The Board's Role in SUPERVISING INVESTMENTS Three Must-Dos

The legal responsibility for supervising investments resides squarely with the board of directors. Whatever authority other parties may have to influence or implement investment decisions, such authority ought to be shaped, guided, and constrained by the oversight of an informed board.

The fundamental challenge for board members is to balance their legal responsibilities against the organization's practical needs. The executive staff is almost always responsible for daily operations, with the CEO or, more commonly, the CFO handling investment operations, including the supervision of outside service providers. But as much as the board depends on the executive team's service, the board may not abdicate its responsibility to supervise.

Good policies help maintain the right balance. With effective policies and procedures, a board can be very active in supervising investments while still delegating authority, encouraging teamwork and community spirit, and articulating a common vision.

There are three actions board members must take to discharge their legal and fiduciary responsibilities — as well as to build a structure that will best promote the organization's investment goals. The laws governing fiduciary investing now clearly provide that when a board takes these three steps, neither the organization, nor the individual board members, shall be liable for the actions of those to whom they delegate, nor for investment losses.

1. ADOPT INVESTMENT POLICIES.

The primary role of policies is to help everyone remember what the board has decided should be done. Written policies help everyone — board members, executive staff, and outside advisors — understand the organization's investment goals and the risks the organization is willing to take to achieve those goals. Since perfection is not required, the first step is to adopt a policy and live with it for a while. You can always make changes based on your experience.

To get started, the board should ask — and answer — the following questions:

- What assets are available to be managed?
- What are our investment goals, time frames, and restrictions?
- What is our tolerance for risk?
- How do we recognize risk?
- What structures and policies need to be created to reach our goals?

2. HIRE ADVISORS.

Although the board should not be choosing among specific investments (everything from stocks and bonds to hedge funds and other, alternative investments), someone has to do it. Delegating this responsibility to someone else is not only permissible but preferable, assuming that the board is conscientious and careful in its choice.

3. REVIEW PERFORMANCE.

Hiring an investment advisor is not a one-time event. The board's legal responsibilities are not discharged unless the board, or its investment committee, regularly reviews the advisor's work and the organization's adherence to established policies in a disciplined manner. This is so central to sound investing that any qualified advisor should present a recommended review process as part of the package of services. (If the advisor does not recommend regular reviews, place one hand on your wallet and back slowly out of the room!)

The good news is that these three actions represent a major portion of a board's duties in supervising investments. Adopt policies, hire an advisor, delegate supervision to an investment committee of the board, review, and repeat as necessary. None of this is conceptually difficult. After the board has taken care of the basics, its job is to support the organization's staff, members, beneficiaries, and investment advisors by standing firm in its decisions and giving the basics time to work. This means, among other things, having the courage to stick to your guns during tough times, resisting impulsive policy changes, and refusing to allow the occasional downturn in results to cause hurried changes in allocations.

THE ROLE OF AN INVESTMENT COMMITTEE

While the ultimate responsibility for the health and well-being of the organization rests with the board, most boards delegate the actual authority over more complex operations to committees or to its executive staff. This is often the case with investments.

An investment committee is, typically, a smaller committee of board members that also may also include additional non-directors as committee members. While there are many variations of how investment committees are established, it is not uncommon for the nonprofit's chief financial officer to chair the committee and to act as a conduit between the committee and those delegated to do the actual work. Under most state corporation laws, a board can delegate its authority to properly constituted committees. Therefore, an investment committee can largely serve in the board's place in supervising the investment process. In fact, BoardSource advises that board members should supervise and not actually manage funds themselves. Direct management by board members effectively eliminates independent supervision. The reason to stress the role of an investment committee is that it facilitates the supervisory process by allowing the work to be done by those board members who have the time, interest, and knowledge that such supervision requires.

The committee will typically receive and review the performance reports submitted by staff and outside advisors, meet quarterly (or at least annually) with the primary consultant and participate in other meetings or reviews as needed. How active the committee might be will depend on the size of the organization, the complexity of the investments, and the presence or absence of internal staff available to assist. In doing this work, the committee is satisfying the prudent-investor requirement of ongoing supervision of outside advisors and is thereby protecting both the organization and the other directors from liability.

Adapted from *Who's Minding the Money: An Investment Guide for Nonprofit Board Members*

Additional resource:
The Nonprofit Policy Sampler