McKenna Foundation Investment Policy

I. Mission and Introduction

The McKenna Foundation ("Foundation") exists to advance the well-being of New Braunfels and the surrounding community. The sale of McKenna Memorial Hospital created a fund that became the Foundation's gifting source. The Board of Trustees ("Board") of the McKenna Foundation is committed to ensuring this is a perpetual fund which will benefit New Braunfels and the surrounding community now and for future generations.

II. Purpose

This Investment Policy established by the Board will:

1. Establish reasonable expectations, objectives and guidelines for the investment of Foundation assets that is clear to all involved parties.
2. Offer guidance and limitations to all Investment Consultants and Investment Managers (as defined in Part VIII of this Investment Policy) regarding the investment of Foundation assets.
3. Establish the relevant investment horizon for which Foundation assets will be managed.
4. Establish a basis for evaluating investment results.
5. Define and assign the responsibilities of all involved parties.

In general, the purpose of this policy is to outline a philosophy and set of guidelines which will guide the investment management of the assets toward the desired results. It is intended to be sufficiently specific to be meaningful, yet flexible enough to be practical.

III. Investment Objectives

The Foundation's investment objective is to generate a total investment return that protects the purchasing power of the capital component, achieves the granting objectives of the Foundation, and recovers the cost of managing and administering the funds.

The minimum return objective is 7.75% per annum. This return objective is based on an assumed minimum distribution rate of 5.0% as discussed more fully in the paragraph below; assumed long-term inflation rate of 2.0%; and assumed investment expenses of .75%. While it is understood that this rate of return will not be achieved in each and every year; the Foundation's objective is to generate this minimum return on investments over rolling 3 to 5 year periods. It is preferred that the portfolio exceed this return; however, during periods when absolute returns do not meet the Foundation's return objective, relative returns versus peer groups and indexes will be used to evaluate overall performance.

This policy assumes the Foundation will disburse, at a minimum, such amount as may be required to maintain the Foundation's tax exempt status under the Internal Revenue Code for private foundations. In general, the current requirement is 5.0% of "noncharitable use assets" which includes cash, securities, and other investments reduced by 1.5% for "cash deemed held for charitable purposes". The Foundation's long term investment strategy will be monitored in the context of meeting the Foundation's distribution policies.

The Foundation's long-term return objectives are listed as follows:

1. Preservation of capital;
2. Generation of income and growth of capital to meet distribution objectives of the Foundation;
3. Generation of growth in the capital value of the Portfolio's assets in order to preserve the value of the Portfolio in real (i.e. inflation-adjusted) terms; and
4. Generation of growth in the capital value of the Portfolio's assets in order to provide the basis for producing an increasing rate of income for distribution.

The Investment Committee of the Foundation may choose investment managers, corporate custodians and /or trustees to provide services necessary to perform the obligations necessary to achieve the stated investment objectives.

IV. Risk Tolerance

The Investment Committee recognizes that prudent investing requires taking reasonable risks in order to raise the likelihood of achieving the targeted investment returns. Research has demonstrated that portfolio risk is best minimized through diversification. In terms of relative risk, the volatility of the portfolio should be in line with general market conditions.

The Investment Committee recognizes that over the long term, the risk of owning equities and alternative investments has been, and should continue to be rewarded with a somewhat greater return than that available from fixed income investments. The role of fixed income investments is to reduce the volatility of the overall portfolio while providing a more predictable stream of income.

V. Asset Allocation Policy

The following will serve as the Foundation's policy regarding the market value allocation of its assets:

Asset Class	Target	Current Range
Equities and Alternative Investments	**70.0%**	**60-80%**
Domestic Stocks	40.0%	30-50%
International Stocks	15.0%	10-20%
Alternative Investments	15.0%	0-20%
Fixed Income	**27.5%**	**25-40%**
Cash	**2.5%**	**0-10%**
Total	**100.0%**	

The Target allocation above is simply that, a target, and may not be maintained over any specific period of time since actual asset allocations will be dictated by current and anticipated market conditions, the independent actions of the Committee, and required cash flows to and from the portfolios. The Range above anticipates this natural fluctuation and provides flexibility for the Investment Managers' portfolios to vary around the Target without the need for immediate rebalancing. At least on an annual basis, the Investment Committee and the Investment Consultant(s) will review both the specific allocation and the Targets for possible rebalancing back to the target allocation, to ensure consistency with the asset allocation guidelines established by this Investment Policy.

VI. Asset Guidelines and Diversification

The Investment Committee desires to permit Investment Managers flexibility to maximize investment opportunities. However, it is cognizant of its responsibility to practice prudent management in order to conserve and protect the assets and to prevent exposure to undue risk. Exceptions to the guidelines stated below may be made upon special written approval of the Investment Committee and shall be subject to annual review.

Holdings in equity and fixed income funds are a permissible investment. The Foundation understands that it cannot influence the investment decisions of mutual funds or commingled trusts to comply with the specific provisions of this investment policy. However, every attempt will be made to select funds whose investment style and philosophy approximate the investment policy guidelines contained herein.

1. Equity Holdings

   Equity holdings shall be restricted to issues of corporations that are actively traded on the New York and American exchanges and NASDAQ. Equity securities in any single industry shall not exceed 25% of the equity portfolio market value for each individual manager. The equity holdings in any single corporation shall not exceed 10% of the market value of the equity portfolio at any time for each individual manager.

2. Fixed Income Holdings

   Fixed income investments may include all securities issued by the U.S. Treasury or other federal agencies. In general, investments may also be made in investment grade corporate, mortgages, asset backed, foreign, and municipal fixed income securities including convertible issues. Investment grade is defined as BBB or better for Standard & Poors, and BAA or better for Moody's. Up to 25% of the fixed income portfolio may be invested in securities that fall below investment grade. The fixed income portfolio should be diversified among issuers within each sector with no one issuer comprising more than 10% of the aggregate fixed portfolio for each individual manager. This does not apply to issues of the U.S. Treasury or other federal agencies.

3. Alternative Investments

   Alternative investments including real estate, hedge funds, global allocation funds, private equity and other investments that are not included in the traditional asset classes outlined above (i.e. domestic and international stocks, fixed income, and cash) may be approved by the Investment Committee on a case-by-case basis.

   It is understood that alternative investments may employ strategies and techniques, as well as trade in securities which are contained in the prohibited investment section list below.

4. Prohibited investments include the following:

   Selling short
   Commodity and Futures Contracts
   Letter Stock or Restricted Stock
   Unregistered Securities other than securities issued by (i) the U.S.
     Treasury or other federal agencies and (ii) municipalities
   Options
   Margin Transactions (Leverage)
   Private Placements
   Derivatives

VII. Monitoring and Evaluating Investments

The overall fund performance will be reviewed on a quarterly basis, with long term emphasis placed on results achieved over a three to five year period. Objectives will be reviewed annually and adjusted, if necessary, after consultation with the Investment Committee, Investment Consultant(s) and Investment Managers. Overall fund performance will be compared to the performance of a similarly structured balanced index in line with the target allocation of each strategy. This custom index will be agreed upon by the Committee and the Investment Consultant(s).

VIII. Oversight and Management Responsibilities

In seeking to attain the Foundation's investment objectives, the Board of Trustees, Investment Committee, Staff, Investment Consultants, Investment Managers and Custodian(s), shall exercise care, skill, prudence and diligence.

1. Board of Trustees – The Board has ultimate fiduciary responsibility for the investment performance of all Foundation assets.
    - This Investment Policy expresses the Board's direction for the management of its investments.
    - The Board delegates the responsibility for the implementation of this Investment Policy to the Investment Committee.
    - This Investment Policy can only be amended with the Board's approval.

2. Investment Committee – The Investment Committee has the responsibility to manage the investment of Foundation assets in accordance with this Investment Policy. The Investment Committee:
    - Subject to Board approval, engages the services of Investment Consultant(s) in accordance with this Policy.
    - Evaluates the performance of the overall portfolio and individual Investment Managers in accordance with the Investment Policy.
    - Evaluates the performance of the Investment Consultant and other service providers.
    - Reviews this Policy annually and reports to the Board any recommended changes for the Board's approval.
    - Periodically report to the Board investment performance, changes in Investment Managers and performance of Investment Consultant(s).

3. Staff – Staff are employees of the Foundation with responsibility for the following duties:
    - Administer the Foundation's assets consistent with the policies, procedures and guidelines approved by the Investment Committee and Board.
    - Provide input to the Investment Committee on Foundation related issues to facilitate their decision making.
    - Manage the Foundation's relationships with external service providers.

4. Investment Consultant(s) – The Investment Consultant(s) shall provide expert advice and recommendations to help the Board and Investment Committee fulfill their fiduciary responsibilities. The Investment Consultant(s) will be recommended to the Board by the Investment Committee with Board approval required. The Investment Consultants:

- Review investment policies, objectives and guidelines annually and suggest appropriate changes.
- Evaluate long-term capital market trends and suggest broad-based allocation policies to be approved by the Investment Committee and, when required, the Board and implemented by Investment Managers, as well as general advice concerning periodic asset allocation rebalancing.
- Exercise a duty of reasonable care to comply with the scope and terms of their delegation of authority from the Board and Investment Committee.
- Research and recommend Investment Managers which are appropriate to implement the Foundation's investment policies and objectives.
- Measures and evaluates investment performance.
- Reports investment performance to the Investment Committee.
- Implement in a timely and effective manner the investment actions as directed by the Investment Committee and Staff.
- Provide investment reports and in addition accounting statements, including all transactions, based on accurate security values both for cost and market value. These reports should be provided on a time frame acceptable to the Investment Committee and Staff.
- Report to the Investment Committee situations where security pricing is either not possible or subject to considerable uncertainty.
- Provide assistance to the Investment Committee and Staff in order to complete such activities as the annual audit, transaction verification, or unique issues as they arise.
- Notify the Investment Committee and Staff promptly if there is a change in ownership or control of its organization.

5. Investment Managers – Investment Managers shall have discretion to invest Foundation assets under their care, custody and/or control in accordance with this Policy's objectives and guidelines set forth herein.
    - Choose specific securities, within the asset class for which they were chosen, to meet the Foundation's investment objectives.
    - Decide when to purchase, sell, or hold these individual securities.

6. Custodians – The assets of the Foundation may be held by an institution designated as the Custodian who shall manage, control, collect and use the assets of the Foundation in accordance with this Investment Policy. The Investment Committee recognizes that accurate and timely completion of custodial functions is necessary for effective investment management and accurate records. Following are the basic duties of the Custodians:
    - Provide complete custody and depository services for designated accounts.
    - Implement in a timely and effective manner the investment actions as directed by the Investment Committee and Staff.
    - Collect all income and principal realizable and properly report on periodic statements.

- Provide accounting statements, including all transactions, based on accurate security values both for cost and market value. These reports should be provided on a time frame acceptable to the Investment Committee and Staff.
- Report to the Investment Committee situations where security pricing is either not possible or subject to considerable uncertainty.
- Provide assistance to the Investment Committee and Staff in order to complete such activities as the annual audit, transaction verification, or unique issues as they arise.
- Notify the Investment Committee and Staff promptly if there is a change in ownership or control of its organization.

IX. Criteria for Selecting Investment Managers

The Investment Committees' selection of and Investment Consultants' recommendation of Investment Managers will be based on prudent due diligence procedures. Investment Managers shall be chosen considering the following criteria:

1. The investment style and discipline of the proposed manager.
2. The size of the organization as measured by the amount of assets under management with respect to the investment style under consideration.
3. Experience of the organization as measured by the tenure of the professionals with respect to the investment style under consideration.
4. Past performance, considered relative to other investments having the same investment objective. Consideration shall be given to both performance rankings over various time frames and consistency of performance.
5. The historical volatility and down-side risk of each proposed investment.
6. How well each proposed investment complements other assets in the portfolio.

X. Investment Manager Performance Review and Evaluation

The Investment Committee will review with the Investment Consultant(s) the performance of the Investment Managers quarterly. The performance monitors will consider the following criteria:

1. Investment Managers' adherence to this Investment Policy.
2. Investment Managers' performance versus the appropriate market indices.
3. Investment Managers' performance versus peer group rankings. Each Investment Manager is expected to perform in the top 40% of their respective peer group over the most recent three year time period.
4. Opportunities available in the equity, fixed income and alternative investment markets.
5. Material changes in the Investment Managers' organizations, such as changes in investment style, personnel changes, and account acquisitions or losses.

The Investment Committee may discharge or replace an Investment Manager at any time it deems such action is necessary and appropriate. The Investment Committee will notify the Board of such actions.