E- 3. ENDOWMENT FUND INVESTMENT POLICY

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Auburn University, (the “University”), investments will be managed by the Auburn University Foundation (the “Foundation”) Investment Committee and University staff in accordance with the policies established by the Board of Trustees (the “Board”). Policies currently governing significant areas of investment management are based upon actions of the Board of Trustees and the Investment Committee.

I. Management of University Investments

The Board of Trustees has delegated responsibility for the University’s investments to the Foundation Investment Committee, which shall recommend and implement investment policy with regard to asset allocation, manager selection and portfolio supervision. In order to facilitate communication and reporting between the Board and the Foundation Investment Committee, a member of the Board shall be appointed as a liaison to the Committee and shall serve as a voting non-director on that committee. The liaison reports to the Board the status regarding the University’s investment policies and results; and reports any recommended changes in investment policy to the Board.

A. Investment Committee Functions

1. The Investment Committee’s principal function is to develop and recommend to the Board such investment and investment related policies, as it deems appropriate.

2. No member of the Investment Committee shall have or appear to have a conflict of interest that impairs or appears to impair the member’s ability to exercise independent and unbiased judgment in the good faith discharge of his or her duties.

3. The Investment Committee will review regularly all investments of the University.

4. The liaison to the Investment Committee will make regularly scheduled reports to the Board of Trustees.

5. The Investment Committee recommends to the Board appropriate policies and procedures for custodianship and access to securities held by the funds, as it may deem appropriate.

6. The Assistant Treasurer, or his/her designee, is the Secretary of the Committee and shall keep minutes of the actions of the Committee.

7. The Committee may engage an investment consultant to work with staff, and advise staff and the Committee, on investment management issues including, but not limited to investment strategy, asset allocation, market trends, investment manager and custodian selection, manager and custodian evaluation criteria, investment performance evaluation, and any other appropriate matters.

B. Specific Functions of the Investment Committee

1. Establish investment objectives for the Endowment Pool.

2. Set asset allocation and manager structure policies for the investments.

3. Establish and continue to update the investment policy, and report the recommended changes to the Board.

4. Select, and as appropriate terminate, investment managers, fund custodian, and the investment consultant for the investments.

5. Establish, monitor, and update the investment process.

6. Review investment performance against established objectives.

7. Review, at least annually, investment activity to ensure compliance with investment policy.

8. Establish and propose to the Board, the spending policy for the Endowment Pool.

II. Endowment Investment Policy and Guidelines

The goal for AU's Endowment investment pool is to provide a real total return that preserves the purchasing power of the Endowment's assets, while generating an income stream to support the academic activities of the University. The Endowment's real total return will be sought from an investment strategy that provides an opportunity for superior total returns within acceptable levels of risk and volatility.

A. Investment Objective

For the long-term, the primary investment objective for the Endowment Pool is to earn a total return (net of portfolio management fees), within prudent levels of risk, which is sufficient to maintain in real terms the purchasing power of the Endowment's assets and support the defined spending policy.

B. Asset Allocation

To achieve its investment objective to the extent provided by law, the Endowment's assets will be allocated among six asset classes. The asset classes are domestic equity, international equity, alternative strategies, real assets, fixed income, and cash. The purpose of allocating assets to these asset classes is to ensure the proper level of diversification within the Endowment Pool.

The strategic asset allocation adopted by Board is:

ASSET CLASSES	Target Allocation	Range
Domestic Equity		
Large Cap	**15.0**	**10.0 - 20.0**
Mid/Small Cap	**7.5**	**5.0 - 10.0**
International Equity		
International Core Equity	**15.0**	**10.0 - 20.0**
Emerging Markets	**5.0**	**0.0 - 7.5**
Alternative Strategies		
Long/Short Hedge	**10.0**	**7.5 - 12.5**
Private Capital	**5.0**	**2.5 - 7.5**
Absolute Return	**10.0**	**7.5 - 12.5**
Real Assets	**15.0**	**10.0 - 20.0**
Public/Private Real Assets		
Fixed Income	**17.5**	**12.5 - 22.5**
Multi-Strategy		
Cash	**0.0**	**0.0 - 5.0**
TOTAL	**100.0**	

Auburn University has modeled the expected return and volatility of the portfolio. The assumptions for the endowment's portfolio are included in Appendix 1.

1. The purpose of equity investments in the Endowment, both domestic and international, is to provide capital appreciation, current income, with the recognition that this class of investment carries with it the assumption of potentially high market volatility over some periods.

2. The purpose of fixed income investments, both domestic and international, is to provide diversification and a highly predictable, dependable source of income. Fixed instruments should reduce the overall volatility of the Fund's assets and provide a deflation hedge.

3. The purpose of private capital investments (including Venture Capital and Private Equity) is to provide long-term appreciation of principal and diversification. The Investment Committee recognizes that private capital investments are more susceptible than stocks and bonds to extended periods of overvaluation and undervaluation, and that returns are much more manager dependent than is the case for marketable securities.

4. The purpose of hedge funds is to earn equity-like returns with less volatility over time. Additionally, hedge funds provide an additional benefit of providing portfolio diversification thereby lowering the probability for the Endowment to have large market value variations over short-term time horizons.

5. The purpose of real assets is to achieve capital appreciation, current income and to invest in an asset-class that has low to negative correlation to unexpected inflation. Real assets also have low correlation to marketable securities – i.e., fixed income and equities.

6. The purpose of diversification is to provide reasonable assurance that no single security, or class of securities, will have a disproportionate impact on the performance of the total fund. Within all asset classes, managers (i.e., active managers or providers of passive investment products) with different investment styles will be employed. Diversification by investment style is an important step in reducing the risk of the Endowment. Investment styles within the seven asset classes are defined as follows:

    a. Domestic Equity

        i. *Large Capitalization* - Managers who invest in larger capitalization companies (generally greater than $10.0 billion).

        ii. *Mid Capitalization* - Managers who invest in mid-sized capitalization companies (generally $2 billion to $10 billion).

        iii. *Small Capitalization* - Managers who invest in small capitalization companies (generally up to $2 billion).

    b. International Equity

        i. *International Market Equity* - Managers who primarily emphasize stock selection in their portfolio construction. The country selection process is mainly a byproduct of the stock selection decision, or can be passively set according to the index country weights.

        ii. *Emerging Markets Equity* – Managers who invest in less-developed economic regions of the world such as Korea, Taiwan, Chile, India, etc.

c. Alternative Strategies

i. *Venture Capital* – Managers who invest in start-up and early stage, high-growth companies. The venture capitalists usually own a minority stake in the company, but are actively involved with the founders to develop strategy, secure financing and recruit management. The main investment objective is to earn returns above those generally available in the public securities market, achieved with long-term capital appreciation.

ii. *Private Equity/Buy Out* – Managers who invest in transactions such as acquisitions, leveraged buyouts, management buyouts, reorganizations, restructurings and spin-offs. The manager usually owns a majority equity position or acquires the entire company. Private equity firms frequently use leverage.

Equity distributions from private equity and venture capital investments, such as the receipt of shares of a company that has gone public, will be liquidated as soon as possible.

iii. *Multiple Hedge Funds/Absolute Return Strategies* – Managers who apply flexible investment styles (i.e., short selling leverage, concentration) across and within asset classes. Strategies include, but are not limited to, the following: merger arbitrage, convertible arbitrage, fixed income arbitrage, hedge equity, long/short equity market neutral, multi-strategy, and global macro managers.

Managers will only be selected if they are annually audited by an independent audit firm

d. Real Assets

i. *Private Real Estate* – Managers who invest in commercial real estate equity, held as individual assets or in commingled vehicles. Holdings generally are significant ownership of commercial buildings such as office, warehouse, retail shopping, and apartments with the intent to earn both a high-current income and longer-term capital appreciation.

ii. *Public Real Estate (REITs)* - Managers who invest in publicly traded real estate investment trusts and real estate operating companies.

iii. *Timber* – Managers who invest in timberlands and private timber companies to manage and harvest timber for pulp, construction, and fine woods. Timber investment companies are generally private investments with the objective to earn high-current income and longer-term capital appreciation.

iv. *Gas/Oil Partnerships* – Managers who invest gas and/or oil operating companies. The objective is to earn a high-current income with return of capital.

v. *Commodities* – Managers or commodities-based indexes that invest in commodities. The objective of investing in this sub asset-class is to gain additional portfolio diversification, inflation protection from unexpected inflation and positive real returns.

e. Fixed Income

i. *Multi-Strategy* - Managers who have the flexibility within parameters to invest in U.S. Investment Grade Bonds, Non-U.S. Investment Grade Bonds, and U.S. Non-Investment Grade.

f. Cash

i. *Money Market Funds* – Short-term pooled investments with a daily net asset value of $1.00.

C. Asset Allocation Review and Balancing Procedure

1. The Investment Committee will review the strategic allocation in the six asset classes, as well as the allocation to various styles of managers within these asset classes, at least annually.

2. Cash flows into and out of the portfolio (i.e., new gifts and spending) shall be allocated to the investment managers each month in a manner that will rebalance the portfolio consistent with asset allocation policies. Rebalancing the portfolio by means of liquidating assets managed by investment managers will be the exception, and only done, when recommended by the investment consultant. Asset allocation reports will be provided to the Committee on a quarterly basis.

D. Performance Measurement, Monitoring, and Evaluation

1. Performance (net of fees) will be calculated on a quarterly basis by the consultant.

2. In addition to reporting time-weighted total returns for each manager and the Pool, a comparison is made with relevant market benchmarks as well as the composite returns for other money managers with similar philosophies to those managers investing for the Pool. Managers should add value above these benchmarks. Reports will include historical data in order to evaluate short-term results against longer-term strategies.

E. Guidelines for Corrective Action

Corrective action should be taken as a result of an ongoing investment managers review process. The following are instances where corrective action or termination may be in order:

1. Major organizational changes in a firm, including any changes in portfolio managers, may require a new contract and interview process. Failure on the part of the Investment Manager to notify the Committee of such changes is grounds for termination. At all times, communication with the managers should be open and informative. Investment managers should be willing and able to meet at least annually with the Committee.

2. Violation of terms of contract constitutes grounds for termination.

3. As part of its overall asset allocation strategy, the Committee will choose managers with certain styles and approaches to provide portfolio diversification. Therefore, it is critical that managers adhere to the original intent of the Committee at the time they are engaged. Any significant changes in investment approach may be grounds for termination.

4. The Committee will not, as a rule, terminate a manager on the basis of short-term performance. If the organization is sound and the firm is adhering to its style and approach, the Committee will allow a sufficient interval of time over which to evaluate performance. The Committee's consultant will provide insight regarding the appropriate length of time. The manager's performance will be viewed in light of the firm's particular style and approach, keeping in mind at all times the Pool's diversification strategy and, as well as, other organizational and relationship issues.

5. Investment managers may be replaced at any time as part of the overall restructuring of the Endowment Pool.

6. Other events or circumstances that are deemed to be in the best interest of the University.

F. Endowment Spending Policy

The long-term objective of the endowment spending policy is to maintain the purchasing power of each endowment with the goal of providing a predictable and sustainable level of income to support current operations. Under this policy, spending for a given year equals 80% of spending in the previous year, adjusted for inflation (CPI within a range of 1% and 6%), plus 20% of the long-term spending rate (4.5%) applied to the twelve month rolling average of market values. The initial spending rate for new endowments with no previous year's spending shall be 4.5% applied to twelve-month (or number of months that the endowment is in the pool) rolling average market values. This spending policy has two implications. First, by incorporating the previous year's spending, the policy eliminates large fluctuations and so enables the University to plan for operating budget needs. Second, by adjusting spending toward a long-term rate of 4.5%, the policy ensures that spending levels will be sensitive to fluctuating endowment market value levels thereby providing stability in long-term purchasing power.

The annual administrative fee, with a long-term spending rate determined by the Board, is also calculated each year by using the spending model described above. The monies generated by this assessment are used to fund the development activities of the University.

An example of the spending calculation can be found in Appendix 2.

G. Gift Policy

It is anticipated that from time to time the University will receive gifts in the form of marketable securities. In such event, the Office of Treasury Services will liquidate the securities as soon as possible. In the event that the securities are restricted from sale for a designated period of time due to regulatory reasons, the University will hold said securities until the restricted period has elapsed and then liquidate the securities as soon as possible thereafter. The University will make no attempt to add value to the Pool by holding gifted securities.

H. Custodian and Depository Activities

The custodian and depository activities of the Pool, including agreements with any banks for the temporary, short-term investment of cash and equivalents will be subject to annual review by the Committee to assure that the University is receiving competitive rates and services.

ADOPTED: January 31, 2008

REAFFIRMED: June 19, 2009

Appendix 1

Asset Allocation Input Assumptions

Expected Returns, Risks, and Correlations

	Expected Return	Standard Deviation	Domestic Equity	Non-US Equity	Hedge (High Vol)	Emerg Mkt Equity	US Core Bond	High Yield Bond	TIPS	World Gov. Bond	Municipal Bond	Emerg Mkt Debt	US Cash	Absolute Return (Low Vol)	Private Eq	Timber	Commodities	Real Estate	US Inflation
Domestic Equity	9.00	19.00	1.00																
Non-US Equity	9.50	19.00	0.70	1.00															
Hedge (High Vol)	9.00	12.00	0.81	0.53	1.00														
Emerg Mkt Equity	10.75	28.00	0.47	0.43	0.36	1.00													
US Core Bond	5.50	6.50	0.20	0.19	0.28	-0.18	1.00												
High Yield Bond	7.00	10.00	0.55	0.42	0.43	0.31	0.32	1.00											
TIPS	4.50	4.50	-0.51	-0.48	-0.33	-0.34	0.78	-0.17	1.00										
World Gov. Bond	5.50	8.50	0.11	0.39	0.13	-0.15	0.74	0.13	0.41	1.00									
Municipal Bond	4.00	5.50	0.20	0.17	0.30	-0.14	0.87	0.34	0.80	0.65	1.00								
Emerg Mkt Debt	7.50	18.00	0.52	0.36	0.53	0.59	0.14	0.53	-0.02	-0.13	0.16	1.00							
US Cash	3.50	2.00	0.00	-0.13	0.06	-0.23	0.11	-0.05	-0.08	-0.07	0.00	0.03	1.00						
Absolute Return (Low Vol)	8.50	5.00	0.63	0.45	0.70	0.25	0.30	0.47	-0.24	0.16	0.25	0.61	0.23	1.00					
Private Eq	12.50	28.00	0.58	0.30	0.64	0.21	0.00	0.20	-0.33	-0.05	-0.06	0.41	-0.08	0.40	1.00				
Timber	8.50	12.00	0.06	0.05	0.13	0.04	0.11	-0.01	-0.11	0.00	0.14	0.04	0.23	-0.01	0.14	1.00			
Commodities	8.00	20.00	-0.17	-0.18	-0.06	-0.11	-0.13	-0.31	0.12	-0.05	0.01	0.10	-0.01	0.06	-0.02	-0.09	1.00		
Real Estate	8.50	11.50	-0.03	0.01	-0.02	-0.17	-0.16	-0.15	-0.20	-0.14	-0.22	-0.03	0.32	0.02	-0.01	-0.21	0.05	1.00	
US Inflation	2.50	2.00	-0.13	-0.26	-0.12	-0.10	-0.24	-0.19	0.07	-0.24	-0.24	-0.08	0.32	0.12	-0.18	-0.09	0.25	0.24	1.00

*Expected returns are for the next 10 years; correlations are based on the longest historical data streams available.

Appendix 2

Sample Spending Calculation

In accordance with the Auburn University Endowment Fund Investment Policy, the endowment spending is calculated using the following formula:

[(80%)(prior year's distribution)(1+CPI)] + [(20%)(twelve-month rolling average market values)(4.5%)]

Spending Calculation:

Sample endowment has a prior year distribution of $74,645. CPI was 3.4%. The twelve-month rolling average of market values is $1,563,895.

[(.80)($74,645)(1+.034)] + [(.20)($1,563,895)(.045)] = $75,821

Appendix 3

Responsibility Table

FIDUCIARY LEVEL	WRITTEN INVESTMENT POLICY	WRITTEN INVESTMENT STRATEGY	TACTICAL ALLOCATION AMONG ASSET CLASSES	STRATEGY WITHIN AN ASSET CLASS	MANAGER & FUND SELECTIONS	SECURITY SELECTION
BOARD OF DIRECTORS	APPROVES	INFORMED	INFORMED			
INVESTMENT COMMITTEE	RECOMMENDS	APPROVES	APPROVES	APPROVES	APPROVES	INFORMED
INVESTMENT CONSULTANT & STAFF	RECOMMENDS	RECOMMENDS	RECOMMENDS	RECOMMENDS	RECOMMENDS AND MONITORS	MONITORS
INDIVIDUAL MANAGERS						APPROVES