

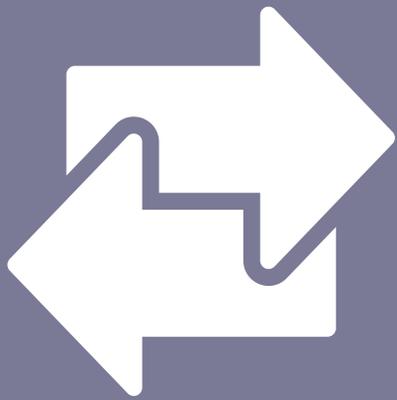
# OCIO.ORG: *The "Toolkit" Workbook*

**O**cio.org is dedicated to advancing Outsourced Chief Investment Officer services through education, advocacy and insight. We offer this collection of presentations or "toolkits" on key topics as a resource for institutional investment committees, business leaders and industry professionals interested in the OCIO business model and best practices.









# STATUS QUO OR OCIO?

Answer the questions below. A score of 50 or higher indicates that OCIO could be an effective solution for your organization.

## Governance



The investment committee understands its fiduciary responsibilities and has time to educate itself on evolving standards specific to the organization's investment purpose (e.g., pension, endowment, foundation, healthcare).

N/A 1 2 3 4 5

The roles of investment committee members and other internal staff are clearly defined. Investment committee meetings are well organized and attended.

N/A 1 2 3 4 5

The investment committee spends most of its time on high-level strategic objectives (risk tolerance and long-term investment goals) and little to no time on the day-to-day management of the portfolio.

N/A 1 2 3 4 5

The investment committee has sufficient financial expertise (either directly or with the help of internal staff or third parties) to select risk-appropriate asset classes and allocation targets/parameters.

N/A 1 2 3 4 5

The investment committee is comfortable and effective in communicating its investment approach and the status of the portfolio to key constituents (e.g., Board of Directors, senior management, outside donors).

N/A 1 2 3 4 5

## Portfolio Construction



The investment committee/organization has sufficient time and expertise to evaluate a wide range of managers and vehicles.

N/A 1 2 3 4 5

If the investment committee receives assistance from third-party advisers (e.g., consultants):

The investment committee is capable of translating advice received from one or more advisers into a comprehensive portfolio.

N/A 1 2 3 4 5

Those advisers have an “open architecture” approach to the selection of managers/vehicles (and do not have financial incentives to recommend specific managers/vehicles to the investment committee).

N/A 1 2 3 4 5

The investment committee wants to make all investment decisions for the portfolio.

N/A 1 2 3 4 5

There is a centralized and disciplined process for making investment decisions.

N/A 1 2 3 4 5

## Implementation



The investment committee has delegated the day-to-day implementation of investment decisions (hiring, firing and monitoring managers/vehicles) either to internal staff or to third parties.

N/A 1 2 3 4 5

If not, the investment committee has sufficient expertise (either directly or with the help of internal staff or third parties) to hire, monitor and fire managers and other parties (e.g., broker, custodians).

N/A 1 2 3 4 5

If appropriate, the investment committee has access to alternative investments (e.g., private equity, hedge funds) for the portfolio.

N/A 1 2 3 4 5

## Risk Management

The investment committee has the ability (either directly or with the help of internal staff or third parties) to:

Conduct due diligence reviews on managers/vehicles (i.e., review and monitoring of corporate governance, operational processes and accounting controls of managers and vehicles).

Review, negotiate and execute the legal documentation required for portfolio investments.

Make tactical changes to the portfolio in response to unexpected market opportunities and challenges.

←————→  
Agree                      Disagree

N/A 1 2 3 4 5

N/A 1 2 3 4 5

N/A 1 2 3 4 5

## Performance

The organization has been pleased with the performance of the investment portfolio over most periods.

←————→  
Agree                      Disagree

N/A 1 2 3 4 5

## Back Office

The investment committee receives full portfolio and performance reporting including data aggregation and attribution analysis.

The finance department has sufficient information regarding the portfolio to respond to audit requests.

The investment committee has support dealing with custodian and prime brokers.

←————→  
Agree                      Disagree

N/A 1 2 3 4 5

N/A 1 2 3 4 5

N/A 1 2 3 4 5

## Talent

If the investment committee relies on an internal CIO/investment office:

The investment office can attract/afford to hire top talent.

There is a deep pool of investment office staff to cushion unexpected departures or to manage succession.



Agree

Disagree

N/A 1 2 3 4 5

N/A 1 2 3 4 5

## Cost

The overall resources available to the investment committee are adequate and within the organization's budget.

The cost of OCIO would be significantly higher than the cost of obtaining similar resources through various internal and external providers.



Agree

Disagree

N/A 1 2 3 4 5

N/A 1 2 3 4 5



# OCIO IMPLEMENTATION SYSTEMS

*A sliding scale of customization and cost.*



## SINGLE PORTFOLIO

- "One -size-fits-all"; no/low customization approach
- OCIO invests the client's assets in a single commingled vehicle with a fixed asset allocation
- All clients with the same risk profile invest in the same fund
- Better for smaller investors: economies of scale for administrative costs and negotiation strength
- Limited to specific strategies
- Investments not portable

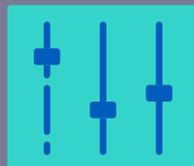


## HYBRID

- More asset allocation flexibility
- OCIO offers one or more commingled vehicles with the ability to vary asset allocation through the use of different underlying "series" or "sleeves"
- Investments have limited portability

## COMBINATION

Choose different systems by asset class (e.g., single portfolio for alternatives, fully customized for traditional)



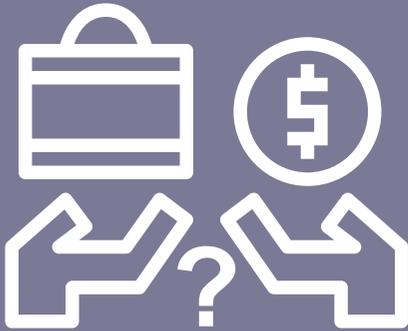
## FULLY CUSTOMIZED

- Closest to in-house CIO: maximum discretion/flexibility within investment guidelines for asset allocation and manager selection
- Portable: client invests directly with external managers/owns underlying investments (rather than a share of pooled vehicles)
- Greatest transparency
- Not practical for smaller investors: higher accounting, custody, operational costs.



# LEGACY ASSETS

It's important to understand how an OCIO will handle the organization's existing investments.



## MARKETABLE

Keep or sell?  
Review carefully!

- Communicate organization's preferences, if any, on retaining particular investments.
- Will the OCIO sell all existing investments, or will it carefully consider whether any fit its strategy requirements?
- For assets that will be sold, how will the OCIO minimize transaction costs and avoid "fire sale" losses?



## ILLIQUID

Don't "orphan" these investments.

- *Fund-of-Funds* - continued reporting
- *Hedge Funds* - ongoing manager due diligence, secondary sales opportunities, timed redemption
- *Private Equity/Real Estate* - ongoing manager due diligence, secondary sales opportunities, capital calls, distributions, voting, side letter compliance, blocker elections



## FEEES

There is no free lunch.

- *No Fee?* Don't expect much.
- *Discounted Fee* – Assets managed at a discount to OCIO's percentage of AUM rate.
- *Full Charge* – OCIO includes legacy assets in overall AUM fee calculation.
- *Fund-of-Funds Fee* – In the case of illiquid fund-of-fund investments, the OCIO charges a flat fee per fund.



# OCIO FEE TEMPLATE



How much does the OCIO really cost?

Variations in OCIO business models and a lack of disclosure standards can make it difficult to assess and compare fees of different providers.

This template helps give a more nuanced view of how a bidding OCIO intends to slice and dice the plan sponsor's assets, and the costs involved.

Note: "Yes" answers in Column L indicate the bidder is not a true OCIO.

A	B		C	D	E	F	G	H	I	J	K	L	M
	Provide Asset Allocation(%)		OCIO Fee	Fund of Fund Fees	Admin. Expenses of Fund of Funds	**Underlying Manager Fees (SMA and Fund)	Fees Plus Fund of Funds Admin. Expenses at Current Allocation	Fees Plus Fund of Funds Admin. Expenses at Proposed Allocation	% Actively Managed Proposed	% Passively Managed Proposed	Disclosure of Affiliated Broker, Custodian, Fund Administrator, or other services fees provided by bidder	% Proprietary Assumed Used for Proposed	
	Current	Proposed									Y/N		
Asset Class*	0.0%+	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Yes, we earn additional fees from _____ Or None.	0.0%
Total	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

**Column A:** Add a row for your current allocation to each asset class (e.g., US Equities-Large Cap; US-Equities-Small Cap; Developed Market Equities; Emerging Market Equities; Frontier Market Equities; Fixed Income; Hedge Funds; Real Estate; Private Equities; Commodities) . If you are not currently using an OCIO provider, ask the bidding OCIO enter its proposed asset classes.)

**Column B:** Enter your current allocation, or zero if not currently using an OCIO provider,

**Column C:** Bidding OCIO to enter its proposed allocations for each asset class.

**Column D:** Some OCIOs charge a flat fee for different asset classes and different implementations of exposure (active or passive). Bidding OCIO to enter fees.

**Columns E, F & G:** Bidding OCIO to input the total fees (if applicable) for fund of fund products, administration expenses and underlying manager fees.

**Columns H & I :** Bidding OCIO to input H. Shows the total fees payable by an asset owner for the proposed implementation of exposure – as a percentage of the plan's assets - to the respective asset classes,. If you are bidding out an existing OCIO mandate, complete I to compare the fees payable under your existing agreement.

**Columns J & K:** Bidding OCIO to enter its proposed allocation to active and passive management.

**Column L:** Bidding OCIO to complete. **This column assumes conflicted fee arrangements that are not OCIO. A bidder that answers "yes" is not a true OCIO.**

**Column M:** Bidding OCIO to enter the amount of proprietary product that they propose to use in implementing their plan, how much is active vs passive (if you see 50bps in column D for a 100% passive exposure, you should be asking why) and whether the bidding firm receives additional fees from other departments within the organization.



# OCIO PERFORMANCE REPORTING

Although there are no required performance presentation standards in the OCIO industry, an OCIO performance report ideally will:

## present actual returns . . .

Hypothetical or backtested returns should be offered only in addition to actual returns and should be clearly marked.

## for all clients . . .

All clients should be included in at least one appropriate composite to avoid cherry-picking concerns.

## that are net of all fees . . .

Including all investment manager fees, fund-of-fund fees, as well as custody, administrative and legal expenses.

## and include both total return and specific asset class composites . . .

To show the value added/detracted by portfolio-level decisions and assess the risk levels behind the returns.

## compared against appropriate benchmarks . . .

Benchmarks should be widely accepted industry standards and comparable to composite characteristics.

## while excluding non-discretionary accounts and legacy investments.

That do not reflect the OCIO's performance.



### Encourage GIPS®

A small, but growing number of OCIOs already adhere to the CFA Institute Global Investment Performance Standards ("GIPS"). GIPS reduces misleading practices and helps level the performance playing field .





# BEFORE THE OCIO SEARCH: HIT PAUSE

First, figure out what your organization needs in an OCIO.



**Check the "whether."** Convene a meeting of key stakeholders and discuss:

- whether there are any anticipated **directional changes or adjustments** to the organization that could affect enterprise risk or the investment portfolio;
- whether there are any near-term **expected inflows** or **pending commitments/liabilities**; and
- whether there is **interest in values-based investing** (e.g., DEI, ESG), if appropriate.



**Identify any issues.** How well is the portfolio achieving its purpose and what needs improvement? Ask if internal teams (e.g., accounting) need additional support.



**OCIO or bust?** Decide whether to limit the search to true OCIO (with fiduciary responsibility, discretion/accountability and independence) or include other outsourced providers that don't offer the same benefits and may have conflicts of interest.



**Investment philosophy.** Make sure the investment committee is clear on its investment philosophy. An OCIO match in investment philosophy is critical.



**"Most Wanted" list.** Which OCIO features or services are most important to the organization? Create a list of three to five "must have" features such as:

- governance and fiduciary support
- experience with similar clients
- alternative investment capabilities
- open architecture manager selection (a "built-in" feature of true OCIO)
- service ethic, firm size/number of clients



**Control.** Determine how much control the investment committee is comfortable delegating. Be reasonable: if the investment committee won't delegate the "meat" of decision-making, it may need to "order chicken" instead.



# HIRING AN OCIO SEARCH CONSULTANT



## Should your organization hire an OCIO search consultant?

Ask the question:

Does the investment committee have the time and expertise to identify the best OCIO providers in the marketplace, conduct extensive due diligence to determine which one is best for the organization, and then negotiate the terms of the arrangement?

*If the answer is "no," consider hiring a search consultant.*

## Look for a consultant that is ...

**Independent.** Check to see whether the search consultant has any ties to outsourcing providers or other financial services firms.

**Experienced.** Explore the history of the firm and check the credentials of the professionals that will be working with you.

**Successful.** Call references. It's not enough for a consultant just to close a search. Ask how long the referring organization has been partnered with its OCIO and if the "marriage" is a happy one.

## What to ask the candidates:



- Provide a brief history of your firm. When was it founded and by whom?
- What is the current ownership structure of the firm?
- Provide biographies of the professionals that will be assigned to our search if we hire you.
- Are OCIO searches your only or main business?
- Do you also provide OCIO or any other type of financial services?
- Do you have any affiliations or financial arrangements with any OCIO providers or other financial services firms?
- How many searches have you performed in the last year? List the types of clients and asset sizes involved.
- Provide three references similar to our organization.
- Outline the elements of your typical search process and a timeline.
- What do you feel are your firm's strengths and limitations?





# DRAFTING AN OCIO RFI/RFP



What's the difference between an RFI and an RFP?

## Request for Information

- Purpose: *eliminate* unsuitable candidates
- Goal: used to *identify* a first round of candidates or "semi-finalists" who will receive an RFP
- Optional: More common in *self-directed institutional searches* in lieu of consultant database
- No. of Recipients: **10-15** potential candidates
- No. of Questions: **5-10** questions directed at organization's "must have" characteristics and services

vs.

## Request for Proposal

- Purpose: *illuminate* promising candidates
- Goal: used to *compare* "semi-finalists" and select "finalists"
- Required: integral to *both self-directed and consultant-led searches*
- No. of Recipients: **4-8** (selected from consultant database or through RFI)
- No. of Questions: **25-50** questions directed at all key characteristics and services





# 10 KEY DECISION POINTS

An OCIO relationship is like a marriage: Be clear on these 10 points before saying "I do."

## PHILOSOPHY

Are there commonalities in the thinking of the candidate and the investment committee?

Does the candidate enhance the investment committee's views on investment policy?

## ROLES

What will be the candidate's roles and responsibilities in the relationship?

Is there flexibility on important areas?

## IMPLEMENTATION

How will the candidate implement the organization's account (i.e., single fund, hybrid, customized separate account, combination)?

What will happen with legacy investments?

## ENTERPRISE RISK

Does the candidate take an enterprise view of the organization and the investment portfolio?

## ASSET ALLOCATION

Does the candidate's asset allocation proposal make sense?

Are the candidate's assumptions overly aggressive or conservative?

How does the candidate handle access to capacity-constrained managers?

Do all clients get *pro rata* access, or are some clients favored?

What other services does the candidate provide, and how will it become part of our team?

Which professionals will the investment committee work with, and will they commit to attend meetings?

Will the candidate specify the members of the team and their commitment in the contract?

Does the board understand all the ways the candidate will get paid?

How deep is the team?

Does the candidate have a succession plan and a structure designed to ensure it will be able to provide services for at least 10 years?

## ACCESS

## OVERALL SUPPORT

## TEAM

## CONFLICTS

## DEDICATION TO OCIO







# OCIO TRANSITION PROCESS

*A smooth "hand-off" requires communication and cooperation.*

## DOCUMENT RELATIONSHIP 30 Days



"GO LIVE"

### ORGANIZATION

- Negotiate/execute IMA
- Give OCIO governing, KYC, and tax documents
- Direct existing managers and custodian to accept OCIO access/authority

### OCIO

- Negotiate/execute IMA
- Link with existing managers and custodian
- Give organization access to OCIO "portal" for position/performance information

## CONSIDER PROVIDER "OVERLAP"

## TRANSFER EXISTING PORTFOLIO 60 Days



### OCIO

- Assume authority and fiduciary responsibility over existing portfolio
- Interact directly with custodian and existing managers

## REVISE IPS 30 Days

### OCIO

- Collaborate on Investment Policy Statement (IPS)
- Develop detailed transition plan

## DEVELOP TRANSITION PLAN 30 Days

### ORGANIZATION

- Collaborate on IPS and transition plan
- Review and approve IPS and transition plan

## IMPLEMENT NEW POLICY 30 - 60 Days



### OCIO

- Implement transition details
- Execute new manager agreements/investment subscription documents
- Transmit instructions to new managers and custodian
- Provide a comprehensive transition review to the investment committee

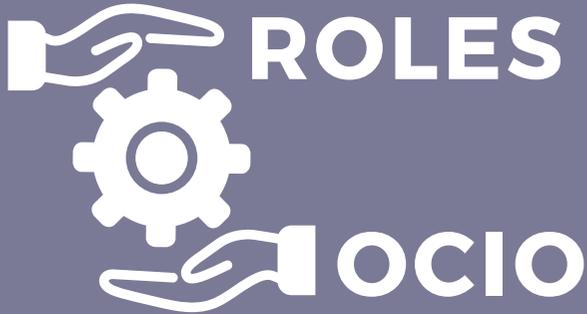
## START OCIO "PERFORMANCE CLOCK"







# IC ROLES AND RESPONSIBILITIES



*Starting with the transition process and continuing through the relationship, certain responsibilities of the investment committee will shift to the OCIO.*

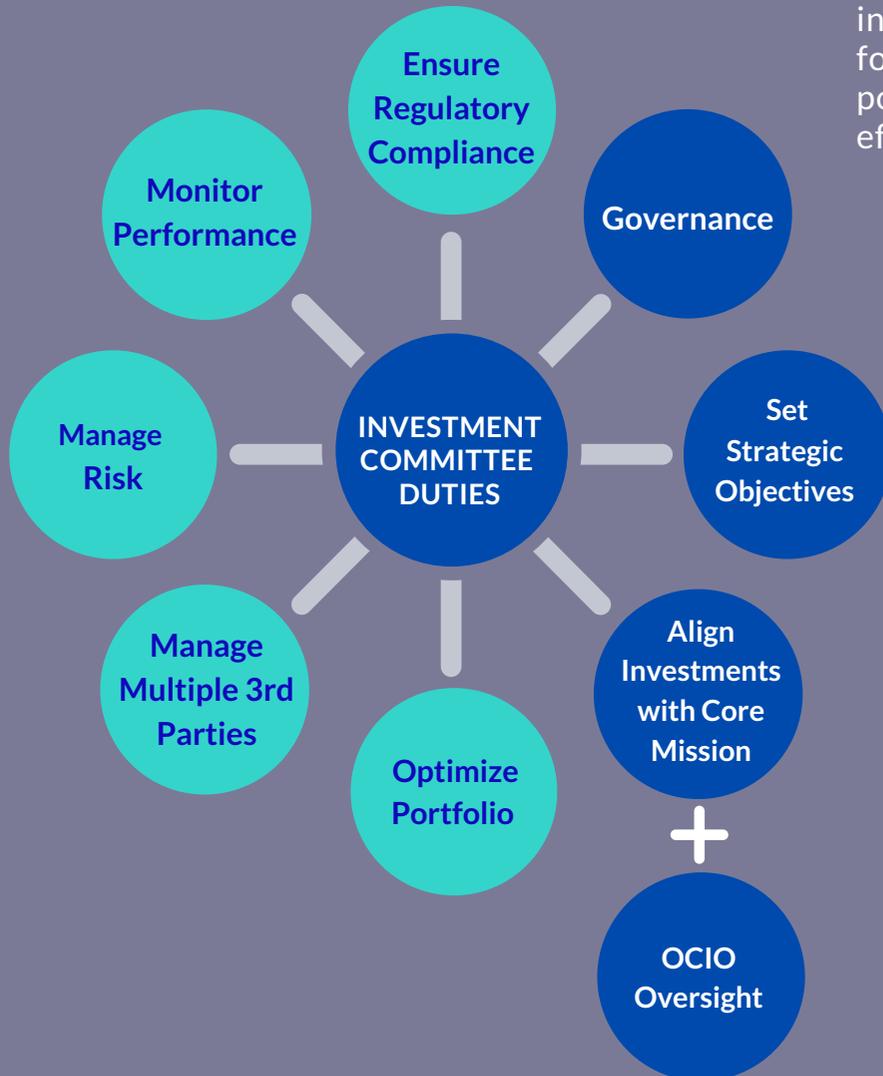
ACTION	DEVELOP/ INITIATE	APPROVE	IMPLEMENT	OVERSEE
Select and review OCIO	Client	Client	Client	Client
Determine investment objectives, risk tolerance, and liquidity needs	OCIO & Client	Client	OCIO	Client
Determine investment policy	OCIO & Client	Client	OCIO	Client
Determine permitted asset classes, asset allocation, allowable ranges, distribution needs	OCIO & Client	Client	OCIO	Client
Custodian selection and interaction	OCIO & Client	Client	OCIO & Client	OCIO & Client
Manager selection, monitoring, termination, and associated transition activity	OCIO	OCIO	OCIO	OCIO & Client
Portfolio tilts due to valuation anomalies or opportunities	OCIO	OCIO	OCIO	OCIO & Client
Communication with client constituents	—	—	OCIO & Client	—



# AFTER THE TRANSITION: THE INVESTMENT COMMITTEE

*Congratulations! You have hired an OCIO and completed the transition process. What should the investment committee do now?*

OCIO LIFTS



in a typical OCIO partnership, the OCIO assumes responsibility for the day-to-day tasks involved in managing the organization's portfolio. Ideally, the investment committee will refocus its efforts on the remaining, higher-level duties, namely, to:

- establish and *maintain a sound governance structure* for the committee;
- periodically *review the financial condition of the organization and* confirm that the *strategic (risk/reward) objectives* for the investment portfolio are in *alignment* with and sufficient to support the organization's core mission; and
- *monitor* the performance of the OCIO.

IC RE-  
FOCUSES



# WHAT'S ON THE AGENDA?



*A suggested one-year meeting framework to address the responsibilities of an investment committees that works with an OCIO.*

	PORTFOLIO REVIEW	MARKETS & ASSET CLASS REVIEW	MISSION ALIGNMENT	GOVERNANCE MATTERS
Q1	<ul style="list-style-type: none"> <li>• Performance</li> <li>• IPS Adherence</li> <li>• Benchmark Review</li> </ul>	<ul style="list-style-type: none"> <li>• Market Update/ Outlook</li> <li>• Focus: Fixed Income</li> </ul>	<ul style="list-style-type: none"> <li>• Liquidity Profile</li> <li>• Spending/Distribution Policy</li> </ul>	<ul style="list-style-type: none"> <li>• Minutes</li> <li>• Review IPS , Charter and IC Succession Plan</li> </ul>
Q2	<ul style="list-style-type: none"> <li>• Performance</li> <li>• IPS Adherence</li> <li>• Portfolio Risk Analysis &amp; Stress Testing</li> </ul>	<ul style="list-style-type: none"> <li>• Market Update/Outlook</li> <li>• Focus: Hedge Funds</li> </ul>	<ul style="list-style-type: none"> <li>• Enterprise Risk Assessment</li> <li>• Risk Profile</li> </ul>	<ul style="list-style-type: none"> <li>• Minutes</li> <li>• IC Education</li> <li>• Review Applicable Laws</li> <li>• Report to BoD</li> </ul>
Q3	<ul style="list-style-type: none"> <li>• Performance</li> <li>• IPS Adherence</li> <li>• Values-Based Investing Analysis</li> </ul>	<ul style="list-style-type: none"> <li>• Market Update/Outlook</li> <li>• Focus: Private Equity and Real Estate</li> </ul>	<ul style="list-style-type: none"> <li>• Treasurer's Report</li> </ul>	<ul style="list-style-type: none"> <li>• Minutes</li> <li>• IC Education</li> <li>• Review Investment Philosophy/ Values-Based Investing</li> </ul>
Q4	<ul style="list-style-type: none"> <li>• Performance</li> <li>• IPS Adherence</li> <li>• FYE Goals: Review &amp; Reset</li> </ul>	<ul style="list-style-type: none"> <li>• Market Update &amp; Outlook</li> <li>• Focus: Public Equity</li> <li>• Long -Term Capital Markets Assumptions</li> <li>• Long-Term Policy Portfolio</li> </ul>	<ul style="list-style-type: none"> <li>• Senior Management Report</li> <li>• Expected Inflows/Outflows</li> </ul>	<ul style="list-style-type: none"> <li>• Minutes</li> <li>• Annual OCIO Review</li> <li>• IC Membership Appts.</li> <li>• Report to BoD</li> <li>• Create next FY calendar</li> </ul>



**T**hank you for your interest in Outsourced Chief Investment Officer services. For more in-depth information and analysis, we invite you to visit [ocio.org](https://ocio.org).

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