U.S. TRUST
Bank of America Corporation

INTELLIGENT OUTSOURCING

Considering and selecting an OCIO

OVERVIEW

Boards of directors, investment committees, corporate officers and plan sponsors all face substantial challenges in carrying out their fiduciary obligations. Common issues include increasingly complex and stringent legislation, higher expected standards in fiduciary management, a greater level of scrutiny and the push to do more with less. Additionally, a market driven by exceptional macroeconomic policies, higher levels of investment complexity and increasing financial demands creates a more challenging environment for investment portfolios that support their financial obligations.

To reconcile competing claims on senior executives' attention, organizations are revisiting their existing investment processes and investment manager relationships. By ensuring that the investment portfolio is managed by a fiduciary investment manager, in accordance with guidelines and goals set by leadership, executives can contribute their talents at the "highest and best use" level. Institutions without a chief investment officer can outsource their investment management, freeing boards of directors and plan sponsors to focus on providing the leadership, guidance and oversight their organizations require. While outsourcing the investment function does not relieve the board of its fiduciary obligations — the responsibility for the hiring and oversight of the investment management firm remains with them — it allows them to work alongside a "co-fiduciary" who manages the investment process within board guidelines.

This paper examines when the outsourced chief investment officer (or "OCIO") arrangement may be appropriate for an organization. We consider how this collaborative relationship can help the leadership team balance its responsibilities to the organization and its mission by providing fiduciary leadership and oversight. Finally, we outline the process for selecting the appropriate investment manager and what to expect as you transition your investment portfolio. This holistic approach provides an investment process that is designed, executed and evaluated in terms of its abilities to fulfill the organization's financial responsibilities and goals.

CONTENTS

FIDUCIARY OBLIGATIONS OF EXECUTIVE LEADERSHIP

Boards of directors provide leadership, stewardship and oversight so that the organization can identify and carry out its purpose. This means that each board member is a fiduciary of the organization, entrusted with the stewardship of all of the organization's assets. These assets include the organization's reputation, its people and all of its property and investments. These fiduciary responsibilities are defined by three requirements: loyalty, prudence and care. These long-standing characteristics help to guide fiduciaries as they carry out their responsibilities.

LOYALTY, PRUDENCE, CARE: THREE FIDUCIARY REQUIREMENTS

Loyalty requires placing the interests of the organization ahead of personal interests. It also requires maintaining objectivity and remaining free from conflicts of interest. When such conflicts are inevitable and unavoidable, the duty of loyalty requires adequate disclosure.

Prudence requires that fiduciaries understand and comply with all applicable laws. It also requires having the knowledge, experience and resources required to carry out one's duties. When any of these are lacking, it is the duty of a fiduciary to delegate these responsibilities appropriately.

Care requires diligence in executing all responsibilities, decisions and actions on behalf of the organization. Once again, this requires that fiduciaries provide the resources necessary for both the planning and the execution of these decisions.

Failing to effectively carry out any aspect of fiduciary responsibility can result in potentially devastating consequences for an organization. Therefore, managing fiduciary risk is a key responsibility for an organization's leadership.

A fiduciary approach to risk management will form the scope of responsibilities for the organization's leadership, with emphasis on three broad areas that are affected:

- The organization and its reputation
- The mission and goals of the organization
- Its financing and investment programs

The organization's leadership is the sole group responsible for designing the goals, risk tolerances and governance policies for these three areas. This leadership function is distinct from the management function, which is responsible for the execution of these policies. Larger organizations often distinguish between leadership and the management staff, while smaller organizations may require people to "wear two hats" and assume responsibility for leadership as well as management and execution. Lack of resources is not just an operational issue — it's a risk issue that must be managed. The organization's leadership must decide whether the organization should "own" this responsibility by expanding their existing team, or whether its resources would be more appropriately allocated to other responsibilities.

For many organizations, the investment portfolio is the link between the organization's financial goals and the revenues that finance carrying out those goals. The board of directors' primary financial responsibility is preserving the real value of the investment portfolio over the long term while spending from the investment portfolio with the expected investment returns. The issue of spending policy goes beyond simply determining a sustainable spending rate, and includes other significant decisions that can have a profound effect on the sustainability of the investment portfolio. While this is a key long-term investment decision, it rarely receives attention from investment committees. A goals-based, client-centered approach recognizes the importance of spending policy, and the investment portfolio becomes integrated into the organization's mission. The board of directors provides leadership by specifying and communicating the goals, governance and appropriate risk tolerance to those responsible for managing the investment portfolio.

NAVIGATING THE NEW REALITY

Expectations of lower market returns, greater market volatility and high cost of liquidity drive the "new reality" of global investment markets. Organizations are increasingly challenged to fund their financial obligations as well as to provide ongoing support for their missions. With annual spending plans in place, charitable organizations must somehow continue to finance these monetary outflows while earning less on their investment portfolios from simple market returns. Low return and low interest rate environments, combined with actuarial assumptions about extended life expectancies, have led to increasing pension problems and liabilities. Given these challenges to both investment portfolios and the market environment of potential returns, nonprofits and pensions are facing an uphill battle to finance their missions. Organizations will need to find additional sources of return beyond the average market return. Investment returns are generated from three main sources: strategic asset allocation, tactical asset allocation and manager selection. Greater sophistication and opportunity in the allocation of investment resources may be required to generate greater returns in a lower return investment environment.

KEY AREAS WHERE NONPROFIT ORGANIZATIONS MAY ADD LONG-TERM VALUE AND BUILD RESOURCES TO CONTINUE AND EVEN EXPAND THEIR MISSION

MAXIMIZING THE IMPACT OF ASSET ALLOCATION

Organizations will need to tap into a global asset allocation that incorporates all appropriate sources of return while providing necessary risk management. This begins with a rigorous strategic asset allocation of both global public investments, such as stocks and bonds, and alternative investments, such as real estate, commodities, private equity and hedge funds. These alternative investments can be sources of additional incremental return with the potential to lower market risk and market volatility within the investment portfolio, given the opportunity for diversification they may provide. After initiating this diversified strategy, organizations can make timely shifts in these market allocations with the goal of capturing short-term opportunities while simultaneously mitigating short-term risks. If executed skillfully, this tactical asset allocation can help grow the organization's capital, while reducing the potential for losing capital from short-term market declines.

MANAGER SELECTION

Beyond the careful deployment of capital, organizations may seek additional return opportunities by employing specialist managers in each of these market segments. This "manager selection" process may present the opportunity to earn above-market returns through the selection of individual investments. Given the number of asset classes requiring specialists in due diligence, this is a highly resource-intensive task. This is especially true for investments such as hedge funds, where due diligence requires sophisticated strategies and complex trading mechanisms. Investment programs such as the one described here require substantial expertise and resources. The design of the investment plan, its execution, its monitoring and its evaluation are each areas of specialization, and these specialties must be coordinated in the context of the organization's unique financial goals. Data from a study by NACUBO/Commonfund[1] published in June 2014 showed that it is unlikely that any but the largest charities and pensions have adequate staff to manage these tasks.

THE CASE FOR OUTSOURCING

To be of the greatest benefit to the organization, the board of directors should identify those key tasks that constitute the board's "highest and best use." Since the board is the only group that can provide leadership regarding the organization's goals and risk management policies, it will likely delegate the management and execution of some of these goals and policies to others. This could include both internal and external staff. However, in the area of financing, and especially in regard to investment management, the board and even the staff of the organization are not intrinsically linked. In fact, the complexity and specialization required for prudent and effective investment management go beyond the resources and expertise of most organizations. The best course of action may be to outsource these responsibilities and share the fiduciary risk of managing the investment portfolio. An adequate due diligence function requires evaluation of both the investment process and the various back-office operations, such as trading, accounting and reporting. In addition, periodic on-site visits are required. Some of the recent financial scandals in investments have occurred because of inadequate due diligence, especially with regard to investment operations. The not-for-profit organizations that invested in these funds faced dire consequences, such as loss of investment value, fines to the organization and its individual directors, and loss of reputation.

> The complexity and specialization required for prudent and effective investment management go beyond the resources and expertise of most organizations.

If outsourcing, the board and its investment committee are still required to provide the leadership and oversight of the investment portfolio to ensure it is managed in a way that is consistent with their financial goals. Outsourcing allows the organization to tap into substantial resources without having to "own" them, thereby providing more time to address issues and activities that truly warrant the board's attention. By reorganizing and realigning its time, budget and other resources, all of the organization's fiduciary responsibilities can be assigned appropriately, and the organization can enjoy a holistic view of its mission, resources and results.

Employing an OCIO should improve control and oversight of all service providers to the investment portfolio and their interdependent responsibilities, tasks and activities. Let's compare and contrast the traditional arrangement — where the board and its investment committee are tasked with managing the investment portfolio — with the OCIO opportunity, which focuses on the coordination of responsibilities among the various participants. Even without considering changes to the board or the investment committee, this complicated task requires tremendous coordination amidst overlapping participant responsibilities. Figure 1 illustrates these interactions between the board, the investment committee and the investment manager, with the support of a consultant and a custodian.

Now let's contrast this with the OCIO serving as the hub of this investment activity and all of its related tasks.

This overwhelming task is further complicated by continual turnover in board membership. We can see in Figure 2 that the OCIO approach coordinates all aspects of the investment process within a single resource. The investment manager can help to provide the continuity, organizational stability and "institutional memory" needed to sustain these responsibilities while balancing a dynamic and changing board. The benefits are clear for institutional asset owners such as nonprofit organizations and corporate pensions, and especially clear for smaller asset owners that lack appropriate resources or expertise.

The OCIO approach provides focus, consistency and clarity while simplifying communication to the board and its investment committee.

FIGURE 1

TRADITIONAL MODEL — INVESTMENT PORTFOLIO MANAGED BY BOARD OF DIRECTORS AND INVESTMENT COMMITTEE[2]

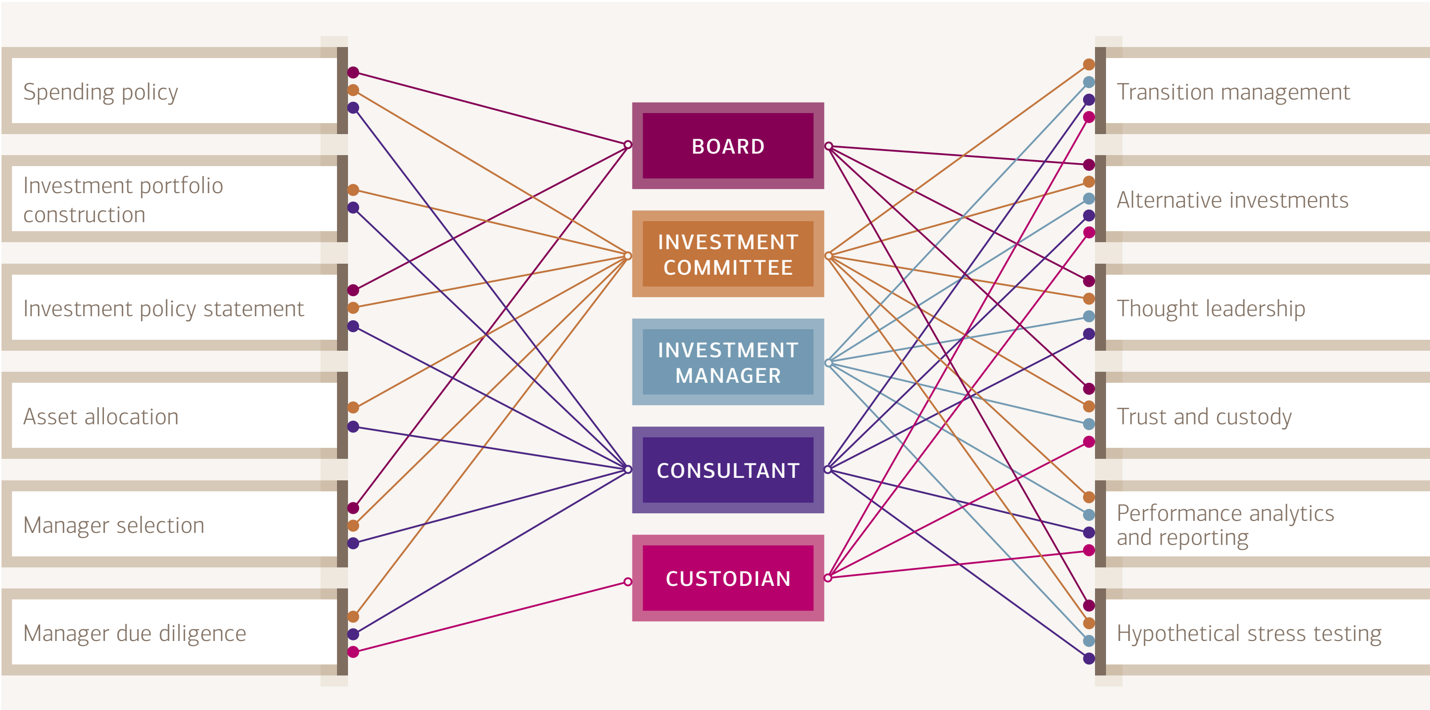
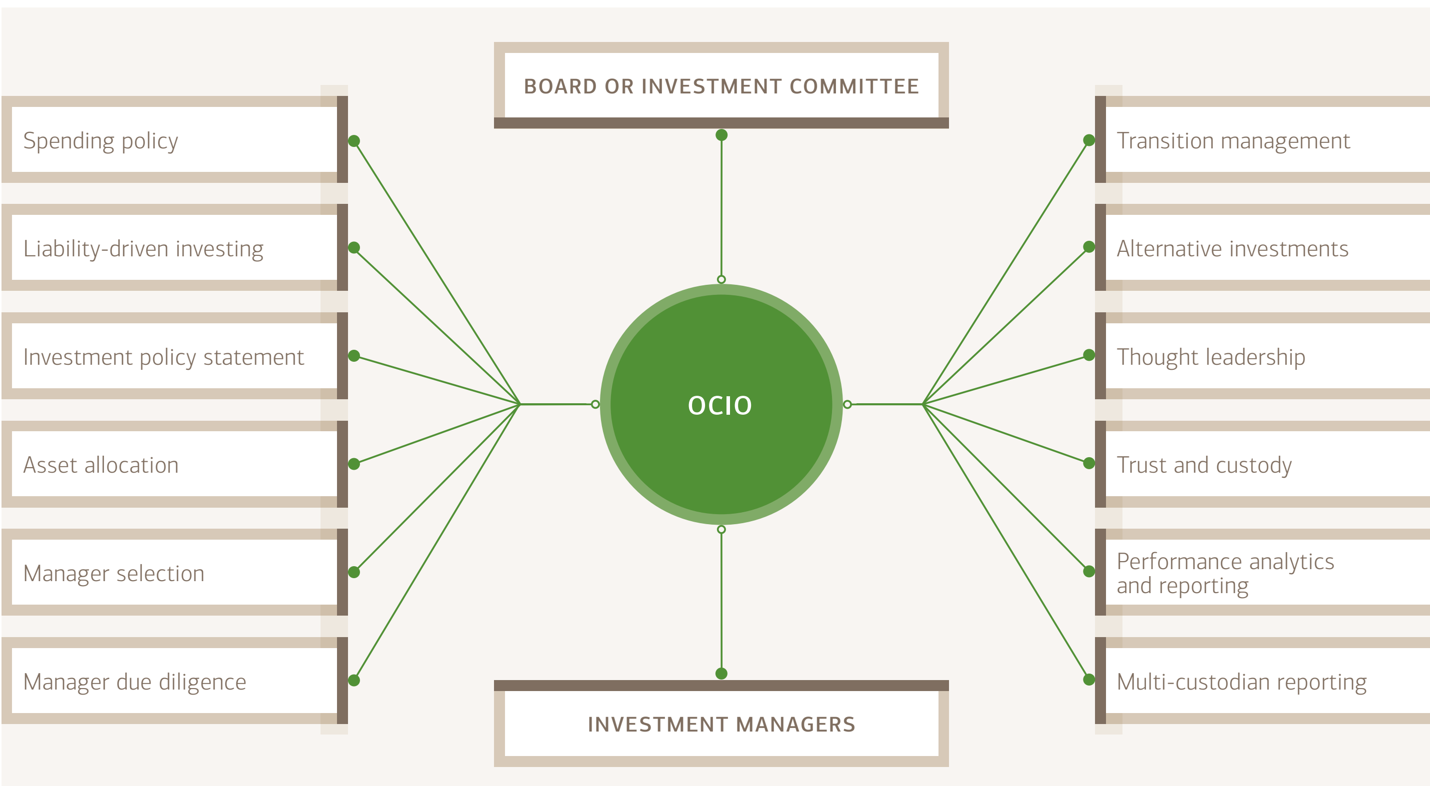


FIGURE 2

COORDINATING THE INVESTMENT PROCESS THROUGH THE OCIO[2]



ROLES AND RESPONSIBILITIES OF AN OCIO

We've noticed a significant amount of confusion within the investment industry regarding the types of service arrangements in place between various types of investment "advisors" and clients. In the NACUBO/Commonfund Study[1] mentioned earlier, we detected conflicting statistics that may indicate a widespread misunderstanding of the arrangements currently in place. Over 40 percent of institutions responding to the study claimed that they had outsourced their investment function. However, 85 percent of these participants also stated that they used an investment consultant as the primary advisor for their investment function. This suggests confusion regarding the definition of outsourcing, as well as a misunderstanding of the natures of the various investment relationships and the roles and responsibilities of each. So, let's take a look at those types of investment relationships.

Investment management relationships can be grouped into two categories: advisory and discretionary. The differences between these two types are discussed in the table below. Advisory relationships are characterized by the basic service of making investment recommendations. These recommendations may include strategic asset allocation, tactical asset allocation, manager selection and the oversight of these managers. Discretionary relationships are characterized by a delegation of responsibility to a third party who makes investment decisions on behalf of the client.

The fiduciary standard is the foundation for a consistent, disciplined investment process — but it's much more than just a standard of investing. The term "fiduciary" is widely used to describe the role of an investment advisor; however, there are three standards of care depending upon the type of investment firm:

- **Broker** — Requires that an investment must be "suitable" for a client "at the time a recommendation is made to an investor for a purchase, sale, or hold of a particular investment" in the context of the client's other holdings and financial situation and needs.
- **Investment advisor** — Requires that an investment must be "suitable" for a client both at the time the investment is purchased and on an ongoing basis in the context of the client's investment portfolio and other holdings, desired investment strategy and financial situation.
- **Trust fiduciary** — Requires that the trustee prudently manage the trust investment portfolio in light of the purposes, terms and other circumstances of the trust. The trust fiduciary standard requires that investment

TYPES OF INVESTMENT MANAGEMENT RELATIONSHIPS

ADVISORY RELATIONSHIPS	Many boards engage in an advisory relationship, whereby the **consultant or advisor simply provides recommendations to the board** regarding investment strategy and investment selection. • The board may feel that the decision making is **shared**, or that it lies with the advisor. Yet in reality the **decision making rests squarely on the shoulders of the board** and on each of its members in an individual, "joint and several" capacity. • This means **each and every member may be held financially liable** for the board's decisions.
DISCRETIONARY RELATIONSHIPS	A discretionary relationship is one in which **the board delegates responsibility for significant investment decisions** to a capable and trusted third-party advisor. • The **task of investment decision making shifts** from the board to the advisor. • The third-party advisor acts in a **fiduciary capacity**, avoiding conflicts of interest while assuming responsibility for executing its investment decisions while assuming a co-fiduciary role with the board. • The board now shares its financial responsibility with its investment manager — and more important, **the organization no longer bears its fiduciary risk alone**.

decisions are to be made not in isolation, but in the context of the entire investment portfolio and as a part of an overall investment strategy. Furthermore, this standard applies to the construction and ongoing management of a trust investment portfolio and not to the purchase, retention or sale of a particular security.

For qualified plans subject to the Employee Retirement Income Security Act of 1974 (ERISA) there are two fiduciary investment definitions:

- **Investment advisor —** ERISA section 3(21): Any firm or individual that provides investment advice, including investment recommendations, for a fee to the plan sponsor.
- **Investment manager —** ERISA section 3(38): A bank, registered investment advisor or insurance company that has sole responsibility for the investment of plan assets.

Due to confusion over the term "fiduciary" and the context in which it's being used, the board should understand the fiduciary role and standard of care that governs each investment advisor. In addition, the board should focus on the governance process used by each investment advisor to monitor and comply with their standard of care and regulatory requirements. This includes the internal oversight committee structure, audit procedures, risk and compliance manual, investment portfolio monitoring tools and risk management processes.

CONSIDERATIONS IN SELECTING AN OCIO

Engaging with an OCIO and shifting from a "management" role to a "leadership" role can be challenging for boards and investment committees. The creation, implementation and monitoring of a sophisticated investment program in the context of this "new reality" of challenging market environments depends upon employing a firm that has substantial investment management resources.

We recommend organizations follow a three-phased approach:

1. Assessment of current investment process
2. Evaluation of key attributes of investment managers
3. Implementation and transition to an OCIO model

This approach allows the board or investment committee to develop buying criteria that align with their most important needs when selecting an investment manager, resulting in easier evaluation of advisors and a quicker decision-making process.

ASSESSMENT OF CURRENT INVESTMENT PROCESS

The investment committee's strength is based on their expertise and decision-making process. Individuals possessing the appropriate knowledge, experience and skill to develop a strong investment process can deliver an investment portfolio that meets the goals of the organization. A consistent investment process can also help mitigate potential irrational outcomes that can be produced by a group committee structure.

A typical investment process follows these basic steps:

1. Identification of goals
2. Determination of return and risk levels
3. Strategic and tactical asset allocation
4. Selection of investment solutions for each asset class
5. Ongoing monitoring and rebalancing

The key document for guiding fiduciaries through the investment process is the organization's Investment Policy Statement (IPS). The IPS should be reviewed annually to ensure that it continues to reflect the goals determined by the investment committee. An assessment of the investment process will seek to identify gaps between the policy and the process. These may not always be apparent, but a self-audit will help focus on areas of strength or weakness and lay a foundation for the attributes that the organization will look for in an investment manager. In fact, a due diligence exercise on your own investment process should be similar to the process you would use to select a manager.

In simple terms you need to ask yourself the following question: “Would we hire ourselves as an investment manager?”

Typically, the following components would be analyzed:

ORGANIZATION

- Corporate and governance structure
- Alignment of roles and responsibilities

PHILOSOPHY

- Investment beliefs and strategy
- Clarity of risk/return dynamics

PEOPLE

- Key decision makers and experience
- Stability of investment committee

PROCESS

- Clarity of process
- Types of analytics and research used
- Communication routines within team

INVESTMENT PORTFOLIO

- Investment portfolio construction and risk management process
- Alignment of buy/sell decisions with process and philosophy

PRODUCT

- Alignment of investment vehicles with risk/return goals of investment portfolio
- Fees for the investment strategy
- Liquidity and cash management process

PERFORMANCE

- Consistency with investment process and risk levels

After this introspective look at your investment process you should be able to determine your board or investment committee’s strengths and weaknesses, and have a better understanding of what is important to your organization. The next step is to establish the level of input or control you want to maintain in the investment process. An OCIO relationship can range from a full OCIO model, where all investment authority is given to the investment manager, to a relationship where discretion is limited. The chart below shows the key decision points in the investment process and whether those are shared or outsourced.

KEY DECISION POINTS IN THE INVESTMENT PROCESS

	INVESTMENT COMMITTEE	OCIO
SPENDING POLICY DEVELOPMENT	Shared	
INVESTMENT POLICY DEVELOPMENT	Shared	
SET STRATEGIC ASSET ALLOCATION	Shared	
TACTICAL ASSET ALLOCATION		√
MANAGER SELECTION AND TERMINATION		√
INVESTMENT PORTFOLIO REBALANCING		√
INVESTMENT PORTFOLIO TRADING AND EXECUTION		√
PERFORMANCE MEASUREMENT AND REPORTING		√

Your assessment will help drive the level of control you would like to maintain. When searching for an investment manager, it’s important to be clear about the type of relationship and level of discretion you would like them to retain. Some providers may not be able to share discretion on certain investment decisions due to product limitations or regulatory restrictions. It’s important to determine the roles and responsibilities of each party in a discretionary relationship, document them in the investment policy statement, and ensure they are reviewed as the relationship develops. Although some of the investment decisions have been outsourced to an investment manager, the board of directors is still a fiduciary over the investment portfolio and the selection of the manager. The role of the investment committee will change from managing the investment portfolio to providing oversight and guidance to the investment manager, including any changes to the investment policy. As with hiring an investment manager for a single asset class, a clear set of evaluation metrics and monitoring routines should be established to track the OCIO's performance.

EVALUATION OF KEY ATTRIBUTES OF INVESTMENT MANAGERS

After completing your assessment you should have a clearer understanding of the specific needs of your organization and the level of outsourcing you require. The attributes you are looking for will form the buying criteria for selecting an investment manager as you evaluate the benefits of each provider. Investment managers that offer discretionary asset management provide a wide range of services and solutions in a variety of product vehicles. It's important to understand how these providers differ from each other and how they will manage your investment portfolio. Although we are focusing on investment management, there may be additional solutions and capabilities an OCIO could provide, such as administration, recordkeeping or strategic consulting. In the assessment of your current investment process, we already reviewed the standard due diligence factors that are typically used when evaluating asset management companies. For consistency we will look at each of these areas and highlight potential differences of investment managers.

Organization

Investment managers can be registered investment advisors, banks or trust companies. There are different fiduciary standards that apply to each of these types of entities, and the legal structure can also vary depending on the type of corporate entity or partnership they operate under. Each of these has different liability and financial structures. A fiduciary should be careful to ensure that the investment manager has a strong corporate and financial structure that can support any potential fiduciary liability. In addition, there should be clear governance structures providing oversight of the investment management process and compliance with all required regulatory rules. Some investment managers will use third-party service providers for key tasks such as administration, custody, trading and manager due diligence.

Philosophy

Each investment manager will have a clear and distinct value proposition describing the key elements of their firm or solution. These vary and will focus on different aspects of the investment process in serving institutional clients. This part of the selection process is heavily influenced by personalities and interactions. It's important that your investment manager wants your business and treats you accordingly, and that you both feel you're "on the same page." A shared philosophy can help to build a long-term relationship, even if the individuals change over time. More objectively, the ongoing client team and its structure will also vary by manager. Given that ongoing interactions will be primarily with the client team, it's important to meet and understand how you will work together.

People

In addition to a consistent and repeatable investment process, the strength of any organization is its people. This includes the senior leadership overseeing the investment strategy, process and culture, and the client-facing investment manager providing day-to-day investment portfolio management. These teams can be organized in different ways, including centralized investment portfolio management with client managers, or local investment portfolio managers supported by internal analysts. Whatever the structure, it's important to have a strong team with investment expertise so that the investment manager would not be compromised by the departure of a key investment professional. Compensation practices may also differ depending on the corporate and fiduciary structure of the investment manager, and these should align with the philosophy and goals of the client.

Process

A clearly defined and understandable investment process provides the basis for the value each investment manager adds to the investment portfolio. From the inception of an investment idea to its purchase within an investment portfolio, the investment process should guide its implementation. Investment managers leverage different forms of investment research and analytical software to evaluate and improve their investment portfolios. Some of these may be internal or proprietary versus purchased from a vendor. Communication routines are also important within the investment leadership team and the client-facing team, ensuring that the latest research and ideas are reaching client investment portfolios.

> A clearly defined and understandable investment process provides the basis for the value each investment manager adds to the investment portfolio.

Investment portfolio

A key differentiator between investment managers is the investment portfolio construction and risk management process. Since the Great Recession in 2008, when the benefits of asset class diversification were strongly tested, Modern Investment Portfolio Theory and traditional asset allocation strategies have been scrutinized, and new approaches focused on risk have been developed. These may involve decisions around the use of active management and its expected risks and benefits, as well as an understanding of the resources and fees necessary to execute and monitor the investment program. Additionally, the role of alternative investments—as well as liquidity and cash flow management in an investment portfolio—are key factors in the investment portfolio construction process. When evaluating each manager it's important that any purchase or sell decisions are aligned to their investment philosophy and process. There should also be governance processes established that actively monitor the investment portfolio against the investment policy statement to ensure the investment portfolio remains in compliance.

Product

Investment managers can implement investment portfolios using a wide range of investment vehicles. These can include pooled or commingled products that bundle investment assets in a single structure, or unbundled multi-manager/product solutions in a multiple-account structure. Liquidity and cash management processes will be affected by the products selected.

Investment pricing can vary from a single-fee method to à la carte for each service, such as investment advice, product fees, custody, trading, etc. An investment manager may also charge performance-based fees on your investment portfolio. Individual investment product fees may be pre-negotiated by the investment manager, or you may be required to contract with the investment product's manager directly. Due to the various pricing methodologies and investment product costs, it is important to view fees at the total investment portfolio level. This will ensure an even comparison across investment managers.

Performance

Investment performance can be challenging to evaluate if the investment manager does not use pooled or commingled investment solutions. Investment managers who offer unbundled multi-manager solutions may not have performance composites due to the customization requirements of each client. However, performance and attribution should be consistent with the investment process and reviewed on a risk-adjusted basis. The performance should also align to the team responsible for the investment decisions made in the investment portfolio.

Selecting an investment manager may seem like a long and complex process, but it doesn't have to be. An organization that knows what it wants to buy can quickly make a purchase decision. As with any purchase, it's about finding the right fit, design and price for the product you are looking for. The more time focused on the assessment phase, the quicker the evaluation phase.

> Selecting an investment manager may seem like a long and complex process, but it doesn't have to be.

TRANSITION TO AN OCIO

Outsourcing your investment portfolio to an OCIO may affect both the investment portfolio and the relationship between the investment committee and the investment advisor. Depending upon the level of discretion you have delegated, these impacts can be significant. In an advisory or consulting relationship, the investment committee maintains the relationship with all the service providers to the investment portfolio. This can include the investment consultant, investment managers and the custodian. The number of service providers and complexity increase if there are restricted assets or multiple pools of assets that need to be managed. An OCIO can simplify this process, but in order to transition to their model, an investment portfolio may need to go through a complete change in investments and service providers. This will depend upon the product solution the investment manager offers, such as a pooled or unbundled product. You may be required to change custodians, terminate investment manager agreements and notify other providers involved in the investment portfolio. This transition can be complicated by illiquid assets such as hedge funds and private equity investments that may not be able to be transferred on a timely basis.

A complete change of investment portfolio may seem unnecessary, but outsourcing your investment portfolio means you have shared fiduciary responsibility with the investment manager. As a fiduciary, the investment manager will manage the investment portfolio based upon their investment process, including their approved investment solutions. It may be possible to retain the investment portfolio's existing investment solutions, but this should not be expected. Replacing investment solutions can be challenging to the investment committee that selected and forged relationships with these individual managers. However, replacing the existing investment solutions is not a reflection of the decision-making ability of the investment committee, but rather a change in the investment process. The new investment manager will develop a new investment portfolio based on their skill and experience, and they should be allowed to do this without any restrictions so that they may implement their best ideas. After all, this is why you chose them.

The role of the investment committee has changed from management to leadership, overseeing and monitoring the investment portfolio and investment manager. This shift in responsibility allows for a broader discussion of the current market environment and strategic changes to the investment portfolio that leverage the expertise and experience of the members of the investment committee more effectively. Investment thought leadership on capital markets, macroeconomic strategy and key investment topics provided by the investment manager will help keep the investment committee aligned with tactical decisions made in the investment portfolio. A successful relationship with an investment manager should be between the two organizations. As the "OCIO," the investment manager needs to work closely with the investment committee and be aware of any strategic changes that may affect the goals of the investment portfolio. This could include any financial or balance sheet concerns, benefit changes or new initiatives.

A CRITICAL DECISION

Boards of directors, investment committees and corporate staff from the endowment, foundation and pension communities are all facing new hurdles as leaders of their organizations. Increased legislative and statutory requirements, leaner staff, higher standards of accountability and lower sources of funding all contribute to a more challenging operating environment. Additional challenges include an expectation of lower investment returns, higher investment risk, increased complexity and a greater dependence on the investment portfolio as a source of funding for the mission of these organizations. Many organizations are considering outsourcing to investment managers who can provide the knowledge, expertise and resources required to develop and manage the sophisticated investment portfolio needed to meet these challenges going forward. By outsourcing the investment function, organization leaders can devote themselves wholeheartedly to those critical responsibilities and activities that allow them to make their greatest contribution to their organizations. In doing so, they can address their primary responsibility of meeting the needs of the investment portfolio's beneficiaries, preserving and enhancing the reputation of their organization, providing governance and oversight, and being the best fiduciaries they can be.

Selecting an OCIO is a critical decision that requires a thorough review of both the current investment process and the potential investment manager. Identifying the appropriate relationship is a key first step, as there are significant differences between advisory and discretionary relationships and the fiduciary standards investment managers may follow. But key to selecting an OCIO is the investment process that they follow. A consistent and repeatable investment process, aligned to the goals of the organization and delivered by an experienced investment portfolio management team, can provide fiduciaries with a strong relationship to help carry out their responsibilities. Given the complexity and scope of responsibility involved, it is essential that the board feels confident about delegating this series of tasks to the OCIO. The board must feel that the firm can develop and execute tasks effectively while using a holistic and goals-based approach. Additionally, the OCIO must be able to establish a relationship with the board that facilitates understanding of the goals and risk tolerances of the organization, and demonstrates how the investment program is helping the organization meet its goals.

LEARN MORE

We have provided a guide to the OCIO consideration and selection process, and we welcome the opportunity to discuss this further with you. For more information, please contact your U.S. Trust, Bank of America representative or **email institutional_investments@ustrust.com**.

[1] June 2014 NCSE (NACUBO/Commonfund Study of Endowments).

[2] 2011 Neuberger Berman Chief Investment Officer Outsourcing brochure and U.S. Trust.