Nonprofit Management Research Panel

Poll: Investment Governance Practices for Nonprofits

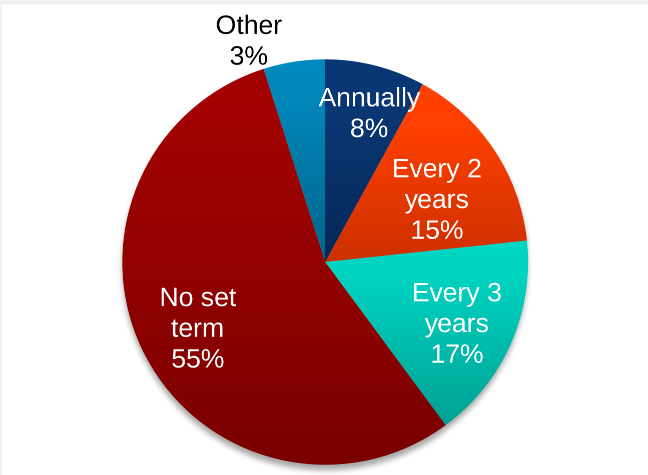
In September 2013, the Nonprofit Management Research Panel conducted a survey to learn more about current investment governance practices for U.S. nonprofit organizations. Additionally, participants were asked to provide their single biggest challenge when it comes to effective investment governance policies. Finance staff, board members and investment committee members participated in the survey, representing 165 U.S. foundations and endowments, and $16.4 billion in combined assets. Investment portfolios ranged in size from $15 million to $2.2 billion in assets. None of the participating organizations are institutional clients of SEI. Below is a summary of the key findings.

Who is primarily responsible for managing the investment portfolio?

According to the poll, the majority (76%) of nonprofit portfolios are governed by an investment committee that meets, on average, about **four times** per year. Additionally, 41% of participating organizations reported using an investment consultant, and 18% use an investment outsourcing partner. About one-quarter (23%) of organizations also reported having full-time internal investment staff; however, the average size of such staffs equates to **less than one** person.

Our biggest challenge is "combining professionals with different mindsets and experience levels to cohesively decide on what is best for the long-term viability of the foundation's endowment, without personal philosophy or short-term reactionary natures coming into play."

Investment Chair Term Limits



Participants reported an average committee size of **seven** people, with an average of only **three** committee members having professional investment experience. Of those organizations with an investment committee, a little more than half (55%) reported having no set term limit for the committee chair, and 23% reported a turnover of committee chairs annually or biennially. Some committees might be challenged by more frequent committee chair turnover, as a regular change in leadership could impact the establishment of a consistent long-term investment philosophy and strategy for the portfolio.

What formal investment governance policies are in place?

Not surprisingly, almost all participating organizations (98%) reported having a formal Investment Policy Statement (IPS) that defines asset allocation, rebalancing, goals and performance metrics for the portfolio. Likewise, almost all (97%) said they have a formal Conflict of Interest Policy that is consistent with guidelines set forth by the Internal Revenue Service.

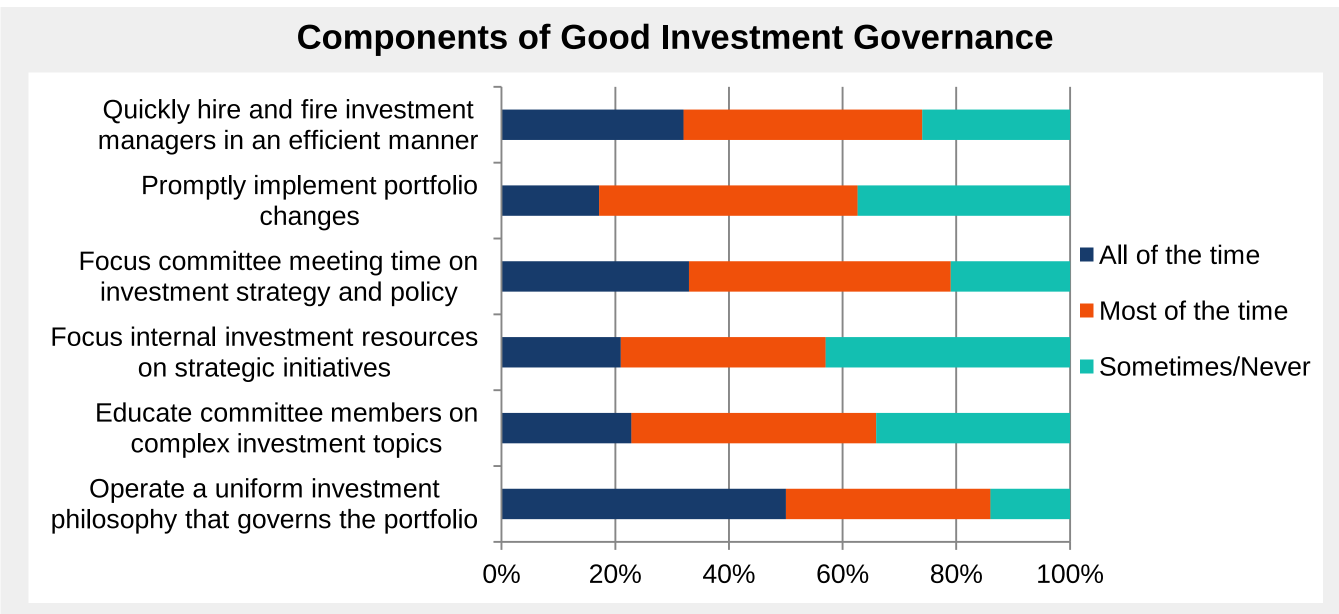
Formal Spending Policies have grown in popularity over the past few years as a result of the impact that tumultuous markets and investment losses have had on nonprofit spending. While the majority of organizations (86%) have a spending policy in place, 14% reported a lack of any document to clearly outline spending needs and goals in support of the IPS. According to a Spring 2013 poll on spending, 36% of nonprofits haven't reviewed or made a change to their spending policies in more than five years.[i]

> ***Our biggest challenge is "balancing the schools of thought that relate to optimal asset appreciation, our spending rate, and the carrying out of our organizational mission."***

An Investment Committee Charter can be another useful governance tool, which defines roles, responsibilities and term limits for the committee. About two-thirds of respondents said their committee has an Investment Committee Charter, 30% said they do not have a charter; and 3% were unsure.

What are the metrics for a successful investment governance process?

Participants were asked to identify their organization's ability to consistently meet a given set of criteria in fulfilling their investment governance oversight:



1. **Quickly hire and fire managers in an efficient manner**
   The ability to nimbly replace a poorly performing manager can greatly impact portfolio performance. More than two-thirds (68%) of poll participants said their organizations are unable to make timely and efficient manager changes **all** of the time. For nearly half (49%) of participating organizations, it takes anywhere from **three months to more than a year** to fire a manager. This can greatly impact portfolio returns and spending, as the under-performing manager continues to manage the organization's assets during that time.

> ***Our biggest challenge is "finding time to identify and screen new investment managers. Good ideas often take too long to implement."***

The process to *search and hire* a replacement manager can also be challenging for many nonprofits, but according to the survey results, it takes less time to hire a manager than it does to fire one. For those using an investment consultant, more than one-third (39%) of participants said it takes anywhere from **three months to more than a year** to hire a manager. In contrast, almost all (87%) of participating organizations that are currently using an investment outsourcing provider reported being able to hire a new manager in **less than three months**.

Despite these challenges to nimbly execute manager-change decisions, 97% of participants felt that their average quarterly committee meetings occurred frequently enough to accomplish their goals.

2. Promptly implement portfolio changes

Only 17% of participants said their organizations are able to quickly make asset allocation changes that take advantage of market opportunities **all** of the time. Liquidity restrictions on certain investment vehicles, as well as hesitation by the committee to reach a decision on a new allocation strategy, might hinder nimble portfolio changes. About half (45%) of participants said they are able to accomplish this task **most** of the time.

> ***Our biggest challenge is "educating committee members on various alternative asset types, to a point where they are comfortable investing in them."***

About half (48%) of organizations said it takes **three months to more than one year** to reach a collective decision on an allocation change to the investment portfolio. Once a portfolio change is finally agreed upon, it takes three-quarters of organizations less than three months to implement it. **All** of the participating organizations currently using an investment outsourcing provider reported being able to make an asset allocation change in **less than three months**.

3. Focus committee time and internal resources on strategic investment initiatives

> ***Our biggest challenge is "keeping the attention of the investment committee focused on strategic issues, rather than tactical ones."***

Meeting once per quarter, on average, makes committee member time particularly valuable for nonprofits. However, two-thirds of participants (67%) felt their organizations are unable to focus committee meetings on strategic investment priorities **all** of the time, without being distracted by more tactical issues. Additionally, 79% of organizations said their internal investment resources face challenges around always focusing time and attention on strategic initiatives.

4. Educate committee members on complex investment topics

Keeping investment committee members well-informed about market fluctuations, complex investment vehicles, new spending methodologies and changing regulations is difficult, particularly for committees that may lack investment expertise and meet just a few times each year. More than three-quarters of participating organizations (77%) said their organizations lack the ability to keep members up-to-date on these topics on a regular basis.

Committee education was a common hurdle voiced by many poll participants, some of whom said their biggest challenges include "keeping investment committee members educated and current with information," "compliance with ever-changing regulations,""creating a continuing education process," and "getting new committee members up to speed."

5. **Operate a uniform investment philosophy that governs the portfolio**
   While most nonprofits have an IPS to govern the investment management of the portfolio, committees are often comprised of members with varying investment knowledge and strong personal philosophies about risk. Despite these differences, it's important that the committee act in unison in the best interest of the portfolio, and 88% of poll respondents said they are able to accomplish this **all** or **most** of the time.

Our biggest challenge is "separating personal financial feelings from the fiduciary requirements necessary to govern a foundation."

Conclusion

Those tasked with the responsibility to grow and perpetuate a nonprofit organization's investments face many challenges, including a decade of volatile markets, limited meeting time, restricted resources and conflicting investment philosophies. Many nonprofit organizations have implemented investment governance best practices, such as an Investment Policy Statement and a Formal Spending Policy, to help them stay on track towards achieving their goals. Having well-defined processes can help streamline decision-making and create a uniform investment strategy, which are needed to execute important portfolio changes in a timely and nimble manner.

According to the survey, 59% of participating nonprofit organizations currently use an outside partner, in the form of a traditional consultant or an investment outsourcing provider, to assist in the investment governance of the portfolio. Additionally, 36% of respondents who do not currently use an outsourcing provider said they would consider using one in the future. An outsourcing provider can be a crucial partner in the investment governance strategy for a nonprofit, providing timely manager and asset allocation changes, assistance in creating an effective investment policy statement, access to committee education materials, and comprehensive reporting towards goals.

NONPROFIT MANAGEMENT
Research Panel

The Nonprofit Management Research Panel, sponsored by SEI's Institutional Group, conducts industry research in an effort to provide members with current best practices and strategies for the investment management of nonprofit foundations and endowments.

*For comments or questions, please contact SEI at SEIresearch@seic.com or **1-866-680-8027**.*

[i] The Current Landscape of Nonprofit Spending: Methodologies & Investment Strategies for Foundations & Endowments. SEI 2013: http://www.seic.com/docs/Institutions/SEI-FNP-WP-Current-Landscape-Nonprofit-Spending-June-13.pdf.

