



INDIANA UNIVERSITY FOUNDATION

Investment Policy

INTRODUCTION

As stated in the Foundation's corporate charter, the purpose of the Foundation is to raise, receive, hold, administer, invest and manage funds from donors wishing to benefit Indiana University. Funds donated to the Foundation for the benefit of the University may be maintained in the form of endowments, quasi-endowments, charitable trusts or other forms deemed appropriate. The purpose of this document is to establish policy and guidelines which will provide for the maintenance and enhancement of Foundation assets. This document will be reviewed at least annually by the Investment Committee of the Foundation's Board of Directors and updated or modified as needed to reflect changes in both the financial markets and needs of the Foundation in support of the University.

INVESTMENT PHILOSOPHY

The Foundation's assets exist to provide long term support to Indiana University. Accordingly, the investment philosophy of the Foundation is based on a disciplined, consistent, and diversified approach utilizing multiple asset classes and multiple managers. Our intent is to accommodate styles and strategies considered reasonable and prudent.

The Foundation spending policy will necessitate distributing a significant portion of the investment return each year and may occasionally require distributing capital from prior gains. However, over the long term, the investment return is expected to be greater than the amount distributed and this excess return will be reinvested. The reinvested portion should be sufficient to cover expected future inflation and investment management and related fees so that the real value of the Foundation's assets is preserved and maintained over time.

Assets may be invested in pooled funds or in direct investments, or a combination of the two. Assets will typically be diversified among high quality stocks and bonds. Additional asset classes may be included when it is reasonable to expect the additional asset class will either increase return or reduce risk, or both.

Assets may be managed either by Foundation staff and/or by external investment managers. External investment managers shall be selected from established and financially sound organizations which have a proven and demonstrated track record managing similar funds. However, in certain alternative asset classes, consideration will be given to less seasoned firms with emphasis placed on the track records of individuals within the firm, in which case there will be a minimum expectation that the principals have demonstrable experience in a similar capacity at established firms. Selection of investment managers shall depend upon factors established by the Investment Committee of the Board of Directors of the Foundation and will be consistent with the laws of the State of Indiana. Such factors include, but are not limited to the manager's investment philosophy, experience and depth of personnel, investment process, past performance, and fee structure.

The Foundation recognizes its responsibility as a stockholder to encourage corporate citizenship, as well as corporate growth, in the companies whose shares are owned by the Foundation. Corporate citizenship and social responsibility will be encouraged through the voting of proxies or other actions based upon information available to the Investment Committee, Foundation



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investment staff, and the external investment managers. Although the Foundation reserves the right to vote proxies for all individually managed portfolios (not mutual or commingled funds), it may delegate this responsibility to the external investment managers. In these cases, the external investment managers shall provide, on a quarterly basis, an accounting of all non-routine¹ proxy votes with explanations. Both the external investment managers and Foundation investment staff have the duty to vote proxies in a manner that is consistent with the investment objectives contained herein. We recognize the Investment Committee could, from time to time, adopt socially responsible policies that may reduce the total return. We also recognize that certain proposals, if implemented, could have a substantial impact on the market prices of the securities held in the portfolio. Therefore, in the absence of specific socially responsible restrictions, proxies shall be voted on in a manner which maximizes the value of the portfolio's securities. Although each proxy vote must be examined on a case-by-case basis, we would generally expect to vote against proposals such as the approval of poison pills, golden parachutes, unequal voting rights plans, staggered boards, and the elimination of shareholder rights, which are designed to make it difficult for a company to be acquired or which have a tendency to entrench current management at the expense of shareholders.

ROLE OF INVESTMENT COMMITTEE

The objective of the Investment Committee of the Foundation Board of Directors is to provide direction for the investment of the financial assets of the Foundation. The Investment Committee is charged with the following responsibilities:

1. To establish policy and guidelines for the receipt, investment, and spending policy/distribution of Foundation assets.
 2. To determine the appropriate asset allocation among these assets.
 3. To provide a system for monitoring the returns on these assets, and to review the performance of these assets.
 4. To hire and dismiss investment managers as needed.
 5. To report to the Foundation Board of Directors.
 6. To monitor the investment goals of the Foundation's Strategic Plan.
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OBJECTIVES

The primary objective of the Foundation's asset management program is to preserve its real (inflation adjusted) purchasing power while providing a relatively predictable, stable, and constant (in real terms) stream of earnings consistent with prudent risk limits and the Foundation's spending needs. We feel the attainment of this broad objective will provide a balance between the current spending needs of the Foundation and the need to preserve the purchasing power of the endowment for future generations.

To meet this broad objective, the specific performance objective is to attain, within acceptable risk levels, an average annual total return that meets or exceeds the sum of the Foundation's spending (distribution) rate, inflation, investment management and related fees. Our focus will be on total return without regard to whether that return is in the form of income or capital gains. In cases where the Foundation is appointed Trustee of a charitable trust, the investment objective is to

¹ Routine proxy votes include matters such as the approval of outside accountants and re-election of directors.



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achieve a return that satisfies the distribution rate while retaining as much of the corpus as possible.

Spending Policy: Permanent endowments will not have their corpus eroded by virtue of the spending policy. The Foundation will distribute 5% of the 12-quarter rolling average of the market value of the Pooled Long-Term Fund. The Foundation will distribute net income from the Pooled Intermediate Term Fund. The Foundation will distribute the contractual rate specified within the annuity or charitable trust agreements.

STRATEGY

Investment Vehicles: Endowment assets will be invested in the Foundation's Pooled Long-Term Fund. Operating funds will typically be invested in the Pooled Short-Term Fund. An additional option is the Pooled Intermediate Fund, which will fill a need for those operating funds which are due to be spent 6 months to two years from the time the cash is received. Charitable trusts may be funded with cash, securities, real estate, or other property and will be reinvested in the Equity Trust Investment Pool, Bond Trust Investment Pool, individual securities, or any combination of the three, as soon as practical. Each Fund will be broadly diversified through investment in multiple markets and use of multiple investment styles. The purpose of diversifying among multiple markets and multiple investment styles is to enhance real returns while reducing volatility. In addition, diversification will provide assurance that no single security or class of security will have a disproportionate impact on the fund's aggregate results. IUF may charge a reasonable administrative management fee to the Pooled Funds and the Charitable Remainder Trusts.

Specific investment decisions will be the responsibility of the internal and external investment managers selected by the Investment Committee to manage the assets. The Investment Committee will from time-to-time develop specific performance objectives and investment guidelines for each manager employed, and shall periodically review each manager.

Asset Allocation: Endowment assets will be invested according to the following asset allocation guideline:

	<u>Target</u>		<u>Target</u>
Large Cap Equities	15.0%	International Developed Equities	10.0%
Mid Cap Equities	8.0%	Emerging Markets Equities	5.0%
Small Cap Equities	8.0%	International Small Cap	5.0%
Buyout/Special Situation	7.0%	Absolute Return Hedge Funds	8.0%
Venture Capital	5.0%	Directional Hedge Funds	7.0%
Timber	3.0%	U.S. Bonds	5.0%
Real Estate	6.0%	High Yield	3.0%
Direct Energy	3.0%	Bank Loans	2.0%

The appropriate asset allocation for each charitable trust depends upon the expected life of the trust, the contractual distribution rate and the circumstances of the beneficiaries. The asset allocation of each trust is reviewed annually by the Trust and Endowment Review Committee. The Trust and Endowment Review Committee will report its activities to the Investment Committee at least annually.



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GUIDELINES

Pooled Short-Term Fund

A short-term investment portfolio will be maintained to meet, on demand, the operating requirements of the Foundation and the accounts that the Foundation holds. As of January 1, 1998, all accounts with cash balances not invested in the Pooled Funds will be invested in the Pooled Short Term Fund. Cash Balances will include operating funds and also endowment assets awaiting the once monthly trade date for investment into the Pooled Long Term Fund. The primary objective of the short-term fund is to earn a rate of return comparable to interest-bearing checking accounts offered by banks while emphasizing preservation of capital.

1. Security Types:

- U.S. Treasuries and Agencies
- Commercial Paper
- Certificates of Deposit and
- Bankers Acceptances of U.S. Banks Repurchase Agreements
- Money Market Mutual Funds

2. Maturity: All securities will typically mature within one year.

3. Quality: Commercial paper must be rated A1/P1. Banks and brokerage firms must receive the specific approval of the Investment Committee. Money market funds may not invest in securities prohibited by these guidelines.

4. Diversification: Commercial Paper, CDs, BAs and Repos limited to \$10 million per issuer. Money market funds limited to \$20 million per fund. Money market funds must manage more than \$500 million in assets.

Pooled Long-Term Fund

Not only will the Long-Term Investment Fund be diversified by major asset class (e.g., stocks and bonds), but within the broad categories as well. The Investment Committee of the Foundation continually reviews the financial markets and directs the allocation among stocks, bonds, and other assets in the fund. This allocation is achieved through manager selection with the individual managers investing in the following security types:

Equity/Equity Trust Investment Pool

1. Security Types: Equity investment shall consist of:

- Publicly Traded Domestic Common and Preferred Stocks
- Convertible Stocks or Bonds
- Stock and Index Options
- Exchange Traded Funds
- Index Futures
- International Stocks
- Securities with warrants attached
- Stock Mutual Funds
- Real Estate
- Venture Capital and Private Equity
- Warrants
- Limited Liability Companies and Partnerships
- Direct Energy
- Similar type instruments

2. Diversification (Per Manager):



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No more than 10% of the portfolio cost may be invested in the equity securities of any one issuer.

No purchase shall cause ownership of 5% or more of any one issue.

No more than 25% of the portfolio market value may be invested in any one industry. (This guideline will apply to each portfolio individually.)

No more than 5% of the market value of the portfolio may be invested in any single partnership.

3. The investment manager(s), subject to the guidelines set forth in this policy statement and such other guidelines as the Investment Committee may adopt from time to time, shall have complete discretion to manage the assets in each portfolio to best achieve the investment objectives. Other guidelines adopted by the Investment Committee, such as dealing with social responsibility issues, will be furnished to the managers as appropriate.

Fixed Income/Bond Trust Investment Pool

1. Security Types: Fixed income investments shall consist of the following:
 - U.S. Treasuries and Agencies
 - U.S. and Yankee Corporate Securities
 - Private Placement Securities
 - Preferred Stocks
 - Mortgage Pass-through Securities
 - Collateralized Mortgage Obligations
 - Eurodollar Securities
 - Convertible Securities
 - International Non-dollar Bonds
 - Asset Backed Securities
 - Pooled Bond Funds
 - Certificates of Deposit and Bankers' Acceptances of U.S. Banks
 - Repurchase Agreements and Reverse Repurchase Agreements
 - U.S. Money Market Funds and Bank Short Term Investment Funds
 - U.S. and Foreign Interest Rate Futures and Options (hedging purposes only)
 - U.S. and Foreign Currency Futures and Options (hedging purposes only)
 - Options on Futures (fully covered writing only)
 - Event-linked Bonds
 - Rule 144a Securities
 - Bank Loans
 - Similar type instruments
2. Durations: Benchmark Index +/- 1.5 Years
3. Quality: The average quality of the portfolio will be maintained at "A" or better, except for high-yield (see below). The minimum quality at time of purchase will be Baa/BBB or equivalent by at least one of the major rating services. High-Yield: The weighted average credit quality of the portfolio should be BBB- or better at all times. All securities must be rated at time of purchase at least B- by Standard & Poor's or B3 by Moody's.
4. Diversification: Excluding U.S. Treasuries and Agencies, no more than 5% of the portfolio market value may be invested in any one issue or issuer. No more than 25% of the portfolio market value may be invested in any one industry. (If more than one manager is hired, this guideline will apply to each portfolio individually).
5. Derivatives: Derivative securities shall not be used to increase the actual or potential risk posture of the portfolio. Investment managers using derivative securities may not effect a



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leveraged portfolio structure, i.e., options and futures positions must be offset in their entirety by corresponding cash and securities.

Abusive Tax Shelters and Listed Transactions

The Internal Revenue Service has identified specific listed transactions considered to be abusive as detailed in **§ 1.6011-4 Requirement of statement disclosing participation in certain transactions by taxpayers**. A listed transaction is a transaction that is the same as or substantially similar to one of the types of transactions that the IRS has determined to be a tax avoidance transaction and identified by notice, regulation, or other form of published guidance as a listed transaction.

The Indiana University Foundation will comply with the form, substance, spirit, and letter of such laws and regulations. As agents of the Foundation contracted to perform specific investment management activities, each investment manager is prohibited from marketing to, or otherwise engaging the Foundation in these listed transactions. Should any of the investment vehicles currently held for the benefit of the Foundation be classified by the IRS as an abusive tax shelter subsequent to the original engagement, each manager is required to notify their Foundation contact immediately and make every effort to divest of this transaction. Such notification should include a detailed listing of any investment transactions or activities performed on the Indiana University Foundation's behalf and the plan to divest these investments.

PERFORMANCE MEASUREMENT

The Investment Committee will establish specific performance objectives and provide for monitoring the investment performance of the managers employed to manage Foundation assets. On a quarterly basis, the Committee will evaluate each manager's investment performance relative to the performance objective, risk guidelines, the manager's stated investment philosophy, and the manager's peer group. For purposes of reviewing performance, it is intended that the following objectives be achieved over a rolling 5-year moving period, net of investment management fees.

Pooled Long Term Fund

1. The total return is expected to exceed that of the Total Target Weighted Index (TTWI) which will be comprised of the appropriately weighted benchmarks in relation to the allocations within the portfolio. Upon completion of achieving the asset allocation targets, the TTWI will be comprised of 15% of the S&P 500 Index (Large-Cap domestic equity), 8% of the Russell Mid-Cap Index (Mid-Cap domestic equity), 8% of the Russell 2000 Stock Index (Small-Cap domestic equity), 10% of the MSCI Europe, Australia, & Far East Index ("EAFE" International core equity), 5% MSCI Emerging Markets Free Index, 5% EAFE Small-Cap Value Index, 10% Lehman Aggregate Bond Index, and 39% of the appropriate blend of alternative investment benchmarks.

In the interim the weightings of the TTWI will be tailored to closely match the actual investment exposure in order to give a realistic depiction of the PLTF and its overall relative performance.

2. The total return for each "active" investment manager is expected to exceed the relevant benchmark. The total return for an index fund is expected to match, but not fall below, the relevant equity benchmark. (Exhibit 1).



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3. Each active investment manager is expected to rank in the top 40% of a universe of advisors utilizing a similar investment style (e.g. Large-Cap Value, Small-Cap Growth, International, Core Fixed Income, etc.) over a rolling five-year period.
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POLICY RELATING TO GIFTS OF SECURITIES

Securities donated to the Indiana University Foundation are processed through the Investment Department and shall be subject to applicable Federal and State tax regulations and according to the guidelines of the Gift Acceptance Policy contained in the IUF Policies and Procedures.



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Exhibit 1

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INDIVIDUAL MANAGER BENCHMARKS

Domestic Equity:

Barclays Equity Index
Commonfund Equity Index
Barclays Alpha Tilts
PIMCO StocksPlus

William Blair
Cramer, Rosenthal, McGlynn

Wells Capital
Snyder Capital

Index

S&P 500
S&P 500
S&P 500
S&P 500

Russell Mid-cap Growth
Russell 2500

Russell 2000
Russell 2000

International Equity:

Artisan Partners
Templeton
Bernstein Emerging Markets
Dimensional Fund Advisors

MSCI EAFE
MSCI EAFE
MSCI EM Free
MSCI EAFE Small Cap Value

Fixed Income:

Loomis Sayles
PIMCO

LB Ag (75%) + ML HY (25%)
LB Aggregate



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Alternative Investment Policy

Diversification Process

The Indiana University Foundation is committed to creating a broadly diversified portfolio of investment strategies. The Alternative Investment Program is consistent with the Indiana University Foundation Investment Policy and will consist of private equity in the form of venture capital and buyout/special situation funds, absolute return strategies, real estate investments and inflation hedge strategies such as timber and oil and gas partnerships.

Goals, Objectives & Performance Measurement

The Indiana University Foundation expects the Alternative Investment Program investment to improve the risk-adjusted returns of the overall portfolio and to smooth long-term portfolio volatility.

Strategic Targets and Tactical Asset Allocation Ranges

The IU Foundation's current target for the Alternative Investment Program is 39% of total market value of the Pooled Long Term Fund. The following are the Foundation's strategic targets and tactical asset allocation ranges for each of the sub classes within the Alternative Investment Program.

	<u>Strategic Target</u>	<u>Tactical Asset Allocation Ranges</u>
Private Equity		
Venture Capital	5%	3-7%
Buyout Funds/ Special Situations	7%	5-9%
Absolute Return Strategies	15%	13-17%
Real Estate	6%	4-8%
Natural Resources/Commodities	6%	4-8%

Committed versus Invested Capital

Capital commitments to fund-of-funds and direct limited partnerships are drawn down (invested) over a period of time, usually four to six years, and capital distributions from the partnerships back to the investors usually begin in year four to five of an investment. Thus, at any given time, the Foundation will only be fractionally invested on the committed funds. In order for the Foundation to reach the allocation target, it must commit more capital than will actually be invested.



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PRIVATE EQUITY ALLOCATION POLICY

Goals, Objectives & Performance Measurement

The primary objective of the private equity allocation of the Foundation is to achieve superior rates of return in excess of what the Foundation could achieve in the public securities marketplace. The higher expected rates of return are needed to compensate the Foundation for the illiquidity and higher risk inherent in the venture capital and leveraged buyout markets.

The Foundation seeks to achieve annualized outperformance of 500-700 basis points over the broad public markets over a full market cycle.

Strategic Targets & Tactical Asset Allocations Ranges

Venture Capital: IUF will seek to identify and pursue top venture managers and commit roughly 10% of the Pooled Long Term Fund value with the goal of having 50% of committed funds invested. Therefore the allocation will equate to approximately 5% of the total Foundation "at cost" (or original investment value). Return of capital and proceeds from gains will be invested in new offerings as they arise with the current stable of private equity managers, or with another targeted alternative investment manager, or with a traditional asset manager until a suitable alternative is identified.

Buyout: The "commitment to invested" ratio for the buyout portion of the private equity allocation has historically been 1.5-1.75:1 rather than the 2:1 ratio needed in the venture capital segment. As such, IUF will over commit to buyouts/special situations in order to achieve a 7% investment level. This ratio will be analyzed and appropriately adapted as the portfolio continues to mature.

The Investment Committee of the Foundation recognizes the importance of venture capital and private equity investments to the general economy of Indiana through the benefits of employment opportunities, educated work force retention and economic diversification among others. When considering investment alternatives, the committee shall include Indiana-based funds or funds that target Indiana University research among those firms with equal opportunity, similar goals, objectives and risk.

ABSOLUTE RETURN STRATEGY ALLOCATION

Goals & Objectives

The primary objective of the absolute return allocation shall be to provide the Foundation with superior risk adjusted returns with a low correlation to domestic equities and fixed income securities.

Performance Benchmarks

With the absolute return allocation, the Foundation seeks to achieve a rate of return that is equal to or better than the one year U.S. Treasury Bill rate of return plus 500 basis points, net of all fees over a three to five year period of time.

In addition to achieving the performance objective above, the Foundation expects the absolute return investment managers or manager of managers to be in the top quartile of their respective peer group over a three to five year period of time. The Foundation expects the standard deviation (or volatility) of the total absolute return allocation to be less than 8% on a rolling annualized basis.



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Investment Strategies

In striving to achieve these performance objectives, the Foundation will seek investment strategies primarily focused on the following three categories: event-driven, relative-value and hedged directional strategies, among others.

- Event driven strategies shall consist of risk (merger) arbitrage and distressed securities.
- Relative value strategies shall consist of convertible arbitrage, fixed income arbitrage and equity market neutral.
- Hedged directional strategies shall consist of managers who specialize in long/short equity management with low net exposure to the public equity market (as defined as the S&P 500). These managers may have a domestic, global or industry-specific focus.

In addition, the Foundation may also utilize multi-strategy arbitrage managers, activist hedge funds, and managed futures.

NATURAL RESOURCES

Goals, Objectives & Performance Measurement

The primary goal of the natural resource allocation of the Alternative Investment Program is to provide an attractive rate of total return (income and capital appreciation) and to offer protection against inflation. This allocation will have a low to negative correlation with most other equity asset classes in the total Foundation portfolio. Consequently when the equity markets are rising, this allocation may decrease in value. This should be perceived as the cost of the hedge, much like insurance, rather than a negative on the asset class.

Strategic Targets & Tactical Asset Allocations Ranges

The Foundation, over time, will commit 6% of the Pooled Long Term Fund to inflation hedge strategies. The Foundation will be looking at primarily timber investments, direct energy partnerships, and commodities.

REAL ESTATE INVESTMENTS

Goals, Objectives & Performance Measurement

The goals of the real estate allocation of the Alternative Investment Program are to provide a 7-9% real total return (net of fees) and protect the portfolio against inflation. This allocation will have a low to negative correlation with all other equity asset classes in the total Foundation portfolio.

As a proxy for this allocation, the Foundation will utilize the NCREIF Real Estate Index as a benchmark.

Strategic Targets & Tactical Asset Allocations Ranges

The Foundation, over time, will commit 6% of the Pooled Long Term Fund to real estate investments. The allocation will consist of global exposure to publicly traded REITS, core properties, value added properties, opportunistic investments, and commercial mortgages.