



The
United
Methodist
Church

Baltimore-Washington Annual Conference

March 2016

Board of Investments of the Council on Finance and Administration

Purpose

The Investment Working Group was formed by a recommendation of the 2014/2015 Divestment Working Group (chaired by Jackson Day) as published in the 2015 Baltimore Washington Annual Conference. That group's finding included the observation that both WesPath and MidAtlantic Funds, our primary investment managers, use Socially Responsible Investment screens (SRI) that screens out about 400 companies based on religious and moral guidance (e.g., alcohol, "adult entertainment", tobacco, weapons, gambling and operating private prisons).

These guidelines are meant for all Baltimore-Washington Annual Conference investment committees, agencies, and local churches.

Recommendations

The Investment Working Group to be made into a standing Committee called the *Board of Investments of the Council on Finance and Administration* that has the following list of responsibilities:

1. Disseminate information on Socially Responsible Investing (SRI) to Baltimore Washington Conference Committees, Boards, and local churches.
2. Be the focal point and advisor for investment guidelines and alternatives for the Conference Board of Trustees, Conference Board of Pension and Benefits, and Conference Finance and Administration.
3. Review investment performance of funds managed by the Baltimore Washington Conference at least semi-annually.
4. To form a standing committee consisting in membership drawn from:
 - Baltimore-Washington Conference Board of Pensions and Benefits
 - Baltimore-Washington Conference Board of Trustees
 - Baltimore-Washington Council on Finance & Administration
 - Baltimore-Washington Conference Board of Church & Society
 - Baltimore-Washington Conference financial staff
5. This committee shall NOT make any investment decisions; those will be made independently by its constituent investment committees.



Submitted

- CFA Representatives (**Daryl Williams - Chairman**, Rick Miller)
- Trustee Representatives (Vince Leggett)
- CBOP Representatives (Wayne Dehart, Carey James, **Curtis Ehrgott - Secretary**)
- Board of Church & Society (T.C. Morrow)
- Staff – Pier McPayten (Conference Controller), Francess Tagoe (HR & Benefits manager), Paul Eichelberger (Conference Treasurer)

Investment Policy Statement

THEOLOGICAL STATEMENT

All that is, was, and will be belongs to God. God has entrusted us to be good stewards of the resources God has entrusted to us. We further need to be mindful that all our financial resources start from a single person giving of his or her substance into the offering plate in our local churches. To be good stewards of what is entrusted to us we must be wise as serpents and harmless as doves (Matthew 10:16b) in our investment practices. We must emulate the servants in the parable of the talents (Matthew 25:18-29) while remembering always to work to do no harm in the work that we do. Likewise, we must remember, 2 Corinthians 9:6 which says: “The point is this: whoever sows sparingly will also reap sparingly, and whoever sows bountifully will also reap bountifully.” In short, we must work to get the greatest benefit from the dollars entrusted to us while making certain that we do not harm people or the environment all the while holding true to our core values and principles.

While lust of money may be the root of all evil (1 Timothy 6:10), the proper use of money is as John Wesley expressed in his sermon 50 On the Use of Money “...it is an excellent gift of God, answering the noblest ends. In the hands of his children, it is food for the hungry, drink for the thirsty, raiment for the naked: It gives to the traveler and the stranger where to lay his head. By it we may supply the place of a husband to the widow, and of a father to the fatherless. We maybe a defense for the oppressed, a means of health to the sick, of ease to them that are in pain; it may be as eyes to the blind, as feet to the lame; yea, a lifter up from the gates of death!”

In short “Gain all you can, save all you can, and give all you can” (John Wesley)

SOCIAL RESPONSIBILITY STATEMENT

In Matthew 7:12 we are commanded to treat others as we would want them to treat us. In Wesley’s Sermon 50 On the Use of Money he told us to refrain from the buying and selling of spirituous liquors, jobs that exposed us to lead or mercury, and even jobs that required “long hours of sitting.” This is the basis for our policies on Socially Responsible Investment. We want



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our investments to be in socially aware companies that provide healthy and quality products while also treating their employees with dignity, respect and a livable wage. As well, we want to influence all companies through our investments to work towards becoming places where these values are championed and upheld.

The General Conference has a policy for investment (§717 of the 2012 Book of Discipline):

“It shall be the policy of The United Methodist Church that all general boards and agencies, including the General Board of Pension and Health Benefits, and all administrative agencies and institutions, including hospitals, homes, educational institutions, annual conferences, foundations, and local churches, shall, in the investment of money, make a conscious effort to invest in institutions, companies, corporations, or funds whose practices are consistent with the goals outlined in the Social Principles; and shall endeavor to avoid investments that appear likely, directly or indirectly, to support racial discrimination, violation of human rights, sweatshop or forced labor, gambling, or the production of nuclear armaments, alcoholic beverages or tobacco, or companies dealing in pornography. The boards and agencies are to give careful consideration to shareholder advocacy, including advocacy of corporate divestment.” (From The Book of Discipline of The United Methodist Church - 2012. Copyright 2012 by The United Methodist Publishing House. Used by permission.)

Investments shall be guided by the following ethical norms according to the Social Principles of The United Methodist Church.

1. An ecologically just world and a better quality of life for all creation;
2. Social justice and the sacred worth of all persons;
3. Sound fiscal policies that protect the economic life of all individuals;
4. Political and governmental responsibility for protection of basic rights;
5. The unity of the world community.

STANDARD OF CARE

To use the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.

The Uniform Prudent Investor Act (UPIA) was approved for use in all states at the 1994 annual Conference of Commissioners on Uniform State Law and by the American Bar Association in 1995. The act provides excellent guidance. Key provisions of the UPIA include:

1. No investment is inherently prudent or imprudent, except in how its inclusion or exclusion impacts the portfolio as a whole;



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2. Trustees/Committees are expected to use all reasonably available strategies to improve the risk/reward relationship of the portfolio;
3. Under most circumstances, the assets of the trust/portfolio must be diversified;
4. Trustees/Committees are obliged to spread portfolio investments across asset classes to enhance performance and reduce risk;
5. The possible effect of inflation must be considered as part of the investment strategy. As a result, use of equities is encouraged to allow the possibility that the portfolio's growth will outpace inflation;
6. Fiduciaries have a duty to either demonstrate investment skill in managing trust assets or to delegate investment management to another more qualified party.

FIDUCIARY RESPONSIBILITY

It is important that we remember that the funds we see are not personal but institutional funds. We are trusted as fiduciaries to ensure the perpetual health of the assets under our management. Our fiduciary responsibility supersedes any personal bias and must be maintained as the highest guiding principle at all times. Fiduciary responsibility comes with several duties as listed below:

Duty of Care as described in Uniform Prudent Management of Institutional Funds Act (UPMIFA) requires that a fiduciary act at all times in good faith and in a manner which is in the best interest of the beneficiaries. Fiduciaries are to be adequately informed about alternatives available at the time of decision. They are to act with the same care that responsible persons would exercise in the management of their own affairs. Where specific instructions are left with regard to legacies, they must be followed unless changed by court order.

Duty of Care includes prudence in the investment context (including diligence in attending meetings), efforts to ascertain relevant information prior to decision making, balanced judgment, adequate assessment and balancing of potential investment risks and returns and adequate diversification of investments.

Duty to Minimize costs is described in UPMIFA section 3(c)(1). "In managing and investing an institutional fund, an institution, may incur only costs that are appropriate and reasonable in relation to the assets, the purposes of the institution, and the skills available to the institution." In devising and implementing strategies for the investment and management of trust assets, trustees are obliged to minimize costs."

Duty to Investigate is described in UPMIFA section 3(c)(2) "[A]n institution shall make a reasonable effort to verify facts relevant to the management and investment of the fund." UPMIFA requires persons who make investment and management decisions to investigate the accuracy of the information used in making decisions; a fiduciary has a responsibility "to examine information likely to bear importantly on the value or the security of an investment."



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Duty of Loyalty prohibits self-dealing by persons who are fiduciaries. They are not permitted to take part in investment decisions that would create a conflict of interest. All investment decisions are to be made with a view to the interest of the beneficiaries rather than to the personal interests of the fiduciary. When conflicts do arise, they should be disclosed to the governing board immediately. Failure to do so will subject the fiduciary to potential liability for any losses suffered due to the breach of the duty of loyalty. Advance disclosure in writing will provide evidence of the disclosure in the event the issue of conflict of interest is raised. Any fiduciary with a conflict involving an investment decision should abstain from any participation in that decision and document the abstention in the minutes of the meeting.

It is important to remember that fiduciary responsibility cannot be delegated. The decision of a board to engage investment adviser(s) will not absolve the board from its ultimate responsibility for the care of the funds. In order to discharge adequately the duties of care and loyalty, the fiduciary will need to demonstrate that appropriate procedures were used for selecting the adviser(s) and for monitoring the results of the advice received. The adviser(s) should be trustworthy and competent to perform the work as outlined by the board. The loyalties of the adviser(s) must run to the beneficiaries, not to individual members of the board.

Fiduciaries are permitted to accept the advice of an adviser where they can demonstrate that their initial decision to engage the adviser was well-founded and where subsequent developments do not give rise to a basis for suspending that reliance. A fiduciary that has knowledge that reliance on an adviser or other financial agent is no longer well-founded may become personally responsible for any loss sustained by the fund as a result of the inappropriate reliance. Therefore, fiduciaries are required to make known any and all misgivings about any investment advisors formally and in a timely manner.

Fiduciaries are responsible for prudently investing funds held in trust and are encouraged to seek expert counsel, often in the form of an investment consultant and portfolio managers, to assist in this process. They need to use sound judgment when making investment decisions. They are expected to avoid reckless speculation while also obtaining an adequate return on the assets entrusted to their care. Inevitably, this means walking a line between excessive caution and excessive risk. Finding that line may not be easy.

Any conflicts of values shall be resolved with discretion, fiduciary responsibility and appropriate consultation.

PORTFOLIO MANAGEMENT

Permitted Asset Classes

All conference, agency, and local church investment committees must consider investment objectives when considering appropriate assets for investment. This Committee believes long-term investment performance, in large part, is primarily a function of asset-class mix. This Committee has reviewed the long-term performance characteristics of the broad asset classes,



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focusing on balancing risks and rewards. We advise all conference based committees to take this approach as appropriate to their particular investment objectives.

The following are asset classes in order of risk (from least to most) that are currently considered appropriate for conference investment: Cash and cash equivalents, Bonds, Stocks, Real Estate (REIT).

Within the approved asset classes, the following are permitted and restricted security types for investment:

Permitted Security Types

1. Mutual Funds – Equity, Debt, Money Market
2. Collective Trust Investments
3. Sub-Advised and Separate Account Investments
4. Individual Stocks, as long as they are traded on the New York Stock Exchange, American Stock Exchange, NASDAQ, or other major U.S. Exchange
5. Individual Bonds, as long as they are rated A or better and traded on a major U.S. Exchange and have a duration of 10 years or
6. Bank Certificates of Deposit

Limited “Restricted” Security Types – Require Case By Case Committee Pre-Approval and Evaluation

1. Private Equity
2. Individual Bonds, currently held, that are downgraded to BBB or lower – may equal a maximum 10% of position
3. Closed-End Funds
4. Unit Investment Trusts
5. Collateralized Mortgage Obligations (CMO's)
6. Real Estate Investment Trusts (REIT's)

Excluded Investment Categories

The following investment categories are not permissible:

1. Precious Metals
2. Short Sales
3. High Yield Bonds – Individually, Mutual Fund, or other
4. Purchase of Letter Stock, Private Placements, or Direct Payments
5. Leveraged Transactions
6. Commodities Transactions
7. Puts, Calls, Straddles, or other Option Strategies



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8. There shall be no investment in any limited partnership, unless the Conference is also a general partner, or unless the vote of the trustees and CFA approves unanimously of the investment. ALL INVESTMENTS OF THIS TYPE MUST BE APPROVED BY THE BALTIMORE-WASHINGTON CONFERENCE COUNCIL ON FINANCE AND ADMINISTRATION, NO EXCEPTIONS

Other Investment Considerations

No individual security, except diversified funds, shall make up more than 5% of any individual portfolio.

Additional Investment Quality Standards

Cash Equivalent Vehicles

All cash equivalent investments shall be pooled investment vehicles, such as money market funds, where the funds' share price is intended to remain constant and the fund's yield is comparable with the current risk-free rate of return. Also permitted in this category shall be United States agency-guaranteed bank certificates of deposit (purchased directly from banks or indirectly through brokerage accounts), short-term U.S. government securities, or bank savings and money market accounts.

Bonds and Other Fixed Income Funds

Bonds

Individual Bonds may be used as long as they are rated BBB or better, are traded on a major U.S. Exchange and have a duration of 10 years or less; investments in high yield bonds and certain convertible bonds should be limited to the use of mutual funds.

Bond Funds

Any selected diversified bond fund shall be pooled investment vehicles, such as a publicly traded mutual fund, providing net asset valuations published on a daily basis.

Common Stocks and Other Stock Funds

Common Stocks

The following criteria will be used for the selection and retention of common stock vehicles:

1. Investments shall not knowingly be made in any company producing, as its core business, alcoholic beverages (beer, wine or distilled liquor) or:
 - a. receiving 10% or more of gross revenues from selling, distributing or marketing alcoholic beverages; or
 - b. receiving 10% or more of gross revenues from supplying key elements for alcoholic beverage production.
2. Investments shall not knowingly be made in any company manufacturing, as its core business, cigarettes, cigars, chewing tobacco or smokeless tobacco or:



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- a. receiving 10% or more of gross revenues from selling, distributing or marketing tobacco-related products; or
 - b. receiving 10% or more of gross revenues from supplying key elements to the tobacco industry (cigarette papers, flavorings, adhesives, etc.).
3. Investments shall not knowingly be made in any company owning or managing, as its core business, casinos, racetracks or off-track betting parlors or receiving 10% or more of gross revenues from the production of goods and services related to the gaming or lottery industries.
4. Investments shall not knowingly be made in any company receiving 10% or more of gross revenues from the production, sale or distribution of products or services that are considered pornographic or meet the legal definition of “obscene” or “harmful to minors.”
5. Investments shall not knowingly be made in companies that receive 10% or more of their gross revenues in for-profit privately run prisons, correctional facilities, jails, penitentiaries, detention centers and transfer centers.
<http://www.gbophb.org/news/release/pr20120103/>
6. Investments shall not knowingly be made in any company:
 - a. receiving 10% or more of gross revenues from the manufacture, sale or distribution of antipersonnel weapons (land mines, “assault-type” automatic and semiautomatic weapons, firearms, etc.), armaments, ammunition or weapons-related systems provided for commercial and private markets (exceptions may be made for weapons and ammunition provided for sporting or law enforcement purposes); or
 - b. whose identifiable ratio of nuclear weapons contract awards from the U.S Department of Defense or comparable agency or department of any foreign government to gross revenues is greater than or equal to 3%.
7. Investments will not be made in corporations in which 10% or more of gross revenues are derived from a combination of the above (1-5).
8. Companies not falling into any of the above categories still may be ineligible for purchase because of reputation, public image or any specific business practices determined to be a gross violation of the Social Principles of the United Methodist Church (such as human rights violations; abusive labor practices, including the exploitation of child labor; flagrant or egregious damage to the environment; and unethical business practices).



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9. Emerging markets commingled equity pools are exempt from the above restrictions if specifically authorized and the aggregate exposure of companies otherwise prohibited does not exceed 10% of the total value of the fund.

Common Stock Funds

Any selected common stock funds shall be pooled investment vehicles, such as a publicly traded open or closed-end mutual fund, providing daily asset valuations. Such investments may include focus on any size domestic or non-U.S. stock.

Asset Class Index and Benchmarking

The investment alternatives are listed below, along with the appropriate Asset Class Index benchmark and Peer Group Comparative Universe to be used for each investment option currently offered in the plan:

Asset Class	Benchmark Index	Comparative Universe
Money Market & Stable Value	Citigroup 3-month T-Bill	Morningstar Ultra-Short Super Credit
Active Fixed Income	Barclay's U.S Aggregate Bond Index	Morningstar Intermediate Term Bond Universe
Balanced	Weighted Average Index	Morningstar Moderate Allocation Universe
Large Cap Value	Russell 1000 Value	Morningstar Large Value Universe
Large Cap Blend / Index	S&P 500 Index less 30 basis points	Morningstar Large Core Universe
Large Cap Growth	Russell 1000 Growth	Morningstar Large Growth Universe
Mid Cap Value	Russell 3000 Value	Morningstar Mid Value Universe
Mid Cap Blend	Russell 3000	Morningstar Mid Core Universe



Mid Cap Growth	Russell 3000 Growth	Morningstar Mid Growth Universe
Small Cap Value	Russell 2000 Value	Morningstar Small Value Universe
Small Cap Blend	Russell 2000	Morningstar Small Blend Universe
Small Cap Growth	Russell 2000 Growth	Morningstar Small Growth Universe
International	MSCI EAFE	Morningstar Foreign Large Blend Universe
International Emerging Markets	MSCI Emerging Markets	Morningstar Diversified Emerging Markets Universe

INVESTMENT MANAGER SELECTION & EVALUATION

All Baltimore-Washington Annual Conference investment committees will consider the following criteria when considering each money manager or mutual fund:

1. **Regulatory oversight:** Each investment manager should be a regulated bank, an insurance company, a mutual fund organization (Registered Investment Company), or a registered investment adviser.
2. **Correlation to style or peer group:** The investment management product (whether a fund or segregated account) should be highly correlated to the determined asset class.
3. **Performance relative to a peer group:** The product’s performance should be evaluated against the peer group’s median manager return for 1-, 3- and 5-year time weighted and/or cumulative periods.
4. **Performance relative to assumed risk:** The product’s risk-adjusted performance (Alpha and/or Sharpe Ratio) should be evaluated against the peer group’s median manager’s risk-adjusted performance.
5. **Minimum track record:** The product’s management team should be managing the specific product or style for at least 5 years. A shorter time period may be used for styles that are oversubscribed, available capacity is limited and when the “Investment Manager” deems it prudent to utilize a specific investment based on detailed criteria that meets the guidelines of this policy.



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6. **Assets under management:** The product or manager should have at least \$200 million under management.
7. **Holdings consistent with style:** The screened product should have no more than 20% of the portfolio invested in “unrelated” asset-class securities. For example, a Large-Cap Growth product should not hold more than 15% in cash, fixed-income and/or international securities.
8. **Expense ratios / fees:** The product’s fees should not be in the bottom quartile (most expensive) of their peer group.
9. **Stability of the organization:** There should be no perceived organizational problems; the same portfolio management team should have been in place for at least 5 years.

All committees acknowledge fluctuating rates of return characterize the securities markets, particularly during short-term time periods. Recognizing that short-term fluctuations may cause variations in performance, the committees intend to evaluate manager performance from a long-term perspective.

All committees remain aware that ongoing review and analysis of the investment managers is just as important as the due diligence implemented during the manager selection process. The performance of the investment manager will be monitored on an ongoing basis and it is at the committee’s discretion to take corrective action by replacing a manager if they deem it appropriate at any time.

On a timely basis, but not less than quarterly, the investment committees will meet to review whether each manager continues to conform to the search criteria outlined in the previous section, specifically:

1. The manager’s adherence to the Portfolio’s investment guidelines;
2. Material changes in the manager’s organization, investment philosophy and/or personnel;
3. Any legal, SEC, and/or other regulatory agency proceedings affecting the manager.

All committees in the best interest of their Portfolios shall set performance objectives for each investment manager. Each manager will be measured against the following four key criteria:

- a. 3-year index measurement
- b. 5-year index measurement
- c. 3- year comparative universe measurement
- d. 5-year comparative universe measurement

To satisfy Investment Policy criteria, an investment fund need only to meet one of the above listed criteria. Although satisfying only one (and even two) of the above criteria meets



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Investment Policy guidelines, such a result would warrant watch list consideration and further review by the Committee. Meeting three of four of the above stated criteria would meet Policy criteria by a comfortable margin.

Watch List Considerations

1. An investment option performs below median for their peer group over a 1-, 3- and/or 5-year cumulative period
2. A manager's 3-year risk adjusted return (Alpha and/or Sharpe) falls below the peer group's median risk adjusted return
3. There is a change in the professionals managing the portfolio;
4. There is a significant decrease in the product's assets;
5. There is an indication the manager is deviating from his/her stated style and/or strategy (style drift);
6. There is a material increase in the product's fees and expenses;
7. Any extraordinary event occurs that may interfere with the manager's ability to fulfill his/her role in the future.

The decision to retain or terminate a manager cannot be made by a formula. It is the Committee's confidence in the manager's ability to perform in the future that ultimately determines the retention of the manager. **Always remember, personal comfort with a manager does not exempt committees from their fiduciary responsibility for fund performance and manager oversight.**

Managers/Funds may be selected which do not meet performance benchmarks, but fit or maintain a particular investment philosophy.

Investment Manager De-Selection

At its discretion, the Committee may decide to de-select a fund/manager by identifying a replacement fund/manager in the same asset class and style. If circumstances exist where the Committee cannot find a replacement fund/manager within a reasonable time period following a decision to de-select a fund/manager, the Committee may decide to freeze the fund/manager to further investments until such time a replacement can be found.

The decision to retain or terminate a fund/manager cannot be made by a formula. It is the Committee's confidence in the fund/manager's ability to perform in the future that ultimately determines the retention of the manager. When considering terminating a fund/manager when possible the committee should begin their search for new funds/managers at least one quarter in advance of manager termination. **Always remember, personal comfort with a manager does not exempt committees from their fiduciary responsibility for fund performance and manager oversight.**



Controlling and Accounting for Investment Expenses

All committees must take into account investment expenses as a crucial part of their investment evaluations. High performance by a manager may be offset by exorbitant fees, depressing overall return on investment. When evaluating management cost committees should take the following into consideration:

Investment management costs and expenses fall into four categories:

1. Money-manager fees and/or the annual expenses of mutual funds;
2. Trading costs, including commission charges and execution expenses;
3. Custodial charges, including custodial fees, transaction charges, and cash management;
4. Consulting and administrative costs and fees.

At least annually, the committees will review all costs associated with the management of the Portfolio's investment program, including:

1. Expense ratios of each investment options against the appropriate peer group;
2. Custody fees: The holding of assets, collection of income, and disbursement of payments;
3. Whether the manager is demonstrating attention to "best execution" in trading securities;
4. Administrative fees: Costs to administer the Portfolio, including recordkeeping, account settlement (participant balance with that of fund), allocation of assets and earnings, and (when applicable) the proper use of 12b-1 and Sub-TA fees to offset these fees.

Investment Policy Review and Amendment

These guidelines shall guide committees in their overall investment management. Every committee should also have an individual Investment Policy Statement (IPS). Every committee will review this it's IPS annually to insure that it is in compliance with the guidelines setforth within this document. Furthermore, every IPS shall be reviewed at least annually to determine whether stated investment objectives are still relevant to the institution and the continued feasibility of achieving the objectives through the current asset mix. It is not anticipated that the IPS will change frequently. In particular, short-term changes in the financial markets should not require adjustments to the IPS.



References

Suggested Investment Opportunities

<http://www.midatlanticfoundation.org/>

SRI Screening List used by WesPath

PDF file on SRI policy

<https://www.wespath.com/assets/1/7/4676.pdf>

Another PDF file on SRI policy

<http://www.wespath.com/assets/1/7/4789.pdf>

List of ineligible companies

<http://www.gbophb.org/sri/ethical-exclusions/>

<http://www.gbophb.org/assets/1/7/ineligible.pdf>