Litchfield Historical Society

Investment Policy Statement

I. Purpose

An Investment Policy Statement outlines and prescribes a prudent and acceptable investment philosophy and defines the investment management procedures and long-term goals for the organization. The principal reason for having a written investment policy is to protect the portfolio from ad hoc revisions of sound long-term policy. The written policy will help maintain a long-term policy when short-term market movements could cause the Finance Committee to doubt its investment strategy. In addition, under The Uniform Prudent Investor Act, it is required by law that individuals acting in a trustee or fiduciary role must clarify the process by which all investment decisions will be made. The law makes clear that following a prudent process is the key criteria for judging whether or not trustees were acting prudently, not whether the investments make or lose money.

II. Philosophy

The Litchfield Historical Society (LHS) or "the Society" preserves and interprets all aspects of Litchfield County History through its museum, the Helga J. Ingraham Memorial Research Library, the Tapping Reeve House, and The Litchfield Law School. The Society's Endowment was established to help fund the operations and capital improvements of the Society and its museums.

III. Finance Committee

The role of the Finance Committee or "the Committee" is to work in conjunction with the Investment Manager "Clarfeld" to establish, monitor and refine an Investment Policy Statement that assists it and the Board in effectively monitoring, evaluating and comparing the performance results of the Investment Manager. To facilitate effective communications, the Investment Manager should meet with Committee on a quarterly basis.

The majority of the Committee will consist of Society Board members. It can invite members of the community who have investment experience to serve on the Committee.

IV. Investment Objectives

The Society's objectives mirror the conservatism and long-term outlook of the organization – To provide a reasonable cash flow for current operating requirements and growth for future capital needs. At the same time protection of the purchasing power of the Society's assets is essential – to shield assets from market volatility significantly in excess of market indices.

As such, the Society will embrace a balanced approach to the portfolio that provides a total return (defined as realized and unrealized capital gains as well as dividend and interest income). This total return should be viewed in the context of a five to seven year period to allow for the volatility of the markets. Investment guidelines should be expressed with quantifiable ranges and the Society's investment manager should seek to achieve the objectives within these ranges.

The Society utilizes and adheres to the tenets of modern portfolio theory to optimize risk-return utilizing a diverse portfolio including a variety of asset classes. The Endowment consists of two accounts: The General Account and the Seherr-Thoss Endowment Account. Both accounts will be managed with a similar investment mandate.

Each portfolio will operate with a similar investment mandate inclusive of guidelines and investment parameters pertaining to risk and return, as outlined below:

Liquidity Provisions
At the time of preparation of the annual budget the Finance Committee will determine the estimated funds which will be made available for the forthcoming year. The performance of the portfolio over the past two years, its performance anticipated during the forthcoming year and expected inflation, as measured by the consumption price deflator, will all be considered. The goal is to withdraw no more than 5% of the total in any one year. This will provide a basis for the budgeting process and also provide the Investment Manager with a liquidity target for the forthcoming year.

The Society will determine the level of capital needed for each account. As projections, needs and cash flow change, the Committee will be required to re-asses previous capital allocation decisions. Ample liquidity in each component of the overall LHS portfolio will be maintained, and assets can be moved in kind, thereby reducing the costs associated with the capital allocation decisions on behalf of the Finance Committee.

A. The General Account

Balanced Growth: Funds are intended to be invested with a medium to long-term investment time horizon (five to seven years). The primary objectives are protection of principal and purchasing power and generation of a stable level of current income. Future capital appreciation is a secondary objective. Modest annual principal fluctuation is expected and acceptable. The portfolio will consist of a determined allocation among equities, fixed income, and cash.

Withdrawals from the General Account are based upon a total return calculation.

B. Seherr-Thoss Endowment

Balanced Growth: Funds are intended to be invested with a medium to long-term investment time horizon (five to seven years). The primary objectives are protection of principal and purchasing power and generation of a stable level of current income. Future capital appreciation is a secondary objective. Modest annual principal fluctuation is expected and acceptable. The portfolio will consist of a determined allocation among equities, fixed income, and cash.

Withdrawals from the Seherr-Thoss Endowment Account are based upon income from dividends and interest only.

V. Risk Tolerance

Investment theory demonstrates that over long periods, there is a relationship between the levels of risk assumed and expected returns. In general, higher risk (or volatility) implies higher returns.

There is no investment that is risk free. There are various sources of risk, including individual investment risk (price, yield, credit, and default risk), market risk, liquidity risk, and inflation risk. Asset diversification spreads the portfolio's investments among different classes to reduce individual investment (non-systemic) risk. Asset allocation spreads investments among different asset classes to reduce market risk. Systemic risk, however, is common to all securities and cannot be eliminated entirely.

Risk will be adequately considered when undertaking every investment decision. The investment manager will seek to reduce risk when possible, however, is cognizant of the fact the in order to generate suitable returns, some level of risk must be assumed.

VI. Asset Allocation

The portfolio's asset allocation strategy, including permissible asset classes and applicable guidelines, is described below.

1. **Strategic Asset Allocation:** Long-term asset allocation based on expected returns, volatility, and the client's unique risk tolerance and/or investment objectives. It is expected that changes in the client's risk tolerance and/or investment objectives will be the primary driver of changes to the Strategic Asset Allocation. The Investment Manager will recommend changes to the Strategic Asset Allocation as part of its annual review of the IPS.

2. **Tactical Asset Allocation:** A tool of active management that establishes a short-term asset allocation in order to take advantage of valuation discrepancies in specific asset classes. The objective of this periodic bias is to produce incremental returns on top of those of an already diversified portfolio. Changes in the Tactical Asset Allocation are infrequent and disciplined, based on the concept that continuous or severe shifts in and out of asset classes introduces "market timing," which increase inefficiencies and market risk.

3. **Asset Class Constraints:** The weighting of each asset class shall be constrained within the Strategic Asset Allocation target ranges below. This constraint serves as a trigger to rebalance the portfolio, as well as a constraint within which tactical shifts to the portfolio must remain.

4. **Rebalancing:** Shall take place if the weighting of any asset class is outside of the Asset Class Constraints, or reviewed for compliance with overall policy allocations at least semi-annually. A rebalancing of the portfolio should bring the weightings of each asset class listed above back in line with its Strategic Asset Allocation ranges. If there has been a short-term tactical change within an asset class, the investment manager will correspondingly adjust the rebalancing process in line with this change. The shift in exposure will subsequently be reviewed with the Society for approval. Trading costs should also be considered prior to rebalancing the entire portfolio.

The most important aspect of any investment strategy is the allocation of investments among the various asset classes. More than any other investment decision, it is asset allocation that will drive the performance of the portfolio. The Investment Manager has selected the following asset classes and long-term asset allocation ranges for the portfolios:

<u>The General Account and Seherr-Thoss Endowment Account</u>

	Min *Range*	***Max*** *Range*	
Class	***35%***	***100%***	**Index**
Cash	0%	25%	3-Month T-Bill
Fixed Income	35%	75%	Barclays Aggregate
Class	***20%***	***65%***	**Index**
US Large Cap Equities	10%	40%	S&P 500
US Small Cap Equities	3%	15%	Russell 2000
International Dev. Equities	4%	20%	MSCI EAFE
Emerging Market Equities	1%	5%	MSCI EM
Real Estate	1%	5%	FTSE NAREIT
Commodities	1%	5%	Bloomberg Commodities

**See Appendix A for definitions.*

An important distinction to the ranges listed above is during the period of initially transitioning the account to its prospective asset allocation, ***forecasted between 6-12mos***; the accounts may be in violation of the recommended long term asset allocation policy weights outlined above. This is specifically addressed as a function of the investment manager being cognizant of the current market environment and the fiduciary responsibility to act in the best interest of the Society. Given the large disparity from the current asset allocation to the projected strategic allocation, there is a need for the investment manager to have a suitable timeframe to transition the portfolio in order to ensure the primary investment objectives are being met.

As the values of various asset classes' change with market conditions, the investment manager will seek to rebalance the portfolio as needed in order to maintain the asset allocation (policy weights). The Investment Manager will review the portfolio on a quarterly basis and adjust weightings if actual weights vary significantly from their policy weights. Strategic allocations will be reviewed annually by the Committee. While the allocations can be adjusted anytime, (with ratification by the Board), the goal being to stay as close to the strategic allocation as possible, barring 1) Unforeseen funding issues of the organization, 2) A change in the scope of LHS operations, or; 3) Material changes in long-term expectations for financial markets.

<u>VII. Permitted Investments</u>

Permissible security types for investment in the aforementioned asset classes include liquid mutual funds, exchange traded funds (ETFs), or diversified separately managed accounts. In the event that a separately managed account is used within the asset allocation, the aforementioned account will be governed by a specific investment policy statement that would require ratification by the Finance Committee.

If LHS receives gifts of securities, it will be the policy to liquidate all individual security gifts and invest the proceeds as outlined in the Investment Policy Statement.

Prohibited asset classes or security types would include:

- Individual stock or bond purchases

- Other prohibited trades would include short sales of individual securities, purchases of letter stock, private placements, or direct payments, leveraged transactions, and purchases of direct real estate (with the exception of REITs).

VIII. Fixed Income Guidelines

The fixed income portfolio will be measured against a benchmark of, the Barclay's US Aggregate Bond Index, over 5-7 year periods.

The Portfolio will target a duration profile within a 25% +/- band of the duration of the Barclays 3-7 Year Treasury Index.

Up to 100% of the fixed income investments will be invested in diversified mutual funds, exchange traded funds (ETFs) and/or separate account managers.

Fixed Income manager returns will be measured against peer group performance with a goal of consistently placing in the top half of that universe.

IX. Equity Guidelines

All equity investments should offer anticipated total returns (on a five to seven year horizon) in excess of the bond portfolio.

The equity portfolio should seek to avoid volatility through diversification and by limiting investments in managers with unusually high volatility measured by beta.

Up to 100% of the equity investments will be invested in diversified mutual funds, exchange traded funds (ETFs) and/or separate account managers.

The equity portfolio will be measured against a benchmark of, the S&P 500 (Total Return) Index over 5-7 year periods.

Equity manager returns will be measured against peer group performance with a goal of consistently placing in the top half of that universe.

X. Investment Selection

The Investment Manager implements this strategy using a mix of passively managed (indexed) mutual funds as well as active management. The Investment Manager believes that passively managed funds are generally cost effective and offer an attractive risk/return tradeoff for several asset classes. However, the Investment Manager also believes that it is possible to identify managers who consistently outperform, at a reasonable cost. The Investment Manager uses active management in the asset classes where there are typically largest deviations among under- and over-performers.

For passive (index) funds, selection criteria will include 1) Past performance (in particular, how closely the fund has tracked its underlying index); 2) Costs and fees relative to competing index funds in the same asset class, and; 3) Reputation and stability of the investment company/manager.

For actively managed funds (to be used when there is the opportunity to generate excess returns on a risk-adjusted basis), the following criteria will be evaluated: 1) Past performance (risk-adjusted). Performance rankings and consistency of performance; 2) A concise and credible strategy on the part of the manager for generating excess risk-adjusted returns; 3) Costs and fees versus other similar funds; obviously, fees cannot exceed the net expected (risk-adjusted) excess return; 4) Length of time the fund has been in existence and under the direction of the current manager(s); 5) Historical volatility of each fund; 6) How the fund complements other assets in the portfolio.

XI. Investment Monitoring and Control

The Investment Manager will provide the Finance Committee with quarterly reports that summarize asset values, inclusive of additions/withdrawals. Quarterly summary statements will be provided one week before the meeting and include:

- Portfolio performance during the quarter for each investment/fund; also shown will be year-to-date performance
- Performance results of comparative benchmarks for the same periods
- End of quarter status regarding asset allocation – current versus policy

The purpose of reports will be to provide the Committee with basic information to allow qualitative discussion of portfolio performance at its quarterly meetings.

The Investment Manager will also furnish the committee, on a quarterly basis, with a sampling of custom blended benchmark returns that are suitable for the Society's portfolio. These benchmarks will encapsulate the most appropriate exposures, inclusive of but not limited to, the Barclays Aggregate index, the S&P 500, the MSCI EAFE. Weightings will be a function of the Society's portfolio each quarter.

Returns on all investments should be measured over the most recent quarter, year-to-date and rolling 3 and 5 year periods.

The Investment Manager is committed to transparency and full disclosure regarding its investment activities. Quarterly performance summaries will be distributed to the Board. The ethical conduct of LHS shall be governed by the rules of the Securities Exchange Commission, the Association for Investment Management and Research (AIMR) and the general policies of the Board of LHS.

Appendix A

Definition of Terms

Terms as used in this policy are defined as follows:

Cash: Cash should be held as a liquidity reserve to take advantage of market opportunities and to respond to operational requirements.

Fixed Income: The majority of all fixed income securities should carry an "Investment Grade" rating or better. Below "Investment Grade" securities are permissible in the portfolio to a moderate degree. Duration is a measure of interest rate sensitivity of fixed income portfolios. The Investment Manager should be cognizant of the duration profiles of inclusive managers and seek to reduce interest rate sensitivity when possible. Bonds will be held to provide stability of current return, and to dampen volatility in portfolio valuations.

Equities: Equity managers can select from high quality Large, Mid and Small-Cap issuers with high liquidity. It is anticipated that there will be significant exposure across the economy to various industries and to various companies within those industries. Equities represent the portfolio's opportunity to grow in value through increases in market valuation and growth in current income through dividend increases.

Rebalancing: Rebalancing of the portfolio to keep within guideline limitations should be considered on a quarterly basis.

Authorized Signatures

Finance Committee of Litchfield Historical Society

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Michael J. Reardon

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Mark E. Macomber

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John Copeland

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Jeff Wacker

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Cathy Fields

Investment Manager "Clarfeld"

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