



Foundations And Endowments Find Help For Navigating Complex Outsourced CIO Market

By Colin Rajala | September 5, 2019

Mark Titzer joined Dominican University as its v.p. for finance in May 2017 with an extensive to-do list from financial strategy and budgeting to rebidding all of its contracts and services. As more pressing day-to-day tasks and operational matters came across his desk, the task of rebidding contracts seemed to be falling down the pecking order like the stock market after an interest rate hike.

Titzer's staff of six had just as much on their plate and the task of rebidding its outsourced cio contract seemed years away, especially with the increased sophistication of investment portfolios and the complexity of outsourced cios and their various institutional models.

Those barriers led Titzer to contract a search consultant to help navigate the outsourced cio rebidding initiative of reviewing and evaluating the options available for a firm to manage its approximately \$35 million endowment.

"We didn't have the expertise or the time to do justice to the process," he said. "we knew we weren't going to be able to ask all the right questions and do a proper comparative analysis...It was a no brainer to work with a search consultant for the due diligence and independent review process." Titzer and his team are not alone, and with the outsourced cio industry expected to grow by 10.7% among nonprofits between 2018 and 2023, according to a report from Cerulli Associates on behalf of BlackRock, more foundations and endowments are likely to turn to search consultants to assist with navigating what can be a difficult evaluation and search process, according to investors.

"I think the prominence of outsourced cio search providers coincided with the growth of outsourced cios in the last six to seven years," said Frank Wilkinson, managing director of North American marketing at outsourced cio SEI Investments. "Then there were probably in the realm of 50 or so companies listing themselves as ocios and that has jumped to more than 80 currently. In the end, it is up to the institutional client to explore

their options, but that has become more and more difficult with so many variables and options available to them, so they have increasingly looked to outside help to assist in the processes."



Frank Wilkinson

Outsourced cio options can range from large multifaceted financial institutions with an investment function, to large investment consulting practices with an outsourced arm, to smaller boutique investment firms, and determining which model is the best fit for institutions is a key reason for the increased usage of search consultants.

InHub, which provides an online RFP technology, has found that greater than 60% of discretionary endowment and foundation RFPs on its platform have a search consultant running the process as opposed to the less than 20% that use a search provider when seeking traditional consulting services, according to Ariana Amplo, founder and ceo of InHub.

“Search consultants bring tremendous value to institutions and they are also forcing provider transparency, which we fully support.”

Frank Wilkinson, SEI

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Ariana Amplo

Beyond the variety of options and models for nonprofits to understand and traverse, the lack of resources, smaller staffs and infrequent board and committee meetings has also pushed some to utilize the search providers.

"They just can't do it themselves, they just don't have the bandwidth," said Tom Donahoe, managing director of outsourced cio search and governance at Manager Analysis Services. "There are many talented people on the committees and boards, but you only have a certain

amount of a governance budget or the time and focus to fulfill your fiduciary duty. If the committee members quit their day jobs, they would certainly be able to undertake a full-blown search by themselves. What they realize is that they can't quit their day jobs, they only meet about four times a year and they really can't respond as nimbly as a fiduciary as they would like.

Connecting With Search Providers

Foundation and endowment forays into the outsourced cio space have been most prevalent among institutions below \$500 million in assets, according to investors and allocators.

The average asset size of an endowment and foundation conducting a discretionary manager search on InHub's platform was just \$52 million in 2019 compared to approximately \$137 million in 2018, according to Amplo.

"As more smaller endowments and foundations adapt RFPs, there are more opportunities for managers to bid in a formal process for these. It is not only a process reserved for large accounts anymore," she said.

Investment advisor North Pier Search Consulting has worked with organizations with roughly \$25 million in assets, but finds its sweet spot to be those with assets of \$75 million to up to the high hundreds of millions, said Managing Partner, Founder and CIO James Scheinberg.

"We are focused on the small- and mid-sized organizations, frankly the organizations that originally would not have the ability to use the firms that charge more to do large ocio searches," said Larry Coats, Jr., president and ceo of ClearView Fiduciary Alliance, a membership-based service that facilitates the sharing and reporting of nonprofits' investment advisor and consultant results to help the institutions understand and analyze their investment programs. The alliance currently consists of 41 member organizations totaling \$1.2 billion in long-term assets with the members ranging in size from \$1 million to \$245 million in assets, according to Coats.

He noted that the organization only does searches for nonprofits that agree to be members of the organization, saying, "We want to see that they are committed not only to a project to find hopefully a good or better

advisor than what they have now, but we want to make sure they are doing that in the context of making a long-term commitment to be better fiduciaries and be better informed fiduciaries."

While smaller organizations appear to be the most prevalent user of the search provider resources, how the institutions connect with the providers is often by chance or through their small networks, according to investors and allocators.

"When you are doing a search for an ocio search provider, having to search for an ocio search firm is adding another level of complexity to the process and it doesn't really happen too often," said Chris Cutler, founder and manager of diligence and outsourced cio search at Manager Analysis Services. "What we are seeing, and we don't think this is efficient, is that people are approaching outsourced cio search providers because they are associated with a large brand or because of a personal relationship a board member already has with an outsourced cio search firm."

Dominican University's Titzer was not aware of what firms might be able to help with a search as he was looking to rebid its contracts. He was fortunate to come into a situation where the institution was working with an advisory firm, PlanPILOT, that was providing fiduciary advisory services for the university's 403(b) retirement plan.

The finance team was going through a set of quarterly training sessions with PlanPILOT's fiduciary team to make sure the team was meeting its responsibilities before he asked if they could, or knew anyone that could, help with an advisory search for its endowment.

"It was an off-handed ask if they do that type of work. It wasn't something we went after immediately," Titzer said, noting that PlanPILOT Managing Director Mark Olsen and Senior Consultant Frank Szymanek were thorough in their process and able to ask all of the right questions to align staff, trustees and its outsourced cio.

For institutions that are looking for search consultants or outsourced cio providers outside of their networks, a good place to start is attending industry events and conferences, according to CFO Jack Willoughby at the First Community Foundation Partnership of Pennsylvania. He noted that the foundation did not utilize a search consultant as part of its rebid process in 2017/2018 as he compiled a list of outsourced cios years in advance of the search by fielding calls from any and all providers to become familiar with the services and models available.

Through his own research he knew the various outsourced cio market segments and his organization's need for a firm with a strong research team. Willoughby asserts that nonprofits that are not familiar with the discretionary manager space should not be hesitant to identify an unbiased opinion to corroborate their own conclusions.

That sentiment was echoed by CIO Bruce Guiot of the Miami University Foundation (Ohio), which tapped Botanica Capital Partners to help conduct an invitation-only search for an outsourced cio that wrapped up last

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year.

"Most folks by then had heard of the ocio model, but did not fully understand what it means or certainly the ways it gets delivered," he said. "We needed someone to educate the board impartially...The consultant was initially brought on to evaluate the 'buy versus build decision.'"

Connecting with search providers is not reserved solely for institutions, as outsourced cios should also be networking with the search consultants to ensure they are aware of the discretionary firms' management team, processes and philosophies.

"As we have grown the business and expanded, we have broadened our sights of the [search] consultant market," said Matthew Wright, president and cio of outsourced cio Disciplina Group. "We brought on [Managing Director] Brian Arsenault to help those efforts and look at search consultants to understand who is in the marketplace and expand our reach to meet with them. Four or five years ago it was not something we focused on. Back then, opportunities surfaced from a committee or staff member who was going to lead the change and we would try and meet them or have someone set up an introduction."

SEI's Wilkinson noted that the outsourced cio firm has historically had resources dedicated to lead generation outside of traditional direct channels, such as referral opportunities, and it has been a natural evolution for them to focus on search consultants.

"We have a dedicated practice within our institutional group committed to serve as intermediaries between SEI and the search providers," he said. "They are independent of direct sales responsibilities and can focus on helping build relationships with search consultants. It was driven by the need to build relationships and drive education on who we are and what we provide."

As institutions and outsourced cios look to build connections with the search providers to help them navigate their search initiatives, the search consultants can distinguish themselves from peers through their own connections to the outsourced cios and qualitative information about the firms, according to Donahoe.

"When people do an outsourced cio search, they don't know the backstory for any number of the organizations," he said. "We differentiate ourselves in our intimate knowledge of these firms. Who is in the driver's seat? How long are they going to be there? What changes at the firm have occurred and what are their motivations? We incorporate these insights in our workings with the board so that they better understand what each firm has to



Matthew Wright

offer and to enable their decisions to be fully informed."

Search Consultant Processes

Many nonprofits, particularly on the smaller side, are board-driven or have a staff that is more administrative than investment-focused, which often means they do not have the requisite skills when it comes time to select an outsourced cio or evaluate performance, according to investors and allocators.

"These organizations are only sitting from their vantage point. They don't see the field like we do," North Pier's Scheinberg said.

Nonprofits have historically struggled with investment advisor RFPs because of the lack of requisite skills, according to ClearView's Coats.

"They didn't have a process, it wasn't logically established," Coats said. "They would call another organization that did an RFP in the last five years and say, 'would you give me a copy of what you send?'"

The inability and difficulties surrounding organizing and executing successful RFP processes has provided an opportunity for search consultants to show their value to institutional investors. Scheinberg finds that constructing an RFP, providing answers from respondents and constructing a scoring grid is "a baseline service that everyone should be doing."

"Having institutional quality oversight over the selection and monitoring of an ocio provider is critical to meeting the institution's financial goals and their fiduciary responsibilities. Retaining a search consultant, performing a thorough RFP and utilizing automated solutions are part and parcel of an effective governance process," said PlanPILOT's Szymanek.

The search processes often begin with search consultants focusing on the organizations themselves to get a better idea about their goals and missions and what they are looking to achieve from an outsourced cio relationship.

"It is similar to a marriage, we are trying to really understand the board, its investment philosophy and their specific goals and needs," Donahoe said. "We engage the members directly and work with them to verbalize and document what their ideal outcome would be."

Scheinberg said North Pier carries a similar approach, saying, "We spend a lot of time at the initial stages, not just getting to know the organization's needs, but we literally sit down and do interviews with every single committee member."



Tom Donahoe

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ClearView takes a varied approach in the early stages of the process, instead focusing on the institution's investment policy statement and addressing issues such as asset allocation, benchmarking, governance roles and responsibilities.

"One of the primary objectives of the investment policy statement is to clearly and specifically define and communicate responsibility, authority and accountability," Coats said.

From there the search consultant or institution will typically issue an RFP to potential candidates directly or to the broad market before beginning the difficult process of evaluating and consolidating responses.

North Pier aims to highlight the differences between the firms to the committee in order to drill down to a shorter list of finalists to present.

"We don't just hold a dog and pony show. We set the agenda and a recommended amount of time to address the different categories," Scheinberg said, noting that he and Senior Consultant Greg Metzger moderate the sessions and are active in asking questions of the presenters.

Manager Analysis aims to filter through the universe before issuing the RFP to help with alignment, according to Donahoe.

Following the RFP distribution, review and evaluation of proposals, the firm aims to narrow the list of proposals to around five finalists as they have shown they "can do what is required, will align with the board's goals, approach and personality, and are not conflicted in any manner," Donahoe said.

He noted that the firm will go through each potential provider with the board or committee to help them understand what each firm offers and what it is likely to excel at.

"Our manager analysis background brings an unusual set of talent to the due diligence of these outsourced cio firms," said Cutler, of Manager Analysis. "I have a strong capital markets background and reviewed over 2,000 alternative investment managers and the reason that is important is I can come into the meetings and understand whether the outsourced cio presentations are truthful and credible or not. The integrity of some of these marketing pitches really matches the integrity of derivatives marketing in the early 1990s. You really need to go through and conduct solid due diligence to understand the capabilities, strengths and weakness of these firms."

ClearView looks at the candidate pool in four groupings: the incumbent, other firms the organization has a business relationship with, providers recommended by board members based on experience at other organizations and, lastly, a list of organizations that submit data to ClearView on behalf of other member organizations. The firm then aggregates responses using the InHub eRFP portal and prepares a series of reports for committee members to review and score respondents on, according to Coats, who noted that the data is then used to facilitate a conversation

and coordinate which firms to bring in for finalist presentations.

Following finalist presentations, the institution is tasked with ultimately making the final selection and entering into the hiring and contract negotiation process.

"The ideal outcome is that five or more years in the future, when we have achieved a successful search, the committee is still with the same outsourced cio provider," Donahoe said. "...Not just because they've gotten good performance, hopefully top quartile, but because their goals and philosophies remain aligned."

He noted that institutions have increasingly looked to the search consultants to help with formalized reviews of the outsourced cios every five years or so.

Those periodic reviews can result in foundations and endowments conducting replacement searches, evidenced by 57% of organizations initiating or planning to conduct a replacement search since hiring their outsourced cio provider, according to the Cerulli report. Of the organizations that have completed the search, exactly half replaced their original discretionary manager, according to the report.

While a majority of North Pier's clients are looking at the outsourced cio space for the first time, the firm has begun to see an uptick in organizations conducting replacement searches as they have a better understanding of the services being provided and their respective needs, particularly when it comes to macro level issues, according to Metzger.

In looking at the outsourced cio market, Scheinberg said North Pier would not hire roughly 80% of the firms claiming to be an outsourced cio and that the remaining 20% can be broken out into various buckets based on liquidity appetites, size, style and ancillary services offered. The firm's research has found that many of the outsourced cio offerings coming from firms with traditional general consulting backgrounds will lag outsourced cios offering tactical investment strategy by about 120 basis points, according to Scheinberg.

"The research we have done in these different models have a very different return stream," Metzger said.

With the outsourced cio and search provider market flourishing, the cost of the searches comes into questions as everything has a price. Luckily for institutions, the cost to hire a search provider is not as daunting as it may seem.

The typical range for an outsourced cio search consultant can range between \$30,000 and \$75,000, with the pricing varying by organization as well as add-on expenses that arise during the process, according to Scheinberg, who noted that institutions need to ask the right questions and "try and nail down what your expenses are going to be." He also cautioned about selecting the wrong outsourced cio as it could cost an institution millions of dollars.

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"The fee from outsourced cio search firms will pretty much pay for itself," Cutler said. "Fees for the search and selection of an outsourced cio are not astronomical in any way. If you think of them on an amortized cost basis over the life by which you are going to keep an ocio, you are talking about a couple of basis points. We may have a dollar price that may look like a lot, but it's not really that much. If you think about how many outsourced cio managers we have met, spoken with and reviewed, you are talking about a huge amount of info you are already gaining access to."

Dominican University's Titzer said the search consultant contract price sealed the deal for his decision to hire PlanPILOT to help them rebid the outsourced cio services.

"There are tight budgets all around here and we don't have the luxury to spend more on third party firms without meaningful results... Even with us not making a change at all, it helped us align the portfolio and reduce costs. The way I look at it, you wouldn't begrudge a copay at the doctor's office for a checkup just like we didn't begrudge the fees to review our outsourced cio," he said.



Mark Titzer

Disciplina's Wright notes that while the cost for institutions to hire a search provider are not "prohibitive," it is another expense that they need to get accustomed to.

"To navigate the landscape, I think institutions need to see what is lost in the cost analysis," he said. "In that analysis the cost, whether it is real or mental, is the opportunity cost that is lost in the risk adjusted returns, which can be a large portion of an organization's operations and programs. Search firms should also aid with fee transparency or true cost. I think that once institutions overcome [that] there will be more growth for ocio search firms."

Search Consultant Concerns And Areas For Improvement

As asset management and investment consulting firms have recognized outsourced cio searches as another potential revenue stream, the firms have added the project-based capability to their businesses, which can lead to concerns of conflicts of interest. Those concerns surrounding search consultants are similar to the concerns of conflicts of interest among the outsourced cio firms they help identify and evaluate.

"I think the space is pretty fair and most search consultants are independent," Wright said. "For firms that are wedded to an asset management firm or consultant, the lines can be blurry. I know they say, 'we have a Chinese wall and no information goes to the other side of the business,' but the more independence and autonomy of firms, the better it is for the industry. We avoid conflicts in our own business by focusing on one line of

business and prefer search consultants that do the same."

Most investors noted that conflicts of interest among the search providers have not been an issue to date and continue to emphasize that these firms avoid any gray areas.

"There is still the potential for conflicts of interest where search providers also offer consulting or ocio-esque services, but by and large our experience has been positive in that the search consultants run fair, unbiased and independent processes," SEI's Wilkinson said.

He noted that the search provider space has also helped outsourced cios mitigate potential conflicts within their services or implementation by saying they "have helped clean up that muddiness."

"If you are a firm that has been reluctant or historically has avoided transparency, chances are now the search consultants will find out. They are asking additional and thorough questions, they are streamlining the process and helping to compare plans the same way, especially when it comes to fees," he said.

While search providers have helped clean up transparency, there are other facets of the space that they have identified as needing to be less opaque.

"A real limitation we have seen in the outsourced cio search space, and really across the industry, involves comparability of performance data," Cutler said. "There are no SEC compliance performance standards, so we rely less on reported historical performance than we would for other types of managers. We find many endowment and foundation industry benchmarks may be overstated so we try to overcome that with our superior analysis of the qualitative aspects of the firms and getting to know the personnel, how talented they are and how they manage the people and the other aspects of the processes"

The sentiment was echoed by North Pier's Scheinberg, who said that the ability to accurately evaluate outsourced cio performance has been a major problem.

"Left to their own devices, the ocio won't show data at a macro level," he said. "We have to create this data on our own. The industry has the tiger by the tail with this. There is a lot of shenanigans."

Taking steps to alleviate the issues, North Pier brought 15 of the top outsourced cio firms together to discuss some data reporting standards during a one-day working group in December 2018.

"We just think it's time," Scheinberg said. "There should be a standard. Organizations 10 years from now should have as easy a time identifying performance on an ocio firm as they do picking a large-cap growth firm out of Morningstar."

Outsourced cios that have looked to be ahead of the curve and open about transparency and performance include Strategic Investment Group,

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which claimed compliance with Global Investment Performance Standards (GIPS) in 2017. The firm's decision to become independently GIPS-verified stemmed from the growing demand for clear, quantifiable track records and to serve as a call to action to its peers to make accurate, appropriate information more accessible to institutions as they review search candidates.

Looking to add more transparency into the space, ClearView launched its Study of Investment Fees for Foundations, Endowments and Nonprofits earlier this year. The study, the results of which are expected to be released soon, was conducted to develop a baseline understanding and analysis of the current structure and levels of investment fees incurred by nonprofits with investment portfolios with assets less than \$500 million and identify the primary variables that impact the investment fees incurred.

Another area where search consultants can aid their nonprofit clients comes during the transition from one outsourced cio to the next.



Chris Cutler

"Transition management is an incredibly important part of the outsourced cio process because once a firm is fired and another is hired, there is a serious gap," Cutler said. "Foundations and endowments might do a good job finding the right outsourced cio manager, but end up with a bad transition management experience. It's always someone else's fault when something goes wrong with a transition."

Cutler noted instances of assets liquidated during a transition sitting in cash before being invested slowly over a period of time, which can result in "slippage" and an institution not being in compliance with their asset allocation goals and losing out on an opportunity to increase assets to use toward its mission.

"That slippage could be 30 basis points on your entire portfolio, or it could be conceivably as much as 70 or 80 basis points when things are really not going well," Donahoe said. "That is many multiples of the cost of doing a search itself."

As search consultants have made improvements on the quantitative side of their approach and processes, outsourced cios see room for improvement on the qualitative aspects of the search processes, according to investors.

Wilkinson has found that the search consultant-led processes have become more formal and structured in that the lines of communication are very rigid during the process. In his experiences the outsourced cio provider, investment committee and staff do not interact until very late in the search process, with it often concentrated into a two-hour finalist presentation.

"At the end of the day, this is a service industry and service industries are relationship driven... You have to get a feel for a firm to partner with over the next three, five, seven years, so a two-hour meeting is probably not the appropriate amount of time. Moving forward, search consultants can probably improve the process by finding touch points along the way for the cios and the organization to build relationships, which may help the process and the end decision ultimately," he said.

Another area that search consultants could improve on is easing rigidity in their qualifications and thresholds for the discretionary managers.

Wright noted that when he started Disciplina after managing Emory University and Vanderbilt University's endowments, outsourced cios said the biggest constraint on business will not be size or assets under management but the number of clients.

"I think that search consultants should factor that into their processes more. The larger outsourced cios in terms of assets, number of clients, are very different from the boutique and niche shops like us," he said. "The larger size, capacity and scale can lead to diminished returns because the service model and returns may get diluted with size."

Ultimately, the shortcomings of search consultants are outweighed by the benefits they provide to understaffed, resource-constrained nonprofits as they are "satisfying a real need in the marketplace" and compensating for the "deficiencies in the governance budget" through their formulation of goals and philosophies, RFP construction, distribution and evaluation, according to Donahoe.

"It is pretty clear that search consultants are here to stay," SEI's Wilkinson said. "They bring tremendous value to institutions and they are also forcing provider transparency, which we fully support... They are asking additional and thorough questions, they are streamlining the process and helping to compare plans the same way, especially when it comes to fees."

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