BEING A BOARD MEMBER DURING TIMES OF MARKET VOLATILITY

JUNE 2020

Volunteer Without Fear: How the OCIO Model Can Help

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Boards play a critical role in the livelihood of nonprofits and the communities they serve. They are the governing fiduciaries backing talented staff teams—an honorable group of individual professionals who are committed to supporting a given organization and believe in community change. Board membership is often coveted, as it enables emerging professionals to express their passions and demonstrate leadership, and retirees to continue to leverage their career through a proverbial "second act."

Boards are the financial stewards and guardians of community assets; they are the grant-makers of scholarships and the securers of strategic investments. Due to the important nature of these decisions, many boards require aspiring members to submit applications and letters of recommendation to help ensure they are qualified to fulfill the entailed fiduciary responsibilities. Board members must adhere to four broad principles:

1. Act prudently and diversify endowment and foundation investments to minimize the risk of large losses
2. Follow the governing documents and donor intent
3. Serve the client first, providing impartial advice
4. Adhere to the duties of prudence, loyalty, and care

As any experienced board member knows, there is one common truth about board membership that is never more evident than in times of crisis—it is voluntary. Directors and trustees are forced to revert to nine-to-five CEOs and lawyers, and devoted parents and children. They are required to focus and sort through the host of priorities demanding their time, which, unlike their community aspirations, is finite.

The COVID-19 pandemic tore through our everyday lives like wildfire. The fastest 30% market decline in the history of the equity markets sent capital markets into free fall.[1] Seemingly overnight, longstanding higher education institutions sent students home, public worship services were cancelled, and community foundations scrambled to create community relief funds. Suddenly, "Am I fulfilling my fiduciary duty?" became a loaded question, unravelling the following thoughts that may be tough to answer:

- Is our portfolio strategy truly consistent with our stated objectives?
- Is each segment of the portfolio fulfilling its assigned role?
- Is the valuation accurate for less liquid investments?
- Who is responsible for compliance?

For some trustees, the decision made before the virus to engage in a discretionary investment relationship—often referred to as Outsourced Chief Investment Officer (OCIO)—has provided solace. Under this model, the board decided to employ an outside investment advisor to manage the organization's foundation or endowment assets. This comprehensive portfolio management model translates to implementing portfolio strategy with full discretion to hire and fire investment managers and includes enhanced risk management. In a non-discretionary investment model, those trustees who serve on boards may find that more work is necessary before they can find peace; individual board members still hold responsibility for monitoring and managing many fiduciary obligations under the traditional consulting model.

So why does the OCIO model provide trustees consolation during times of extreme market volatility, as has occurred in the wake of COVID-19?

Bases are covered: While OCIO can take many forms, one of the most basic features of any discretionary relationship can be especially helpful in times of uncertainty: continuous monitoring. OCIO firms provide nonprofit organizations with additional fiduciary oversight; teams are stacked with investment professionals devoted to monitoring each position in the portfolio within the guidelines of the organization's investment policy statement (IPS). Unfortunately, many nonprofits are understaffed. Community foundations, for example, have less than one full time equivalent dedicated to the investment portfolio.[2] Thus, it cannot be assumed that staff will be capable of providing continuous coverage during volatile periods.

All systems go: Monitoring portfolio risk may require changes or adjustments to be made to a portfolio immediately. Depending on the type of change—i.e., rebalancing to policy guidelines or for opportunistic positioning—it may be imprudent to wait until the next quarterly board meeting to implement. As the OCIO partner is given discretion over portfolio management, they have the green light to make changes within the guidelines of the organization's IPS when necessary.

Quality in consistency: Change in board leadership and composition often comes with a fear of "rocking the boat," which can impede quick decision-making and postpone the implementation of good ideas in the investment portfolio. The objective, discretionary nature of the OCIO relationship keeps the ball rolling across board terms and helps to ensure that a nonprofit's portfolio is adequately positioned for a fast-moving crisis.

Headline risk averted: Need we say more? With total portfolio management comes total accountability. A nonprofit's OCIO firm is on the hook for the impact of decisions made in the portfolio.

Market dislocations provide opportunities: Just as it is an OCIO partner's job to monitor positions, they should also be on the lookout for opportunities. When markets move quickly, so do windows of value in market dislocations. The OCIO model can help organizations avoid investment slippage by dodging lag time associated with majority voting and reviewing capacity issues with staff.

With the appropriate level of support and expertise, boards provide nonprofit organizations with stability through periods of crisis and triumph. Those fiduciaries who are aware of common shortcomings in focus, decision-making, and structure may have a better opportunity for continued success.

FEG has several thought pieces which may be helpful for identifying the strengths and weaknesses of your organization's governance structure. Those publications, as well as other helpful insights, can be found here: https://www.feg.com/insights.

To the individual trustees and directors, FEG thanks you for your continued commitment to your organizations and their endowments and foundations! We are incredibly honored to work alongside you to help make positive, lasting change in your communities.

Do you know an organization that could benefit from the OCIO model? Reach out to Devinne Kelly, one of FEG's Senior Associates standing by to help: dkelly@feg.com 513.827.3204, or visit www.feg.com for more information and additional resources.

[1] Financial Times, @_PeterWells, S&P Global, Refinitiv. FT Calculations using bear markets as classified by S&P Global.

[2] FEG 2019 Community Foundation Survey, www.feg.com/cfsurvey

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