risk: The risk that bond issuer will default on their obligation.

8.1.2.3. Inflation Risk: The risk that investment returns will be lower than the rate of inflation.

8.1.2.4. Interest Rate Risk: The risk that a change in interest rates will decrease the value of bonds, equities and all other asset classes.

8.1.2.5. Liquidity Risk: The risk that investments cannot be readily converted into cash at prevailing prices. (While this risk is low due to the nature of the Endowment Funds' investments, the Great Credit Crunch proved that Liquidity Risk exists even on a portfolio of bonds issued by the Canadian Government and the Provinces).

8.1.2.6. Market Risk: The risk that adverse volatilities will cause losses.

8.1.2.7. Risk Mitigation Strategy

The above risks are knowingly assumed by the Endowment Funds in order to generate the required rate of return that will fund annual withdrawals while preserving the real value of invested capital in the long run.

The Investment Policy Statement therefore identifies investment return objectives, approved asset classes and any limitations to control risks within each asset class. For example the Investment Policy Statement should include references to:

8.1.2.7.1. Investments in Equities and clearly distinguish as being comprised only of the investments permitted as detailed in the Investment Policy Statement, and be listed on the exchanges as detailed in the Investment Policy Statement.

8.1.2.7.2. Investment in Fixed Income should clearly identify investable markets (Canadian bonds, U.S., International Developed Markets or Emerging Market debt) within the allocation. Likewise, limits are established and reviewed on the type of credit quality that will be ideal for the policy or investment cycle.

8.1.2.7.3. In the event that investments in Alternative Asset Classes (AAC) such as REITS, Private Equities, and other investments are held, they should be reviewed quarterly and limits should be placed within the Investment Policy Statement to control the commonly inherent risks they are exposed to (and any specific risks that are unique to this asset class).

8.1.2.7.4. The Investment Policy Statement that is subject to an annual review and possible amendments will detail what are approved and what are not approved asset classes and will establish limits to control the exposure to the specific risk factors outlined above.

8.1.3. Implementation Risks

Implementation risks are those that the Endowment Funds are exposed to in selecting the right manager or the right investment style (active vs. passive). Likewise implementation risk could include excluding a specific set of asset classes for the wrong reasons or a biased review due to a benchmark misfit during volatile economic or political times.

8.1.3.1. Risk Mitigation Strategy

The Investment Policy Statement reflects the need for a continuous review of these long-term implementation risks. Major elements of exposed implementation risk are reviewed on a five-year cycle. Likewise, the Audit and Risk Management Committee reviews of performance, meetings with the Investment Manager, and regular engagement and education in the investment business are the primary means for addressing this implementation risk.

8.1.4. Performance Shortfall

The assets of the Endowment Funds are expected to be invested to generate a target rate of return that will preserve the fund’s capital and provide the necessary income to fund the College’s annual obligations.

The expenditure rate is controlled by the Board of Governors while the rate of inflation is driven by uncontrollable market and economic factors.

To manage the risk of diluting the long-term capital of the Endowment Funds and to avoid excessive benchmark risk, the Endowment Funds will establish an investment return objective. This rate may be adjusted higher or lower based on changes to the expenditure rate or expected volatilities in inflation.

Performance shortfall is the measurement of the achieved long-term rate of return vs. the target rate of return (outlined above). For example, if the shortfall on a four-year rolling period exceeds 3%, corrective action may be required. These actions include but are not limited to:

- Changing the approved expenditure rate;
- Changing the approved asset classes and/or allocation limits within the Investment Policy Statement;
- Changing the existing Investment Manager.

Market benchmark performance can be used as a secondary benchmark but can lead to higher risks than desired and can inherently cause an unintended and natural performance shortfall.

8.1.5. Administration

8.1.5.1. All investment limits and risk controls such as maximum or minimum exposure by asset class or security and credit limits are included in the Investment Policy Statement and are not part of this Risk Policy. The limits in the investment policy should be reviewed annually with the asset manager for accuracy, completeness and appropriateness.

8.1.5.2. This Risk Management Policy is reviewed on an annual basis by the Audit and Risk Management Committee and the review should include the appropriateness of approved asset classes, desired long-term rate of return, the expenditure rate and other relevant risk policy issues.

PROCEDURE

The management of the assets of the Endowment Funds is delegated to the Finance and Administrative Services Department of the College, who will engage a professional investment consultant through a competitive process to act on the College’s behalf with quarterly due diligence monitoring.

RELATED MATERIALS

- Ontario Ministry of Advanced Education and Skills Development, Minister's Binding Policy Directive 2.0 Banking, Investments and Borrowing

- Ontario Colleges of Applied Arts and Technology Act, 2002