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# Developing an Investment Policy Statement for Nonprofits



# Introduction

An investment policy statement (IPS) for nonprofits such as public charities and private operating foundations is a living document that governs the investment of the organization's charitable assets to further its philanthropic mission. Essentially, an IPS is a roadmap for investing the nonprofit's financial assets in stocks, bonds, ETFs, mutual funds, or other financial investments.

## **The IPS answers questions such as:**

- What asset classes and investment vehicles should be considered?
- What are the criteria for selecting or replacing investments?
- What level of risk tolerance is acceptable?
- What is the time horizon for the investments?
- What is the spending policy?

Nonprofit and foundation boards have a fiduciary duty to monitor investments and take action, when necessary, to protect the financial viability of the organization. Having, abiding by, and regularly evaluating the IPS is considered a best practice and is integral to the strategic management of assets.

# A Roadmap

As a roadmap for how assets will be invested, an IPS helps the nonprofit and foundation focus on the purpose of the charitable assets. An IPS can provide a means to:

- Document the organization’s investment philosophy and goals
- Define what goals philanthropic capital is to be used for:
  - Operating expenses
  - Charitable giving
  - Annual or program funding
  - Scholarships
  - Capital projects or investments
- Quantify the need and return expectations
- Incorporate the annual spending policy into the investment strategy
- Be mindful that some investments may be restricted as “endowed” funds, thus they are not to be used for short-term cash flow needs



# Investment Policy Best Practices

The IPS states the organization's investment objective. It is developed by taking into account several factors, such as its risk tolerance, investment time horizon, and spending policy, which then can serve as the basis for asset allocation. Since the statement reflects the philosophy of the nonprofit or foundation, the investment policy should be as specific as possible. Of course, policies will vary depending on the goals and governance of the nonprofit and can include:

## **Purpose of Capital**

A statement outlining the investment goals in the context of the organization's mission. It often includes information on the board's fiduciary duty regarding decision-making, stewardship, and obligation to act in the best interest of the nonprofit or foundation.

## **Time Horizon of Investments**

Stating the time horizon of the charitable or philanthropic capital to meet investment goals in your IPS will help identify the length of time assets are intended to be sustained. That may affect the board's decision on the investment horizons, time frames, types of investments, and fees.

## **Spending Policy**

Articulating the intended distribution rate and over a particular time frame (for example, a 3-, 5-, 7-year rolling plan) is important to supporting investment decisions around liquidity, while also providing the added benefit of flexibility in any single year.

## **Roles and Responsibilities**

The roles and responsibilities of the board of directors, committees such as investment and/or finance, and any professional investment advisors selected to manage and monitor the organization's investment assets should be outlined in the IPS. Defining those roles within the framework of objective decision-making and a continuity plan for times of leadership or management changes will help the organization stay focused on long-term goals.

# Investment Policy Best Practices

## (continued)

### **Board Governance**

Good governance supports a culture that maintains fiduciary best practices. It begins with a clear understanding of who is responsible for the oversight and management of the investment assets and the tasks necessary to implement the IPS. That awareness will help the organization stay focused on the long-term goals in times of change or during periods of market volatility and disruptions.

Keep in mind that the full board retains overall responsibility of assets and should receive regular reports on investments at least quarterly. When necessary, the board should take action to protect the financial viability of the organization.

### **Asset Allocation**

This section of the IPS specifies the strategic asset allocation ranges, including minimum, maximum, and target policy weights for each asset class. These include, but are not limited to, cash, bonds, equities, real estate, commodities, derivatives, and alternative investments such as private equity, private credit, and real estate. An investment advisor can help you identify indexes or benchmarks to measure performance for each asset class.

Each will have specific risks and opportunities, which an advisor also can help define. Among the considerations are liquidity, inflationary pressures, the interest rate environment, and sustainable and impact investing objectives.

### **Risk Tolerance**

The ability to assume risk is typically framed in context of the nonprofit's annual spending requirements and the time horizon of meeting investment goals. In taking an efficient investment approach, the IPS should indicate the level of risk (low, medium, or high) the organization will accept to achieve the portfolio's objectives. If desired, quantitative metrics can be included.

# Investment Policy Best Practices

(continued)

## **Risk Management**

Because market conditions may cause the portfolio's investment in various asset classes to vary from the established allocation guidelines, the IPS can include a risk-management section describing conditions and parameters for rebalancing. Of course, any rebalancing strategy involves a trade-off between risk reduction and transaction costs. Rebalancing reviews are generally conducted on a semiannual basis and when significant cash inflows or outflows occur.

## **Annual IPS Review**

Your board should review the IPS as least annually. When a major transition occurs, such as a change in the time horizon or investment objective, investment managers, spending, portfolio rebalancing, laws, or regulatory environment, it is an opportunity to re-evaluate the goals and performance of investments. That review may require redirecting investments.

## **Sustainability Criteria**

If your nonprofit or foundation has sustainable or impact investment policies and objectives, identify approaches to incorporate investments that consider sustainability criteria. The growth of sustainability and impact-focused strategies and products has created numerous options to increase returns and make an impact in society.

# Contact Us

An investment policy serves as a guide of how and when a nonprofit organization or foundation invests funds in a responsible, sustainable manner. While the board is ultimately responsible for establishing and monitoring the financial viability of the organization, professional investment advisors can help.

William Blair has extensive experience working with nonprofit and foundation boards. We can help you determine how an investment policy statement can help your organization further its mission and how to best achieve those objectives.

If you are interested in learning more, contact a William Blair wealth advisor or email [pwm@williamblair.com](mailto:pwm@williamblair.com).

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