

UUA Investment Committee – Minutes

Walden Asset Management
One Beacon St
Boston, MA 02108
August 10, 2011

Members Present: Jim Sherblom *Chair*, Julie Skye, Arnold Bradburd, Dan Brody, Clyde Grubbs, Carol McMullen, Tim Brennan

Guests: Jerry Mitchell, Jeane Pupke, Charles Sandmel, Lucia Santini, Will Saunders, Craig Scholl

Staff: Rachel Daugherty

NEPC: Scott Driscoll, Doug Moseley, Scott Perry

1. Minutes from meeting of May 20, 2010

Motion: Moved McMullen, seconded Sherblom, approved. Minutes adopted without amendment.

2. UUCEF Performance Review – Moseley, Driscoll – NEPC

- 2nd Quarter Market Observations and Opportunities
 - 2nd quarter was dominated by macro-economic concerns, particularly slow US growth and European debt crisis.
 - Immediate risk-reduction does not need to be pursued, but a risk-balanced approach to asset allocation remains paramount.
 - Opportunities for high risk-adjusted returns exist in pockets of the capital markets.
 - Market volatility must be expected as a more regular event that what we saw in the past.
- 2nd Quarter 2011 Plan Review
 - Year to date the Endowment is up 4.8%
 - The trailing one-, three-, and five-year returns, +22.7%, +6.9%, and +6.5% ranked in the top quartiles of their peer group.
 - We are also performing well against total endowment universe, not just the custom universe (\$50 to \$100 million). Large endowments have trailed smaller endowments because private equity has trailed public markets. Over 10 years their returns have converged.

2. SRI Research and Analyst – Brennan

- As discussed at prior meetings, we believe that another SRI research firm could better meet our needs. We have received strong proposals from two firms: Jantzi Sustainalytics and IW Financial. The reports produced by the consultant will assess companies' social performance and assign scores based on the UUA's social criteria. Rhumblin Advisors, which makes the greatest use of the data, has reviewed sample reports and talked to each

firm. They believe both firms meet their needs. Fees are roughly the same and no more than our current provider.

Motion: The treasurer is authorized to select from the two firms under consideration an SRI research firm to help guide security selection for the Fund; and further, the treasurer will consult with Glenn Farley of the CSRI before making a selection. Moved: Bradburd; seconded: Skye; motion passes.

Action item: Brennan will circulate information to the committee about the selected firm.

3. Review of UUA's and committee's mission and purpose – Brennan and Sherblom

- Brody: There are two different models: 1st is that endowment is tool to generate funds to advance the mission. 2nd is that endowment provides resources to support mission while reflecting values. The UUA Board leans towards latter.
- Sherblom: It's a question of keeping things in balance. As trustees get clearer about the "single bottom line," that has effect on membership of committee and how we select managers. We need experience at the table and we must also work extra hard to find balance with multicultural multigenerational challenge.

Action item: McMullen and Brody will work together to draft a mission statement for the committee.

4. Liability insurance for committee members – Brennan

- The UUCEF had been insured through Church Mutual (CMI). They do a great job with congregations, but may not be equipped to deal with an entity as large and complicated as the UUA. We engaged Risk Strategies review our coverage and make recommendations. On their advice, we have moved this coverage to Chubb and increased the coverage to \$5 million.
- McMullen: Every member should get a copy of the policy and have it looked over by his/her own advisor. In addition, each member needs to carry his/her own insurance.

Action item: Brennan to research indemnification of committee members.

5. Legal structure of the UUCFE – Brennan

- Right now the UUCEF is part of the UUA. What that means from a liability perspective is that if the UUA were subject to a large liability claim, the court could go after the assets of the congregations in the UUCEF. This issue was raised by counsel, therefore a disclosure was included in the risk factors. In addition, our auditors have recommended that we consider a separate legal structure.

- Legal counsel now recommends that the new entity be organized as a charitable organization as determined by the IRS. Our auditors told us that the audit would cost nothing extra because the financials would be presented on a consolidated basis. The one difference is we would have to file a 990, which they estimate would cost \$7-\$12K.

Motion: To urge the UUA board of trustees to move forward to set up the UUCEF as a separate legal entity organized as a nonprofit charity under IRS rules, as long as the cost to the UUCEF doesn't exceed 3 basis points. Moved: Sherblom; Seconded: Bradburd seconds; motion carries.

Action item: Brennan and Brody will work through the implications of setting this up as a separate entity by June 30 2012

6. Criteria for IC selection - Sherblom

- Sherblom: Under the bylaws the committee has 7 members, 3 of whom are designated because of their positions: the treasurer (Brennan), Financial Advisor (Brody) and Board Liaison (Grubbs). The concern from a fiduciary point of view is that when you don't want a big committee and three are designated without regard to their financial experience, it puts a greater weight on those who have experience.
- Brody: We need to consider the implications of policy governance. The Board is looking at committees in binary way: does it advise the board or the president? The board's consultant says the IC looks more like staff work and that the UUA does not need a committee appointed by the Board. However, other endowments do not do it that way. He believes that in the end the Board will follow the precedent of the Retirement Plan committee and take responsibility for making the IC appointments.
- McMullen: There is an important line between an active manager of portfolios and someone who understands structure, strategy and process. This is not gained by picking stocks, but by sitting on boards.
- Scholl: The statement of qualifications used in 2007 is as follows:
Committee membership should make every effort to reflect the diversity of membership and views within the UUA and investor organizations. The Committee seeks to include members with knowledge of UUA priorities, programs and communities and socially responsible investment practices. In addition, a majority of committee members should have direct professional institutional investment experience. This experience would typically be gained as an investor, consultant, money manager or lawyer specializing in institutional fiduciary issues. The investment professional or legal experience should include involvement as an investor for an organization with more than \$100 million to invest or as a service provider to funds with more than \$100 million under management. Investment professionals will be in positions where their peers

would typically hold or supervise professionals who are Chartered Financial Analysts, a designation from the CFA Institute.

- Bradburd: Committee should review and update statement of committee member qualifications.

Action item: Once the committee agrees on language, the IC will recommend to the board the qualifications for membership on this committee and that they incorporate this into governance policy.

7. World Capital Markets Investable Universe – Moseley

- Moseley presents NEPC’s analysis of the total investable assets in the world. This has implications for the UUCEF asset allocation policy, but should not be viewed as determinative. Analysis does not include derivatives, which are becoming more important.
- Mitchell: Larger endowments use overlays and derivatives.
- Sherblom: We should address these questions: how do we think about GAA managers? Should we be rethinking hedge funds? Should we have a dedicated allocation to real estate?
- Santini: We sometimes focus too much on market cap instead of global share of GDP.
- McMullen: This helps in identifying large shifts, e.g. when oil sector rose from 6% to 20% of the benchmark. Issue is magnitude and direction. Then you can be explicit about where you’re willing to deviate.

8. Implications of NEPC’s Analysis for Our Portfolio – Sherblom

- Sherblom: If we look at alternatives where we have 25% with GAA managers and a hedge fund, we have made a big commitment to alternatives. This is similar to the largest endowments, but not mid-sized endowments.
- Santini: thinks of alternatives as less transparent and less liquid. GAA is not “alternative” in the sense that the term is usually used.
- Mitchell: Unless you can get the very best managers, don’t do private equity.
- Sherblom: GAA managers are not adding return, but they lower volatility.
- Doug: GAA gives access to some investment categories for which we wouldn’t want to have a dedicated manager. Also it gets away from style box mandates and gives managers more flexibility. NEPC believes there is a premium for investing in private vehicles with less liquidity. If we consider private equity, probably a fund of funds, it would take 5 to 8 years to achieve exposure.
- McMullen: This is a client/business communication issue. It is important to better understand the values of our investors. I survey 100% of clients annually.
- Charles: From my experience, most important is preservation of capital, values, return.
- Santini: UUA website should be a financial education resource.

- Skye: Concerned about bond mutual funds in a rising interest rate environment.
- McMullen: need to think about the number of managers. “Manager creep.” Moseley says we are close to the high end of number of managers for our size.
- Mitchell: over time managers do not add return. Emerging markets are 80% correlated to large cap US equities. So even if our asset allocation is wrong, it won’t be wrong by much.
- Grubbs: Advanced economies are not growing. It would be wise to think about restructuring.

Action item: Santini, Skye, McMullen will come up with articles for an online resource.

Action item: Do a survey in 2012 that would ask congregations about what their priorities are.

9. Major items to consider in upcoming year - Sherblom

- There’s no reason to radically rethink the allocation targets, the committee is comfortable where we are.
- Scholl: On the equity side, consider use of alternatives to market cap weighted benchmark. Use risk-adjusted return, equal weight, etc. (NEPC will present alternatives to market cap weighted benchmark.)
- Sherblom: over the next year, the committee should address the following:
 - a) Number of managers. Look at equity managers. Should Rhumblin be core or maybe all cap?
 - b) International: should we have four managers? Would we do just as well with three? Believes that in the future the line between emerging and developed will blur.
 - c) Look again at GAA managers.
 - d) Review of fixed income managers.