



Discussing the Intersection of Strategy, Risk, and Finances: A Focus on Reserves & Investments

Taylor Powell

Jim Mari, CFP®

We'll get you there.



Disclosures

CliftonLarsonAllen Wealth Advisors, LLC (“CLA Wealth Advisors”) is an SEC-registered investment advisor that offers a wide array of private wealth advisory services. For more information about CLA Wealth Advisors’ business practices, fees, and services, please refer to our Form ADV Part 2A (the “Disclosure Brochure”). Your investment professional must provide you with a copy of the Disclosure Brochure before or at the time when you enter into a legal agreement with us.

Performance can not be guaranteed and any references to past specific performance should not be interpreted as a promise to achieve results. Investing involves various degrees of risk. You may lose money, including the principal of your investment.

Before deciding whether to engage CLA Wealth Advisors to manage any investment assets, you should review CLA Wealth Advisors’ Form ADV Part 2A (the “Disclosure Brochure”). Our Disclosure Brochure provides detailed description of CLA Wealth Advisors, its services, fees, and other important information including explanation of conflicts of interest. CliftonLarsonAllen Wealth Advisors, LLC is a wholly owned company of CliftonLarsonAllen LLP.

Different types of investments involve varying degrees of risk, including the loss of principal. There can be no assurance that the future performance of any specific investment or investment strategy (including those undertaken or recommended by CLA Wealth Advisors), will be profitable or equal any historical performance level(s).

This report relied on information supplied by the client’s current third party vendors and cannot be independently verified for accuracy without going outside of the scope of this engagement. While these sources are believed to be reliable, the data providers are responsible for the accuracy and completeness of their statements. Nothing came to our attention that would cause CLA Wealth Advisors to believe that the information presented is significantly misstated.





The information herein has been provided by CliftonLarsonAllen LLP for general information purposes only. The presentation and related materials, if any, do not implicate any client, advisory, fiduciary, or professional relationship between you and CliftonLarsonAllen LLP and neither CliftonLarsonAllen LLP nor any other person or entity is, in connection with the presentation and/or materials, engaged in rendering auditing, accounting, tax, legal, medical, investment, advisory, consulting, or any other professional service or advice. Neither the presentation nor the materials, if any, should be considered a substitute for your independent investigation and your sound technical business judgment. You or your entity, if applicable, should consult with a professional advisor familiar with your particular factual situation for advice or service concerning any specific matters.

CliftonLarsonAllen LLP is not licensed to practice law, nor does it practice law. The presentation and materials, if any, are for general guidance purposes and not a substitute for compliance obligations. The presentation and/or materials may not be applicable to, or suitable for, your specific circumstances or needs, and may require consultation with counsel, consultants, or advisors if any action is to be contemplated. You should contact your CliftonLarsonAllen LLP or other professional prior to taking any action based upon the information in the presentation or materials provided. CliftonLarsonAllen LLP assumes no obligation to inform you of any changes in laws or other factors that could affect the information contained herein.

Welcome & Housekeeping

- CPE certificates will be emailed with-in 4 weeks following today's presentation to the email that was used to register. Recommended CPE of 1.5 credits total will be given for attendance of today's roundtable.
- All presentations will be available at the CLASconnect.com under the past events page at the end of the week.



Agenda

- I. Welcome and Focusing on the Future
 - I. Define Reserves and Why They are Needed
- II. Reserves: NFP Industry Perspective
 - I. Describe the Current Environment
- III. Tactically Building Data-Driven Risk-Based Reserves
- IV. Financial Planning/Investment Policy Statement
 - I. Essential Investment Policies
 - II. Evaluating Performance
- V. Investment Opportunities: Short-, Medium-, and Long-Term Approach
 - I. Common Pitfalls



Learning Objectives

- Identify how to gain perspective on turning dreams into reality
- Identify how to leverage and elevate reserves as a mechanism for growth
- Summarize your knowledge of financial planning and investment strategies





Welcome and Focusing on the Future

We'll get you there.

CPAs | CONSULTANTS | WEALTH ADVISORS

©2022 CliftonLarsonAllen LLP. Investment advisory services are offered through CliftonLarsonAllen Wealth Advisors, LLC, an SEC-registered investment advisor.

Discussion 1

What does your organization's dream for the future state look like?

Expanded current services to more people

Creation of new services/offerings



Why Organizations Need Reserves

- Bridge cash flows
- Maintain financial solvency
- Weather economic cycles
- Fund (un)expected opportunities
- Protect against unpredictable political behavior
- Maintain and purchase productive assets
- Reinvest for programmatic relevance and impact
- Generate interest income to support operations
- Drive capacity for new debt to fund major capital needs

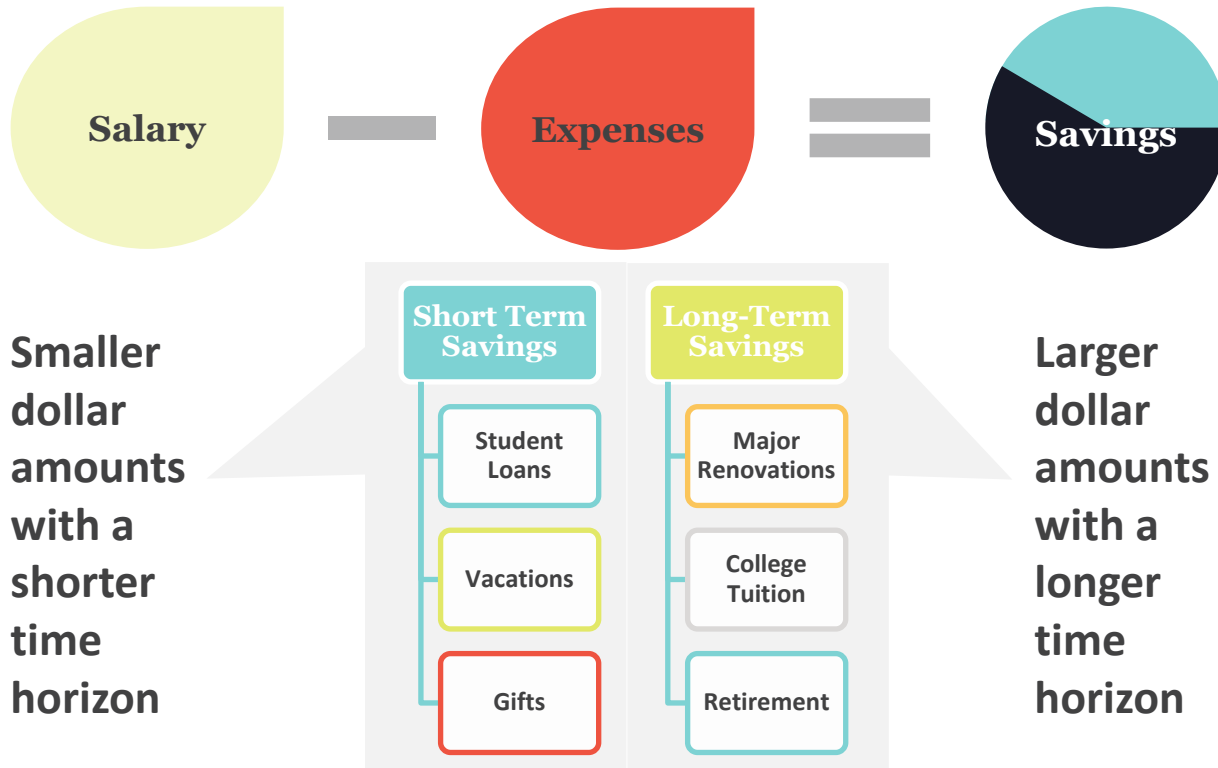


The Nature of Reserves

- Represent accumulated surpluses over time.
- Investments represent **a portion** of that reserve.
- Perpetual in nature.
- Ultimate source of internal financing.
- Performance is generally out of management's control.
- In-house and board investment expertise is typically weak.
- Pressure for sound management and governance.



Analogy to Personal Financial Planning



How Do You Define Sustainability?

“The ability to carry out activities that will achieve your mission while also developing and maintaining capacity for mission relevance into the future.”





The Current Environment & Reserves



We'll get you there.

CPAs | CONSULTANTS | WEALTH ADVISORS

State of the Industry

- It's never been more important to find ways to continuously monitor the financial health of your nonprofit organization.
- A 2018 analysis of nonprofit financial health conducted by Oliver Wyman, SeaChange Capital Partners, and GuideStar by Candid concluded that among U.S. nonprofits:
 - ✓ 7-8% are technically insolvent with liabilities exceeding assets
 - ✓ 30% face potential liquidity issues with minimal cash reserves and/or short-term assets less than short-term liabilities
 - ✓ ~50% have less than one month of operating reserves



12 Key Metrics to Monitor the Financial Health of Your Nonprofit

BY NANCY MASTER | JANUARY 13, 2021



Nonprofit finance leaders are responsible for ensuring good stewardship of donor dollars, so the greatest possible percentage of resources can go toward achieving your mission and not operational expenses. Nonprofit leaders want

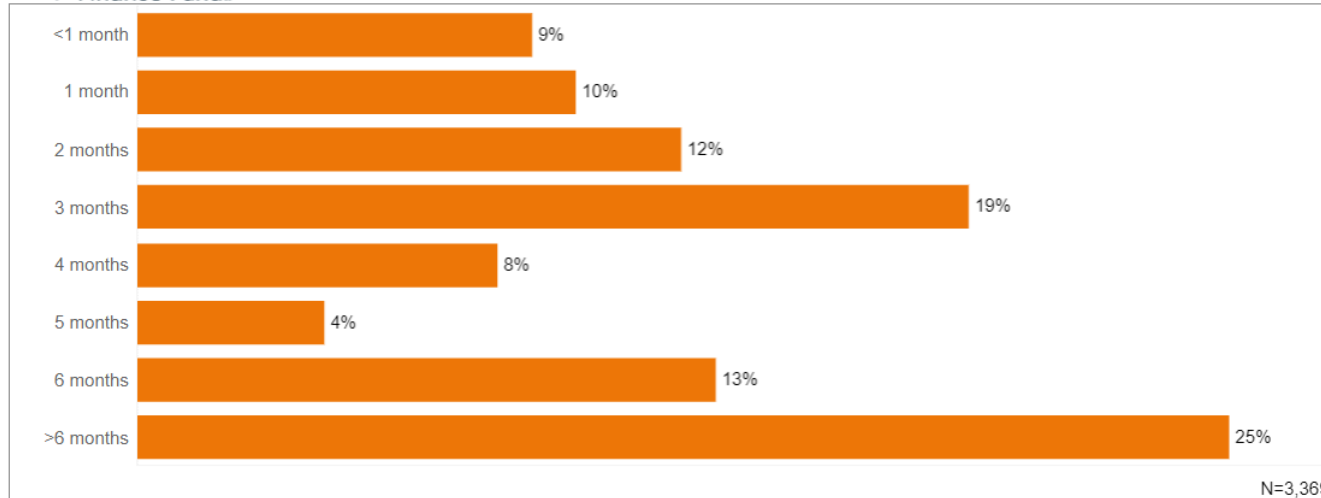


State of the Industry



Cash on Hand

© 2018 Nonprofit Finance Fund. All Rights Reserved.



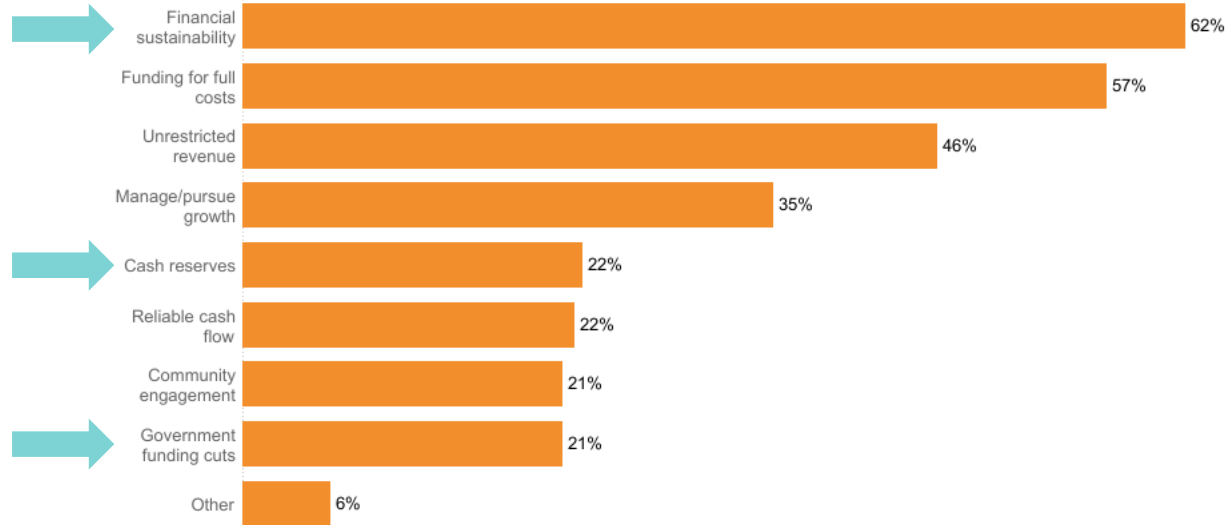
State of the Industry (cont'd)



Nonprofit
Finance Fund

Top operational/financial challenges

© 2018 Nonprofit Finance Fund. All Rights Reserved.



N=2,694



In the Media: More Pressure Than Ever

The Mercury News

THE CHRONICLE OF

PHILANTHROPY

ARTICLE

MARCH 10, 2020



As Coronavirus Threat Continues, Experts Tell Nonprofits to Shore Up Reserves

By Dan Parks, Emily Haynes, and Maria Di Mento

Community News • News

Coronavirus pushing arts and nonprofit groups to the edge: Pizarro

A disaster relief fund will be needed — and it starts with all of us



Accumulating Funds - Avoid accumulating funds that could be used for current program activities. To meet this standard, the charity's unrestricted net assets available for use should not be more than three times the size of the past year's expenses or three times the size of the current year's budget, whichever is higher.



How Is The Shutdown Affecting America? Let Us Count The Ways

HEALTHCARE FINANCE

MAR 09, 2018 | MORE ON REIMBURSEMENT

Moody's says nonprofits struggle to maintain credit ratings in 2017

Mergers and acquisitions didn't necessarily help providers and labor costs remain a burden as downgrades go up.



End Game \approx Sustainability

- Ability to carry out activities that will achieve your mission while developing & maintaining capacity for mission relevance in the future.



Common Misconceptions

IRS regulations prohibit nonprofits from having a profit

If a nonprofit has a reserve, they are hoarding donor funds

Nonprofits with reserves don't need more funds



Discussion 2

What are key risks that could prevent achieving the dream future state?





Developing Risk-Based Reserves

We'll get you there.

CPAs | CONSULTANTS | WEALTH ADVISORS

©2022 CliftonLarsonAllen LLP. Investment advisory services are offered through CliftonLarsonAllen Wealth Advisors, LLC, an SEC-registered investment advisor.

Business Model Components

	Operations		Non-Operating Reserves & Investments	
	Current Business Lines: <i>Ongoing revenue and expenses associated with current business lines</i>	Future Initiatives: <i>Exploratory, aspirational new business lines, offerings, or efforts</i>	Reserves: <i>Short-term holdings</i>	Investment Pool: <i>Long-term investment portfolio</i>
Money In	Dues, Grants, Registrations, Publications, etc.	TBD	Growth	Growth
Transfers	from reserves from investment income from investment pool	TBD	from investment income from investment pool to operations to investment pool	from reserves to reserves to operations
Money out	Expenses	Expenses	--	--
Net	???	???	???	???



Corresponding Questions and Tools

Operations		Non-Operating Reserves & Investments	
Current Programs: <i>Ongoing revenue and expenses associated with current business lines</i>	Future Initiatives: <i>Exploratory, aspirational new business lines, offerings, or efforts</i>	Reserves: <i>Short-term holdings</i>	Investment Pool: <i>Long-term investment portfolio</i>
What economic changes in current business lines are you expecting to see over the next several years?	What are the assumptions about upfront investment, ongoing expense, and expected revenue from these initiatives?	How much of your reserves and investment portfolio (corpus and earnings) should you deploy to fund operations? What amount of expense (and when) are you willing to invest to earn additional revenue?	
Exam Revenue and Margin Goals Pricing Plan Scenario Modeling	Revenue and Margin Goals Pricing Plan Marketing and Sales Plan Portfolio Management Discipline	Reserves Policy Investment Policy Scenario Modeling	



2008: The Last Wave of “Best Practice”

A WHITEPAPER

BY: *The Nonprofit
Operating Reserves
Initiative Workgroup*

In spring 2008, a *Nonprofit Operating Reserves Initiative Workgroup* (see member list on page 10) comprising experienced individuals representing multiple facets of the nonprofit sector was convened with the objective of:

1. Defining an “*Operating Reserve Ratio*”
2. Using the ratio to focus attention on the importance of nonprofit financial stability.

The *Nonprofit Operating Reserves Initiative Workgroup* reached consensus on definitions for *operating reserves* and the “*Operating Reserve Ratio*.” The workgroup also reached a conclusion on what constitutes adequate *operating reserves*. Workgroup member Richard Larkin had previously concluded and written that the answer is: it

MAINTAINING NONPROFIT OPERATING RESERVES

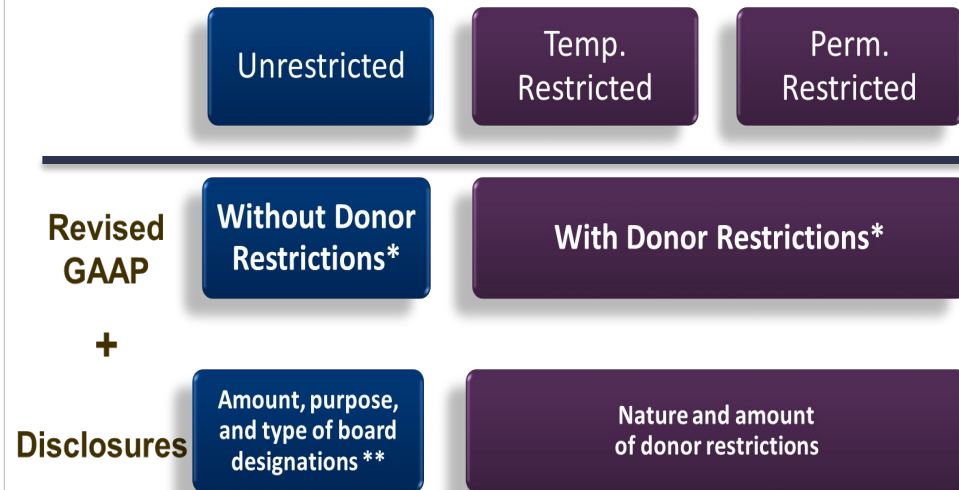
An Organizational Imperative for Nonprofit Financial Stability
December 2008

A top priority for nonprofit leaders needs to be maintaining *operating reserves* at levels adequate for achieving financial stability. While this may seem obvious, preliminary research indicates that many organizations neglect to put aside funds that will help them preserve their capacity to deliver on their missions in the event of unforeseen financial shortages.

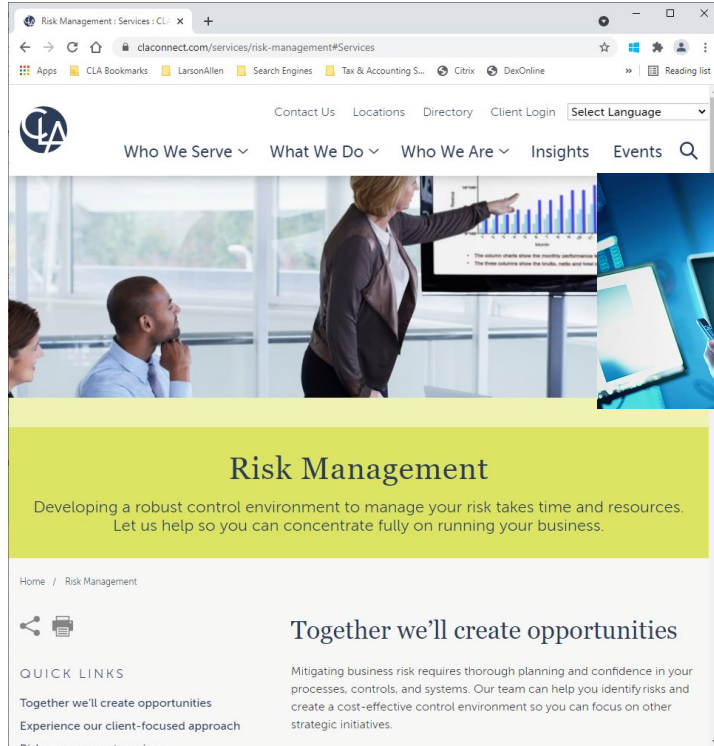
The fact is numerous nonprofits have negative reserves and are already at risk. The Work Group (see side bar) recognizes that the current economic crisis threatens the very existence of thousands of nonprofit organizations. At a time when nonprofit organizations may be focused on survival, the thought of building reserves may seem a distant priority. But for organizations currently just hanging on which expect to survive this crisis and those in relatively stable current financial condition which seek to fortify their position, the Work Group encourages including operating reserves in the planning process. Organizations which review their policies closely and devise plans for replenishing their *operating reserves* to an agreed upon adequate level will emerge from this current economic crisis in a stronger financial position, positioned to withstand the next challenge that arises.

Briefly, *operating reserves* are the portion of “unrestricted net assets” (see Figure 1) that nonprofit boards maintain or designate for use in emergencies to sustain financial operations in the unanticipated event of significant unbudgeted increases in operating expenses and/or losses in operating revenues. “Unrestricted net assets” is a required line item in the balance sheets of financial statements prepared in accordance with generally accepted accounting principles (GAAP) and IRS Forms 990 of nonprofit organizations. [See “*Operating Reserve Ratio*” - page 2]

Figure 1 -- Suggested balance sheet net asset terms presented in an illustration that all nonprofit CEOs and boards need to understand.



Post-Recession Resurgence of ERM + Data



Risk Management Services: CL

claconnect.com/services/risk-management#Services

Contact Us Locations Directory Client Login Select Language

Who We Serve What We Do Who We Are Insights Events

Risk Management

Developing a robust control environment to manage your risk takes time and resources. Let us help so you can concentrate fully on running your business.

Home / Risk Management

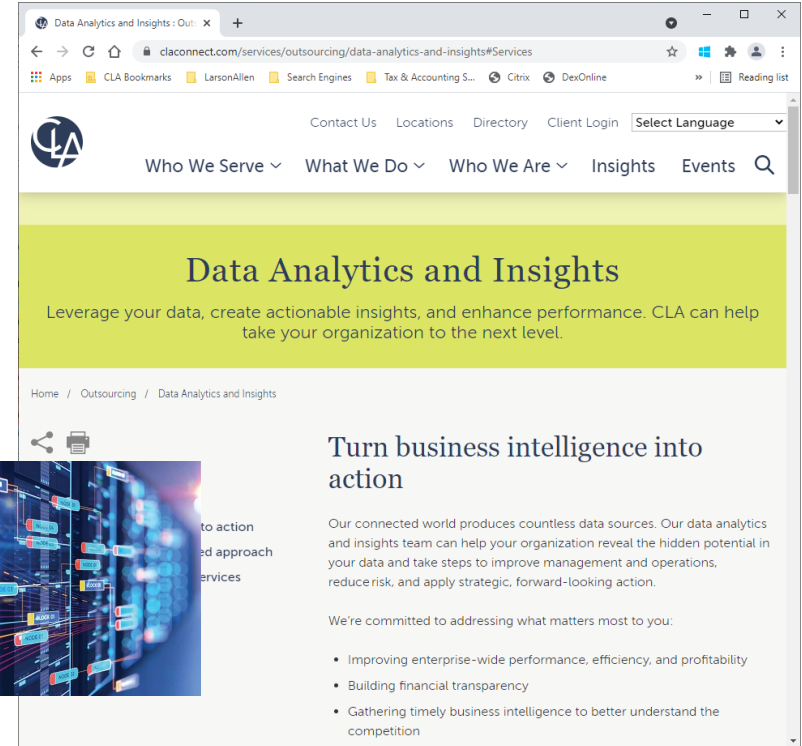
Together we'll create opportunities

Mitigating business risk requires thorough planning and confidence in your processes, controls, and systems. Our team can help you identify risks and create a cost-effective control environment so you can focus on other strategic initiatives.

QUICK LINKS

Together we'll create opportunities

Experience our client-focused approach



Data Analytics and Insights: Out

claconnect.com/services/outourcing/data-analytics-and-insights#Services

Contact Us Locations Directory Client Login Select Language

Who We Serve What We Do Who We Are Insights Events

Data Analytics and Insights

Leverage your data, create actionable insights, and enhance performance. CLA can help take your organization to the next level.

Home / Outsourcing / Data Analytics and Insights

Turn business intelligence into action

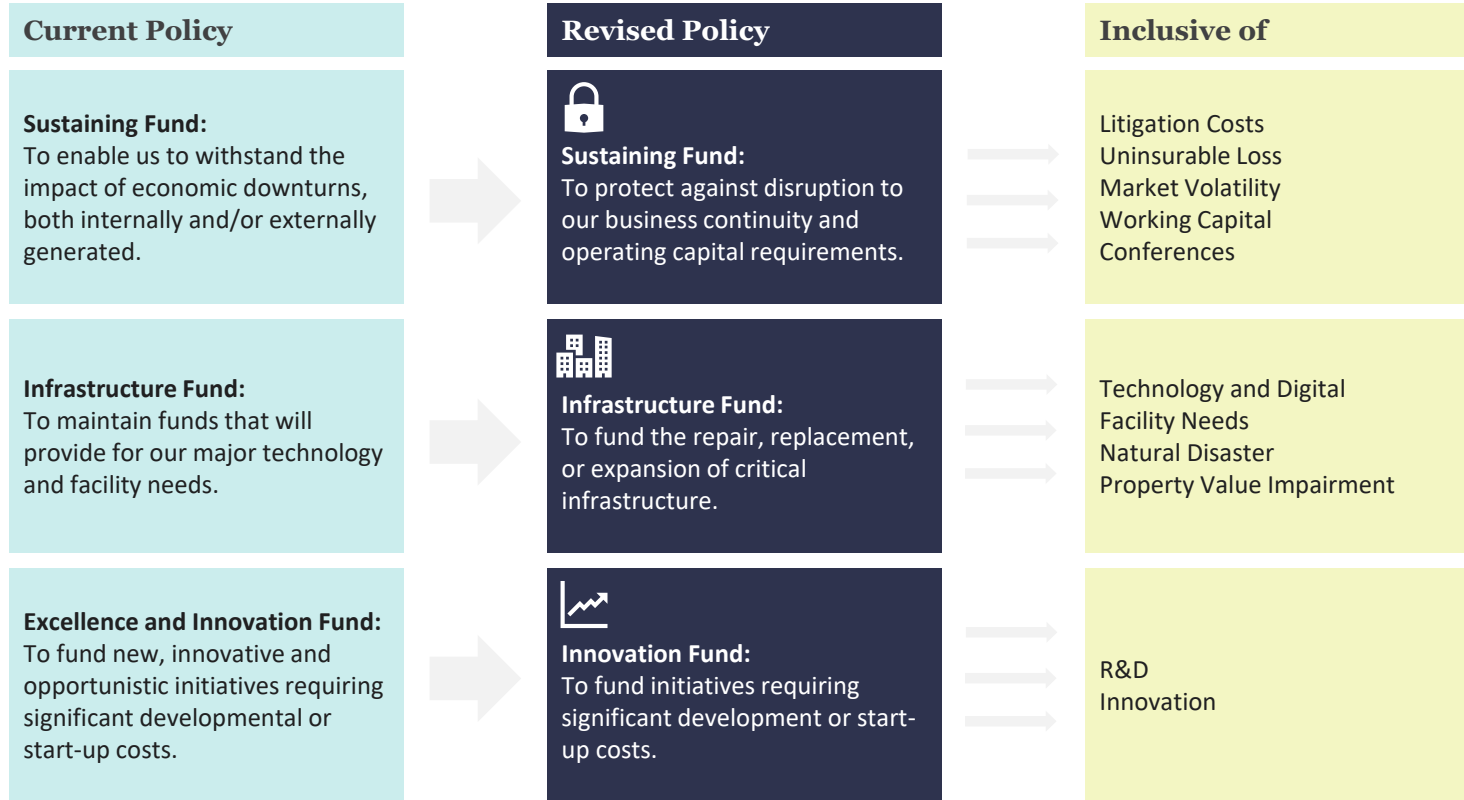
Our connected world produces countless data sources. Our data analytics and insights team can help your organization reveal the hidden potential in your data and take steps to improve management and operations, reduce risk, and apply strategic, forward-looking action.

We're committed to addressing what matters most to you:

- Improving enterprise-wide performance, efficiency, and profitability
- Building financial transparency
- Gathering timely business intelligence to better understand the competition

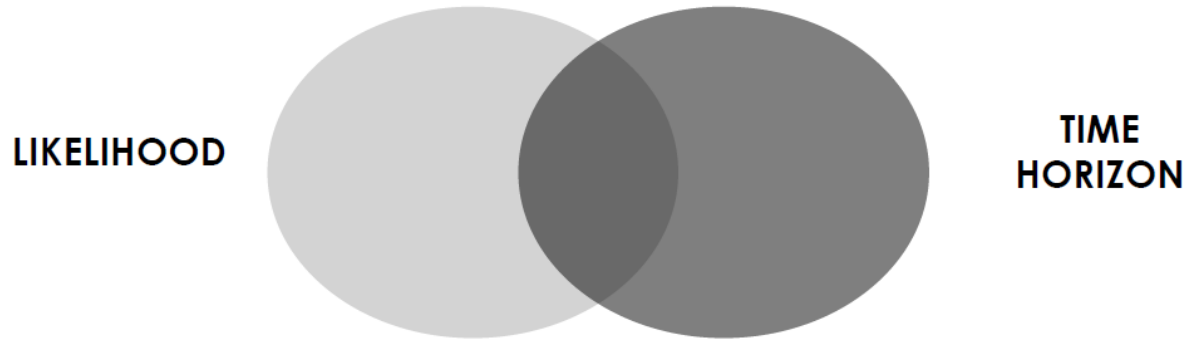


Sample Reserve Categories: Data-Driven Revisions

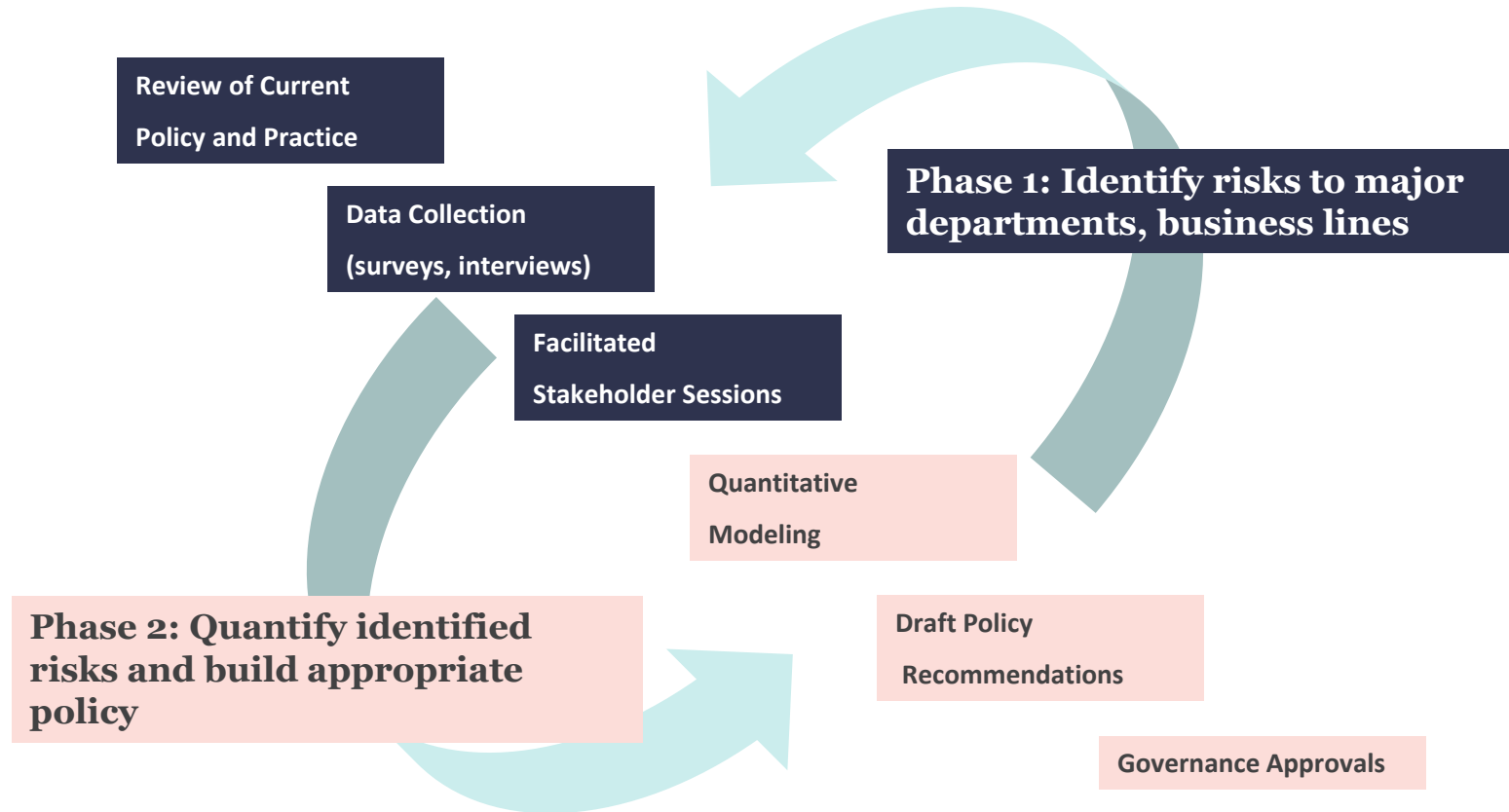


Likelihood and Timing

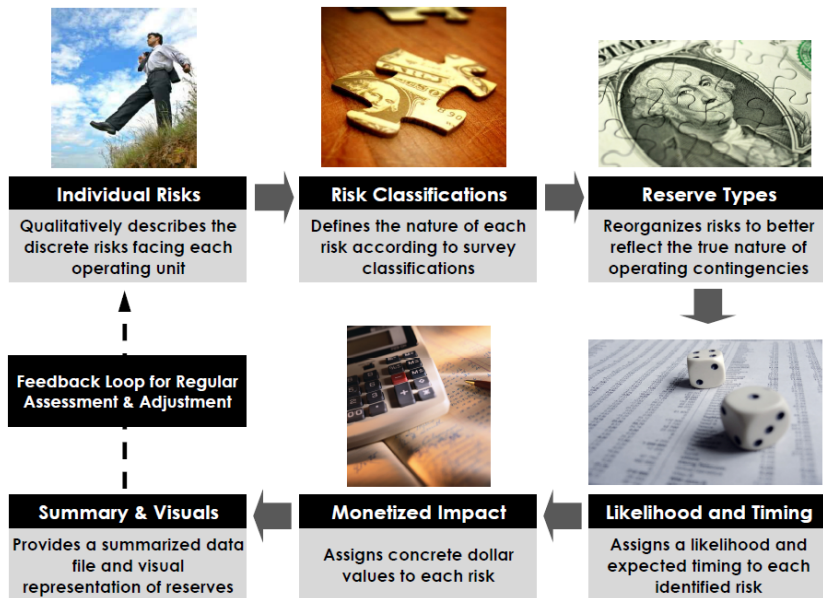
- Not everything will happen at once.
 - Consider the time horizon for the risk – less than 1 year, less than 5 years over 5 years
 - Take into account the level of risk – high, medium, low



A Data-Driven, Risk-Based Method



Data-Driven Reserve Model Schematic



Reserve Category	Reserve Sub-Category	Identified Risk/ Opportunity Area	Estimated Reserve Requirement	Estimated Likelihood % per Survey	Estimated Time Horizon per Survey	Reserve Levels at 12/31/2020			
						At Full Value	Recommendation	Per Current Policy	CLA Notes
Sustaining Fund	Working Capital / Operating Reserve	To provide internal working capital to finance minimum operating cash flow and debt service needs.	\$ 12,810,000	Medium	Within the next 12 months	12,810,000	12,810,000	N/A	Calculation = 3 months FY 2022 budgeted expenses
Sustaining Fund	Uninsurable Loss	To protect us in the event of uninsurable loss	\$ 7,500,000	Low (25% or less)	1 - 3 years	7,500,000	1,875,000	N/A	Discounted to 25% reflect low likelihood and prospective overlap with other categories.
Sustaining Fund	Market Volatility	To fund a loss of investment interest income caused by market volatility	\$ 10,000,000	High (75% or higher)	Within the next 12 months	10,000,000	10,000,000	N/A	Reasonable assumption prepared by Controller, CFO, and CIO, endorsed by CLIA.
Sustaining Fund	Litigation Costs	To protect us in the event of litigation	\$ 7,500,000	Low (25% or less)	1 - 3 years	7,500,000	1,875,000	N/A	Discounted to reflect low likelihood and prospective overlap with other categories. Covers potential chapter exposure.
Sustaining Fund	Lease Revenue Impairment	To offset a loss of revenue from facility leases	\$ 300,000	High (75% or higher)	Within the next 12 months	300,000	300,000	N/A	Passed this apart from "Property Value Impairment" given its focus on underlining a revenue stream. See calculation below.
Sustaining Fund	Conferences	To offset a loss of revenue from conference activities	\$ 8,000,000	Low (25% or less)	Within the next 12 months	8,000,000	6,000,000	N/A	Set at 50% given unknown of current environment.
Sustaining Fund Subtotal						\$ 46,110,000	\$ 32,860,000	\$ 50,393,000	
Infrastructure Fund	Technology and Digital	To fund the repair, replacement, or expansion of critical technology infrastructure	\$ 5,000,000	High (75% or higher)	1 - 3 years	5,000,000	5,000,000	N/A	Fully fund at 50M.
Infrastructure Fund	Facility Needs	To fund the repair, replacement, or expansion of critical facility infrastructure	\$ 2,500,000	Low (25% or less)	1 - 3 years	2,500,000	2,500,000	N/A	Fully fund at 50.5M.
Infrastructure Fund	Natural Disaster	To offset the negative financial impact of natural disaster	\$ 5,000,000	Low (25% or less)	5 - 10 years	5,000,000	2,500,000	N/A	Discounted to 50% reflect low likelihood and prospective overlap with other categories.
Infrastructure Fund Subtotal						\$ 12,500,000	\$ 10,000,000	\$ 10,000,000	
Excellence and Innovation Fund	Innovation	To fund initiatives requiring significant development or start-up costs	\$ 10,000,000	100%	Within the next 12 months	10,000,000	10,000,000	N/A	Fully fund at 50M.
Excellence and Innovation Fund Subtotal						\$ 10,000,000	\$ 10,000,000	\$ 2,000,000	
Scholarship Fund	Scholarships	To provide self-sustaining financial support for our scholarship program	\$ 2,000,000	100%	Within the next 12 months	2,000,000	2,000,000	N/A	No change proposed.
Scholarship Fund Subtotal						\$ 2,000,000	\$ 2,000,000	\$ 2,000,000	
Total Reserve Amount - All Categories						\$ 70,610,000	\$ 54,860,000	\$ 72,393,000	






A Deeper Dive on Investment Risks

We'll get you there.

CPAs | CONSULTANTS | WEALTH ADVISORS

©2022 CliftonLarsonAllen LLP. Investment advisory services are offered through CliftonLarsonAllen Wealth Advisors, LLC, an SEC-registered investment advisor.

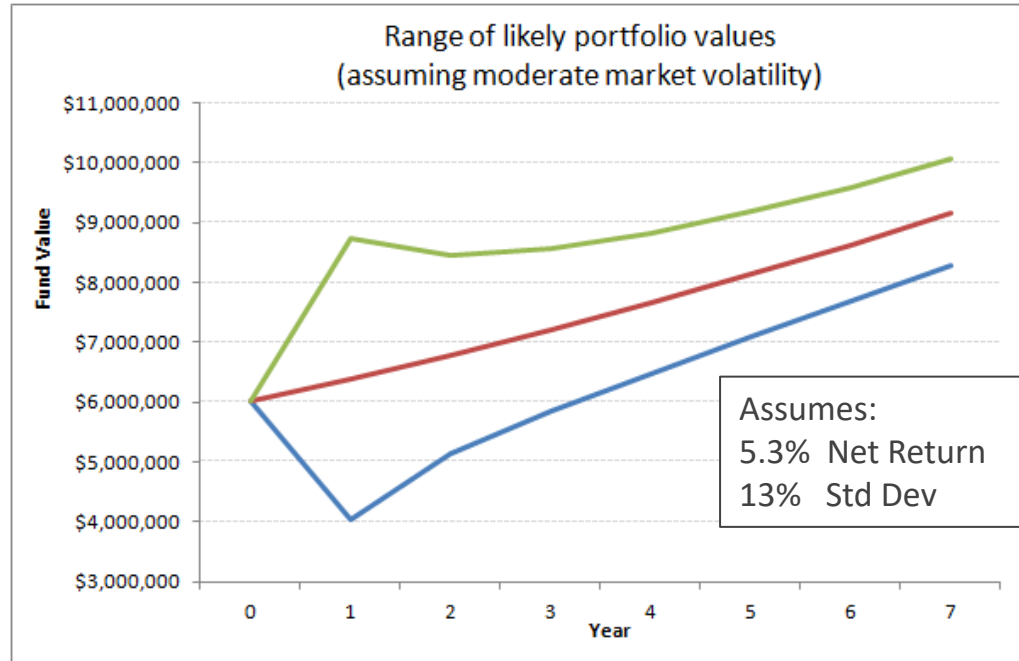
Measuring Risk Tolerance

- I. Individual investors understand risk qualitatively - typically via Risk Tolerance Questionnaires & Surveys
 - i.e. By how much could the total value of your investments decline before you would want to sell?
 - a) -5%
 - b) -10%
 - c) -20%
 - d) -30%
- II. We employ quantitative measures with institutional investors.
 - I. Cash Flow Analysis  Time Horizon
 - II. Asset/Liability Management Techniques
 - I. Cash Reserve
 - II. Cash Matching
 - III. Duration Matching
 - IV. Monte Carlo Simulation
 - III. **Financial Stress Testing**



To an institution (presumably a patient and well-diversified investor), volatility must be managed in consideration of its short term impact on the entity.

Non-intuitively, long-term forecasts are **more accurate** than short-term forecasts
Hypothetical Risk/Return, 7-year Outlook



Developing a Risk Budget (Tolerance)

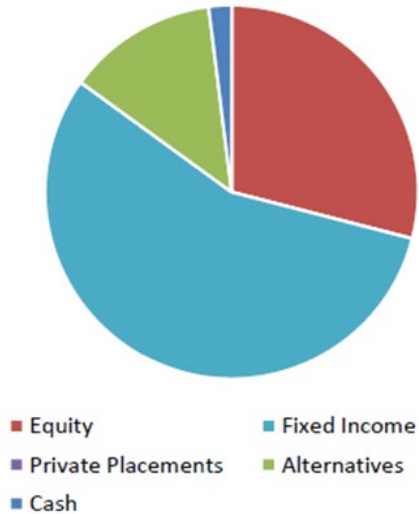
Portfolio Summary

Objective:	Balanced Account
Strategy:	Total Return - iShares

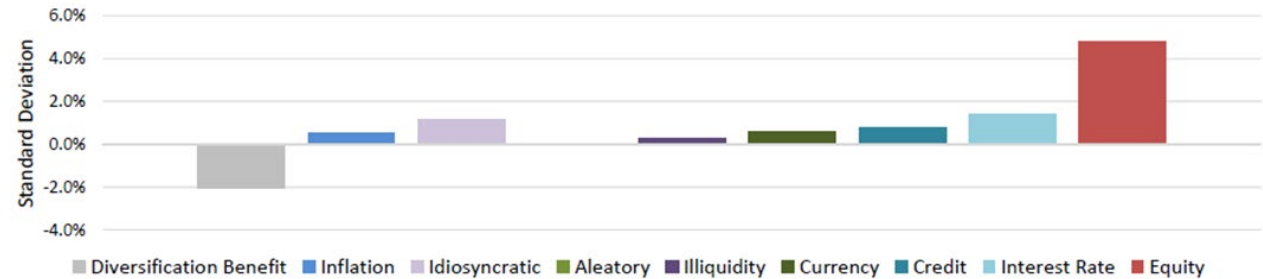
Portfolio Characteristics		Current	Target
Total Return Estimate	<i>7-10 Year, Annualized</i>	4.4%	4.8%
Risk Estimate	<i>Standard Deviation</i>	7.0%	7.5%
Sharpe Ratio	<i>Risk/Return Efficiency</i>	0.31	0.35
Value at Risk (Mod. Volatility)	<i>1-Year</i>	-9.7%	-10.2%
Value at Risk (High Volatility)	<i>1-Year</i>	-16.7%	-17.6%

Asset Allocation

When appropriate policies and parameters are put in place and the risk and return needs are quantified to align with the strategic plan, investment selections become a byproduct of a process that focuses on stewardship and governance.



Sources of Portfolio Risk



Diversification: A Functional Approach

Inflation Protection Assets help protect a portfolio from unanticipated inflation.

Liquid Real Assets

- TIPS
- REITs
- MLPs
- Energy & Commodity Stocks
- Managed Futures

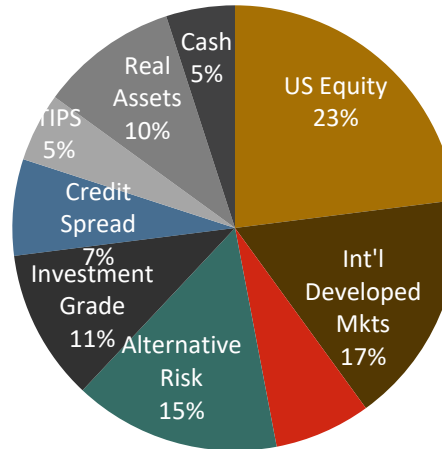
Private Real Assets

- Real Estate
- Energy, Mining and Minerals

Risk Reduction Assets dampen overall portfolio volatility through their own low volatility and by having a low correlation to Growth Assets.

Investment Grade Credit

- Cash
- Municipals
- Treasuries
- Investment Grade Credit
- Emerging Market Debt



Growth Assets generate returns based on growth of the world economy.

Large Cap

Small Cap

International Equity

- Developed Markets
- Emerging Markets
- Frontier Markets

Private Equity

- Venture Capital
- Buyouts
- Mezzanine Financing

Alternative Risk Assets exhibit low correlation to traditional strategies

Risk Reduction

- Multi-Asset Managers
- Long/Short Equity
- Market Neutral
- Merger Arbitrage

Opportunistic

- Global Macro
- Distressed Debt
- Concentrated and Special Situation managers





Developing a Reserve Policy



We'll get you there.

CPAs | CONSULTANTS | WEALTH ADVISORS

Investment Policy Statement: An Essential Document

CFA® Institute Definition

- A strategic guide
- Anticipates issues related to governance
- Plans for the appropriate:
 - Asset allocation
 - Internal and/or external investment managers
 - Monitoring and reporting results
 - Risk management
- Establishes accountability
- Offers objective course of action during periods of market disruption

A highly customized document, uniquely tailored to the preferences, attitudes and situation of each investor.

CFP® Board Definition

- A written expression of the client's objectives of risk and return along with any constraints in their implementation.
- Governs all investment decisions for the client.
- Outlines responsibilities of the client and planner alike.
- Provides a means for evaluating investment performance.

While all investment policy statements share basic features, they will differ by client type and within client type.

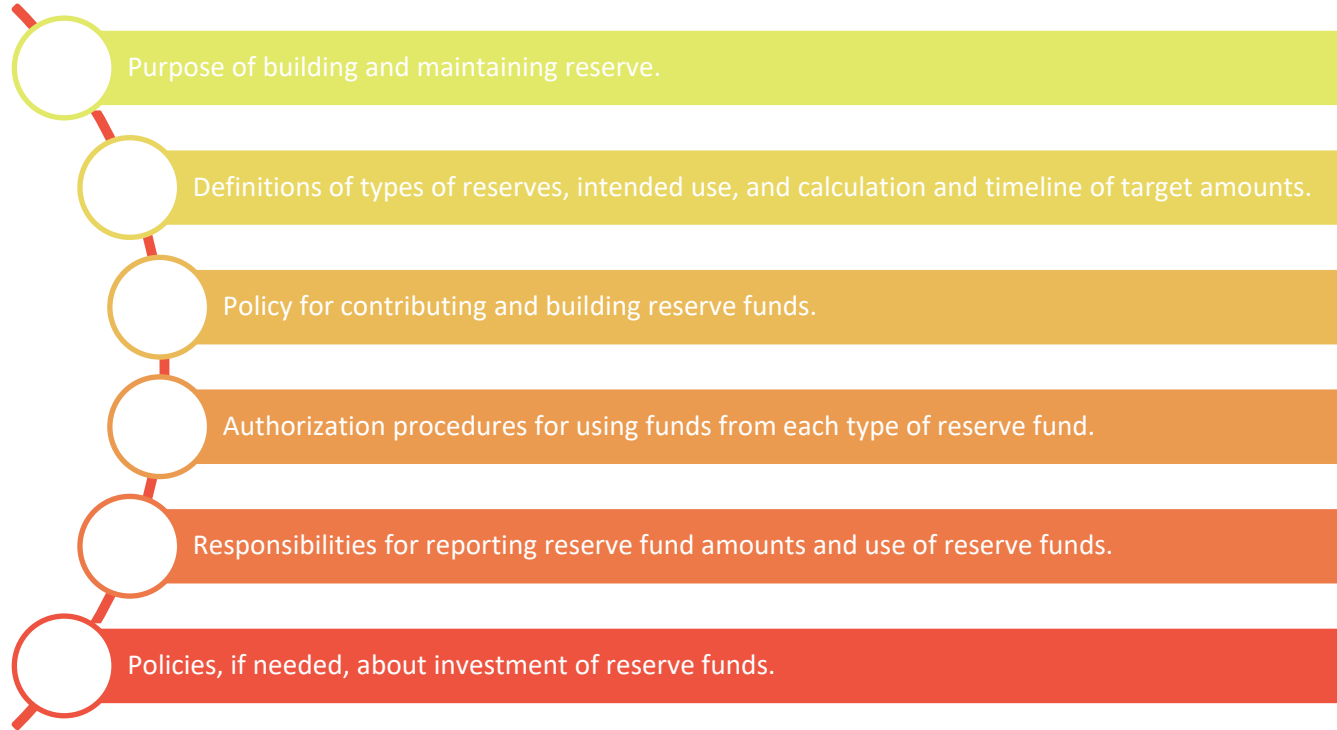


Some Perspective

- The Investment Policy Statement is often overlooked, even by investment professionals.
 - Frequently looking to make recommendations that fit the IPS but not review the document to ensure it is appropriate.
- There are not many places to get specific advice for how to write and manage the document.
 - Templates offer generic one-size fits all solutions



Policy Development – What to Include



Some Specific Items:

- History & Purpose of the Fund
- Standard of Care
- Annual Review/Update Affirmation
- Definition of Duties
- Investment Objectives
- Asset Allocation
- Rebalancing
- Benchmarks
- Manager Guidelines and Restrictions
- Prohibited Securities/Transactions
- Brokerage / “Soft Dollar” Use
- Securities Lending



Essential Investment Reserve & Endowment Policies

Purpose- What are the intended/restricted uses of the funds and how will they be invested/accessed to meet these needs?

Operational Needs/Transfers-What are the operational needs associated with these funds that will in part dictate their relative liquidity requirements. What policies, procedures and approvals will be required to transfer funds from reserves/endowments to operations?

Spending Policy-What are the board-designated, donor imposed and regulatory spending policies associated with these funds (e.g., scholarships, capital campaign, private foundation requirements, etc.) and how will they inform the investment policy ?



Standard of Care

What is the appropriate legal jurisdiction?

- Common Law (trust law originated state courts)
 - Prudent Person Rule
 - Prudent Investor Rule
- ERISA (Federal law for qualified pension plans)
- State Statute (governs state and municipal funds)
- Uniform Prudent Management of Institutional Funds Act (UPMIFA governs many endowments/foundations)

In nearly all cases, individuals with oversight or operational responsibility are fiduciaries.

A fiduciary duty is a legal duty to act solely in another party's interests.



Definition of Duties

Governing Body

- Trustees / Board of Directors / Other
 - Ultimate fiduciary responsibility
 - Must ensure appropriate policies and governance

All others are **delegated authority** by the Governing Body.

- Finance Committee / Investment Committee
- Financial Officers / Staff
- Investment Advisor / Consultant
 - Discretionary
 - Non-Discretionary
- Custodian
- Other (i.e., legal, actuarial)

Include language about how “Conflicts of Interest” are resolved.



Critical Roles & Responsibilities

- **Management: Executive, Finance, Development** Develop policies for board approval that clearly outline the nature, use, restrictions, goals and accountabilities associated with investment reserves and endowments
- **Board, Officers, & Committees** (Executive, Finance, Investment)
Review, Understand and Drive Consensus around investment, reserve and endowment policies consistent with their fiduciary role donor intent, strategic priorities and regulatory compliance. Monitor and update on a periodic basis.



Critical Roles & Responsibilities

- **Investment Advisors** - Responsible for consulting with management and the board/committees to ensure adoption of sound investment policies, strategies and accountable reporting consistent with the intended use and restrictions associated with the underlying funds.
 - Includes defining risk tolerance, time horizon, asset allocation, return objectives, asset class and peer benchmarks, reporting format and frequency
 - Can act with or without “discretion”
 - Should be independent of underlying investment managers
 - Typically paid a management fee percentage of the market value of Assets Under Management (AUM)



Critical Roles & Responsibilities

- **Investment/Fund Managers** - Those organization and funds actually deploying the asset allocation strategy as set forth in the board approved investment strategy (e.g., large cap, small cap, fixed income, real estate, private equity etc.).
 - Report to the organization directly and/or through the Investment Advisor
 - Are hired, retained or fired based on investment advisor/management recommendation to the board based on performance and ability to adhere to the investment policy and meet associated objectives
 - Typically paid a management fee percentage of the market value of Assets Under Management (AUM) in addition to internal fund fees



Annual Review/Update/Affirmation

The IPS should contain:

- Authorized signature & date
- Dates adopted, updated, affirmed

At least annually:

- IPS should be affirmed or updated
- Estimated fees/expenses should be affirmed by governing body or put out to bid.



Investment Objectives

Should present clear understanding of investment philosophy and objectives.

- Return Objective
 - Relative to Inflation (i.e., CPI + 4%, CPI + 1%)
 - Actuarial - Investment Return Assumption
 - Spending + Growth Target (i.e., 4% + 2% = 6%)
- Time Horizon
- Liquidity Constraints
- Risk Budget (Tolerance)
- Regulatory Considerations
- Taxes
- Unique Circumstances



Rebalancing Back To Target Asset Allocation

- IPS should specify who is responsible for **monitoring** the fund, **recommending/approving** any changes and **executing** trades.

Options include:

- Governing Body
 - Finance or Investment Committee
 - Financial Officers / Staff
 - Investment Advisor/Consultant (may require discretion)
 - Some combination of the above?
- What are the rules for rebalancing back to Target?
 - Periodicity (daily, monthly or quarterly review)
 - Absolute difference (± 2 percentage points)
 - Relative difference ($\pm 5\%$)



Essential Investment Reserve & Endowment Policies

Asset Allocation-What mix of assets (e.g., money market cash, equity, fixed income, real estate, private equity, etc.) will best achieve the risk and return objectives of the portfolio. Typically expressed in ranges (high, low, target) to avoid divestitures that may not make strategic/tactical sense. Required periodic rebalancing of the portfolio should also be specifically stated.

Prohibited Investments-What investments for reasons of risk, social responsibility and/or organizational mission should be prohibited from the investment reserves/endowment portfolio (e.g., tobacco, alcohol, fire arms, etc.) and how will this be achieved and monitored? What is the potential impact on performance?



Manager Guidelines and Restrictions

Disclaimer

In today's rapidly changing and complex financial world, no list or types of categories of investments can provide continuously adequate guidance for achieving the long-term investment goals of the Fund. Any such list is likely to be too inflexible to be suitable for the market environment in which investment decisions must be made.

Therefore, it is the process by which investment strategies and decisions are developed, analyzed, adopted, implemented and monitored, and the overall manner in which investment risk is managed, which determines whether an appropriate standard of reasonableness, care and prudence has been met for the Fund's investments.



Manager Guidelines and Restrictions

Each investment manager shall:

- Follow their respective IPS guidelines
 - Equity
 - Fixed Income
 - Cash Equivalent
 - Alternative Investments
- Vote proxies and tender shares
- Immediately notify the Committee in writing of any material changes in the investment outlook, strategy, portfolio structure, ownership or senior personnel.

Separately Managed Accounts have more flexibility to impose restrictions than do mutual funds or other pooled accounts.



Prohibited Securities / Transactions

Each investment manager shall not invest in... (examples)

- Non-marketable securities
- Short-selling
- Margin trading
- Private placements
- Direct investments in commodities
- Fixed income securities below investment grade
- More than 5% of the outstanding shares of any one company
- Penny stocks
- Derivatives



Brokerage / Soft Dollar Use

Best Execution refers to executing Client transactions so that the Client's total cost is the most favorable under the particular circumstances at that time.

Soft dollar practices involve the use of client brokerage by an investment manager to obtain certain products and services to aid the manager in its investment decision-making process. The practice of using client brokerage to purchase research has become extremely complex. No finite set of standards can cover all potential situations or anticipated future developments concerning the types of investment research available to investment managers.

Source: CFA Institute



Securities Lending

Prohibited or Allowed?

“Securities lending is a well-established practice where funds make short-term loans of stocks or bonds to incrementally increase returns to investors.”

Source: BLACKROCK

“The act of loaning a stock, derivative, other security to an investor or firm. Securities lending requires the borrower to put up collateral, whether cash, security or a letter of credit. When a security is loaned, the title and the ownership is also transferred to the borrower.”

Source: Investopedia

You may be denied access to the security when you need or want it.



Benchmarking Performance

- Strategic Benchmark
 - Broad-Based Indices
(i.e., 50% DJ Total Stock Market, 50% Barclays Aggregate)
 - Weightings are drawn from Target Asset Allocation in IPS
- Tactical Benchmark
 - More “Granular” Indices
(i.e., 20% Russell 1000 Value, 30% Russell 1000 Growth, 40% Barclays Aggregate, 10% Merrill High Yield)
 - Actual weightings, from current holdings

Strategic and Tactical benchmarks allow for the calculation of Attribution Analysis.

Attribution Analysis – Helps to answer what portion of performance is due to: Asset Allocation and Manager Selection



Evaluating Performance

- Key is to clearly outline roles, responsibilities and expectations in the investment policy
- What are you buying when employing an Investment Advisor?
 - A consultant to ensure best practice expertise in the design and monitoring of your Nonprofit investment, reserve and endowment policies
 - An independent advisor to your management, board and relevant committees in evaluating performance and making responsible recommendations consistent with your return objectives and risk profile
 - An independent fund/manager platform best suited to deploy your strategy



Evaluating Performance

- Performance targets should be net of all costs and appropriate for each specific asset class (emerging market equities, domestic small cap, short-term municipal debt, etc.)
- Benchmarks should be chosen and compared for each element of the asset allocation and within the peer group of funds/managers (i.e., which managers did better or worse in beating the asset class benchmark?)
- An Overall *Personal Composite Return* target should be established for the portfolio which takes the appropriate percentage of all the underlying asset class benchmarks to reflect the return you should be achieving based on your asset allocation



Better Governance starts with focusing on what can be controlled

Fiduciaries have control over the following three factors:

- 1) Risk (overall portfolio volatility and market capture)
- 2) Diversification
- 3) Fees

Return Expectations are **residual & systematic**.

Fiduciaries should act prudently and weigh the above issues carefully in order to construct an efficient portfolio.

Fiduciaries should develop and maintain proper documentation to support their decisions.



Investment RFP Process

- When To Bid Out
 - Not meeting performance targets over agreed upon investment cycle (no less than 3 years)
 - Client service issues
 - To assess the market (at least every 10 years)
- Three flavors:
 - Money Managers
 - Broker Dealers
 - Independent Advisors



Investment RFP Process

- Trade-offs:
 - Cost
 - Independence
 - Depth of Internal Resources
- Send Out 4-6 RFP's Covering the 3 Flavors
- Develop a Scoring Matrix
- Have 2-3 Finalist Present to Board Committee





Common Pitfalls

We'll get you there.

CPAs | CONSULTANTS | WEALTH ADVISORS

©2022 CliftonLarsonAllen LLP. Investment advisory services are offered through CliftonLarsonAllen Wealth Advisors, LLC, an SEC-registered investment advisor.

Common Pitfalls

- Not understanding the underlying advisor, manager, fund and custodial costs associated with your portfolio. In a low-return environment these have a major impact on net returns and are very negotiable.
- Confusing Investment *Advisors* with Investment *Managers*. Advisors should be independent of the managers and the investments they recommend.
- Establishing risk tolerance based on individual perspectives of management and/or board/committee members rather than what is appropriate for the organization.



Common Pitfalls

- Excessive allocation to high-cost, complex and often low performing alternative investments
- A lack of understanding around key terms. For example a “Basis Point” is a short-hand expression of cost or return. 100 basis points =1%, 50 basis points =.50%, etc.
- Paying additional fees for giving investment advisors “discretion” (i.e., accepting a “fiduciary” standard rather than mere “suitability”)



Questions?

Taylor Powell, CPA
Taylor.Powell.@claconnect.com

Jim Mari, CFP®
Jim.Mari@claconnect.com



CLAconnect.com



CPAs | CONSULTANTS | WEALTH ADVISORS

CLA (CliftonLarsonAllen LLP) is an independent network member of CLA Global. See [CLAglobal.com/disclaimer](https://claglobal.com/disclaimer).

Investment advisory services are offered through CliftonLarsonAllen Wealth Advisors, LLC, an SEC-registered investment advisor.

©2022 CliftonLarsonAllen LLP



How We Will Work With You

It's our job to engage in conversations, listen to what you really want, and apply our talents and experience to make extraordinary impact on your organization and life.

We'll get you there.

CPAs | CONSULTANTS | WEALTH ADVISORS