Mission & Governance Challenges

Boards consistently coming up short...

- **Scant time and attention**: many boards meet only infrequently.

- **Focused on the wrong thing**: 70% look more at managers than the allocation, when over 90% of the return is driven by the allocation.

- **Most challenged by** difficulties with board oversight and execution.

- **Confused by** the overwhelming number of investment options and approaches in the market.

- **Must address** competing interests ranging across members, donors, beneficiaries and the community at large.

- **Mission-driven investments**: over half don’t know where to go next.

In our study, over 60% of organizations performed below the average, and the average wasn’t very good.

The best-governed organizations outperformed their peers nearly two to one over a five-year period.

Mission & Governance
What are the ingredients for an effective board and organization?

**Structure**
- Professionalism
- Composition
- Engagement
- Staff / consultant
- Institutional knowledge
- Diligence
- Transparency

**Human Factors**
- Leadership
- Culture and trust
- Individual competencies
- Experience
- Diversity
- Group dynamics

**Group Processes**

**Board Tasks**
- Mission and planning
- Financial stewardship
- Human resources
- Performance monitoring & accountability
- Risk management
- Community representation & advocacy

**Board Competencies**
- Board development
- Board management
- Decision-making

FEQ™ = Structure + Process + People

Mission & Governance
Board Assessment

<table>
<thead>
<tr>
<th>Key Dimensions</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Quick check</td>
</tr>
<tr>
<td>• Board structure</td>
</tr>
<tr>
<td>• Board and org. culture</td>
</tr>
<tr>
<td>• Board responsibilities</td>
</tr>
<tr>
<td>• Board process</td>
</tr>
<tr>
<td>• Governance quotient</td>
</tr>
</tbody>
</table>

**Highlights**

- Areas of strength
- Areas for improvement
- Divergent views
- Gaps in knowledge
- High priority items
- Overall effectiveness

---

**Mission & Governance**

**Board Assessment**

---

**GSAC Comprehensive Report 2018 - U.S. Governance Survey**

**A. Governance Effectiveness**

- Good board orientation
- Board plans direction
- Evaluates EQ plan
- Financially sound
- Board/EAD roles clear
- Resources used efficiently
- Board has high credibility
- Board is committed
- Board is competent
- Board is conflictual
- Board reviews effectively
- Board has high consistency
- Board is collaborative
- Board understands position
- Board is knowledgeable
- Board is prepared
- Overall effectiveness

---

**Quick Check Report**

<table>
<thead>
<tr>
<th>No.</th>
<th>Statement</th>
<th>Low</th>
<th>High</th>
<th>Avg</th>
<th>Legend</th>
<th>Poor Avg</th>
<th>Average Avg</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>This organization’s orientation for board members accurately portrays their roles and responsibilities</td>
<td>2</td>
<td>5</td>
<td>3.6</td>
<td>Positive</td>
<td>3.6</td>
<td>3.6</td>
</tr>
<tr>
<td>2</td>
<td>This board is currently involved in planning the direction and future focus for the organization</td>
<td>4</td>
<td>5</td>
<td>4.7</td>
<td>Positive</td>
<td>4.7</td>
<td>4.7</td>
</tr>
<tr>
<td>3</td>
<td>The board does an excellent job of evaluating the performance of the chief executive (CEO), CFO, COO, Treasurer or Executive Director</td>
<td>3</td>
<td>5</td>
<td>4.5</td>
<td>Positive</td>
<td>4.3</td>
<td>4.3</td>
</tr>
<tr>
<td>4</td>
<td>This organization is financially sound (assets are balanced)</td>
<td>3</td>
<td>5</td>
<td>4</td>
<td>Positive</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>5</td>
<td>Board members demonstrate clear understanding of the respective roles of board and other personnel (CEO, COO, CFO, Treasurer or Executive Director)</td>
<td>4</td>
<td>5</td>
<td>4.2</td>
<td>Positive</td>
<td>4.2</td>
<td>4.2</td>
</tr>
<tr>
<td>6</td>
<td>The organization’s resources are used efficiently (good value for money spent)</td>
<td>4</td>
<td>5</td>
<td>4.5</td>
<td>Positive</td>
<td>4.3</td>
<td>4.3</td>
</tr>
<tr>
<td>7</td>
<td>The board has high visibility with key stakeholders (e.g. voters, donors, beneficiaries, investors, taxpayers, etc.)</td>
<td>2</td>
<td>5</td>
<td>3.6</td>
<td>Positive</td>
<td>3.5</td>
<td>3.5</td>
</tr>
</tbody>
</table>

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**Mission & Governance**

*Frequently asked questions (FAQs)*

*How often should my organization conduct a board assessment?*
Recommended once per year, but at least every two years, as boards regularly turn over members.

*What are the benefits of board assessment?*
Clarify mission & objectives of the organization. Identify board strengths, areas in need of improvement, knowledge gaps, priority items and areas of commonality and disagreement.

*Isn’t this a huge commitment of time and resources?*
Our online self-assessment tool is easy to administer, and concisely reports actionable results. The survey, while in-depth, only take about 45 minutes to answer, and can be completed on a smart phone or tablet. There is also a short-version of the survey available (Quick Check). The organization can also selectively include key staff along with board members.
Governance Portal

- Dedicated client portal with convenient access
- Easy-to-administer
- Secure
- Immediate results
- Sophisticated reporting
- Ongoing tracking for trend analysis
- Usable from a computer or mobile device

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Portal: Two Views

Admin View

- Client creation
- Data collection
- Reporting and data export for analysis

Client View

- FEQ – Senior leader response
- GSAC – Self-administration
- Reporting

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Client Use

Attached are several documents related to this survey article from Benefits Magazine that discusses the research efforts of firm Fund Governance Analytics (FGA). One of the studies examines the relationship between measures of fund governance and investment performance.

The next document is the survey instrument that was used for the assessment. I completed the survey on behalf of MCERA to generate a FEQ score. I believe this result confirms what all of us know, the importance of good governance of the organization. We should all be extremely proud that it supports not only what we all believe, but that also shows how MCERA is doing.

Your organization’s FEQ score is 68.98. This places you in the first quintile among the U.S. Public Pension peer group.
Fund Governance Assessment System™ (FGS)

Module 1: FEQ™ – Board Structure Review

Module 2: GSAC – Board Process Review

One-of-a-kind, governance benchmark database allows peer and universe comparisons.

System designed to collect data on 182 governance attributes.
Module 1: The FEQ™ - Structure Review

1) Professionalism
2) Board Composition
3) Engagement
4) Staff
5) Institutional Knowledge
6) Due Diligence
7) Transparency

Data collected from the organization’s most senior staff member in typically less than 30 minutes.
Additional Benchmarks

1) Use of Policies
2) Board Training and Development
3) Board Diversity
4) Compensation
5) Professional Experience
6) Self-assessments
Other Crucial Data

1) Market Value of the Assets
2) Investment Returns
3) Funding Ratios
4) Investment Expenses
5) Asset Allocation
Module 2: The GSAC - Process Review

- Exhibit good criterion-related validity related to external and internal ratings of organizational effectiveness.

- Able to discriminate between stronger and weaker aspects of board functioning.

- Established a high degree of correlation between scores on the Quick Check and the other 11 subscales and the Governance Quotient.

GSAC Key Dimensions

1) QuickCheck

Data collected from board members, senior staff and the chief executive.

QuickCheck takes less than 15 minutes to complete.

Full assessment in 45 minutes or less.

2) Board Structure

3) Board / Organizational Culture

4) Board Responsibilities

5) Board Processes

6) Governance Quotient
Public Pensions Results

Public Pension Fund Performance by FEQ™ Quintile, 5 YR Average*

Average 5 YR Return is in percent, the FEQ™ is in standardized governance units and the Bond Yield Spread Index is basis points adjusted (divided by 10) to maintain the scale.

*Based on the work, Asset Owner Governance and Fiduciary Effectiveness: The Case of Public Pension Funds, by Christopher K. Merker, Ph.D., CFA, ©2017, Marquette University (2008-12)
Public Pensions Results

Average of Top Five and Bottom Five Public Pension Plans as Ranked by 5 YR Investment Returns*

Average 5 YR Return is in percent, the FEQ™ is in standardized governance units and the Expense Ratio is in basis points.

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*Based on the work, Asset Owner Governance and Fiduciary Effectiveness: The Case of Public Pension Funds, by Christopher K. Merker, Ph.D., CFA, ©2017, Marquette University (2008-12)
Governance Explanatory Power

*Based on the work, Asset Owner Governance and Fiduciary Effectiveness: The Case of Public Pension Funds, by Christopher K. Merker, Ph.D., CFA, ©2017, Marquette University (2008-12)

*McFadden Pseudo R-squared. High values in the 0.20-0.40 range. Model was 93% predictive.
Higher Ed Results

R² was same value as with our original study of public pensions.
Interpretation: 1 unit increase in the FEQ, 0.29% increase in annual return.

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Source: FGA-Commonfund 2021 Study of Governance in Higher Education. Average annual returns are shown for the four year period 2017-2020.
Governance Summary

• Top FEQ organizations outperform their peers 2 to 1.
• Top FEQ organizations see more consistent performance outcomes.
• The FEQ is 93% predictive of sustained funding.
• Top FEQ organizations see lower bond yields.
• Positive change in 12 months

Ten unit increase in the FEQ

• 360 bps increase in annual return
• $37 mm decrease in annual required contribution

*Based on the work, Asset Owner Governance and Fiduciary Effectiveness: The Case of Public Pension Funds, by Christopher K. Merker, Ph.D., CFA, ©2017, Marquette University
## U.S. Public Pension Survey

<table>
<thead>
<tr>
<th>Topic</th>
<th>Finding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Self-assessment</td>
<td>A vast majority of organizations indicated they conduct governance self-assessment either infrequently or not at all.</td>
</tr>
<tr>
<td>Use of investment policies</td>
<td>Nearly 80% of organizations are using some form of investment policy.</td>
</tr>
<tr>
<td>Review of policies</td>
<td>Typically reviewed every year or two.</td>
</tr>
<tr>
<td>Diversity</td>
<td>Women, while in the minority, are still better represented than minorities, which tend to be a low percentage of board composition.</td>
</tr>
<tr>
<td>Compensation</td>
<td>Only about a quarter of organizations see some form of board compensation for service.</td>
</tr>
<tr>
<td>Training</td>
<td>Most conduct some training, typically on an annual basis.</td>
</tr>
<tr>
<td>Background in investments</td>
<td>While half believe they have a medium to high level of professional experience on the board, at least a third of all boards also say they have low representation of skill and experience on the board.</td>
</tr>
<tr>
<td>Expense</td>
<td>A wide-range of investment expense structures exist.</td>
</tr>
</tbody>
</table>
Now Available -

The Trustee Governance Guide: The Five Imperatives of 21st Century Investing

Over 80% of the financial assets in the United States fall under the purview of a trustee. That’s a big responsibility for an estimated 1% (around 1.5 million people) of the U.S. working population charged with overseeing investments for millions and millions of beneficiaries, corporations, public sector and non-profit organizations. In a world proliferated by investment products, increasingly dominated by indexes, faced - particularly in the pension world - with increasing liabilities, more regulation and a growing number of social and sustainability objectives, what's a trustee to do?

The Trustee Governance Guide is here to help guide today’s board trustee through the brave new world of 21st century investing. The Guide focuses on the critical aspects of the Five Imperatives: Governance, Knowledge, Diversification, Discipline and Impact.

Based on over a decade of research, practice, and discussions with many key decision makers and influencers across the industry, this book addresses the many topics related to better governance, greater mission-driven, financial performance and impact. The questions the book addresses include:

• What is good governance, how do we know it when we see it and why does it matter?
• How much knowledge is necessary to be a competent board member?
• Why should board self-assessment become a standing, annual review item?
• As a board, where should our time be spent to be most effective?
• What are the key elements of a diversified portfolio?
• What's the difference between socially responsible and ESG investing?
• Can I focus on sustainability and still be a good fiduciary?

This book will provide a way for boards to improve and benchmark their own governance performance alongside their peers, and uniquely covers related investment topics in each chapter.

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Praise For -

_The Trustee Governance Guide: The Five Imperatives of 21st Century Investing_

“Trustees in the modern world are faced with an ever-changing investment environment. Now more than ever a guide to governance is essential reading for them. This book is structured in a very simple, intuitive fashion to help trustees easily research topics that may challenge them during the discharge of their responsibilities. I found the fifth imperative, Be Impactful, particularly useful as it deals with the biggest challenge that investment professionals face today: what is the purpose of finance? The answer to this question lies at the very heart of what it means to be a trustee.”
—Paul H. Smith, President & CEO, CFA Institute

“This book provides a thorough, accessible and practical guide for trustees and staff that have the honor and the responsibility of stewarding long-term capital for a non-profit institution or pension. Authors Christopher Merker and Sarah Peck advance the investment governance field by making an informed and strong case for understanding ESG as a risk management issue and by introducing a Fiduciary Effectiveness Quotient assessment tool. Investment stewards that want to understand and follow best practices will benefit from reading this book.”
—Cathleen M. Rittereiser, Executive Director of Commonfund Institute and co-author of _Foundation and Endowment Investing_

“Finally, a book that demonstrates empirically what many practitioners have long believed to be true: board governance can significantly enhance investment returns. In addition to showing the importance of good governance, the authors also outline the key attributes of a superior governance structure, and how any board can improve its governance structure. The five imperatives, outlined herein, offer an accessible guide to improving board governance and performance. The Trustee Governance Guide should be required reading for all trustees and trust executives.”
—James Wilbanks, Executive Director, Mendocino County Employees Retirement Association

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In Conclusion

Good governance by institutional fund asset owners (pensions) makes a significant incremental difference to value creation as measured by their long-term risk-adjusted rate of return . . . Funds can create more value if they correctly assess their governance and determine an investment strategy commensurate with their capabilities.”

- Gordon L. Clark and Roger Urwin

Governance and leadership are the yin and the yang...without governance you risk tyranny, fraud and personal fiefdoms. If you have governance without leadership you risk atrophy, bureaucracy and indifference.

- Mark Goyder
Appendix
About Fund Governance Analytics, LLC (FGA)

Founded in 2017, FGA is the ESG research, education and technology transfer partnership of Marquette University. A research and technology partner to leading global organizations such as Commonfund Institute, CFA Institute and Nasdaq, FGA has conducted groundbreaking research in ESG data analytics, corporate short-termism and asset owner governance, and has played a critical role in the development of Global ESG Investment Product Disclosure Standards (CFA ESG Working Group) and ESG certification (CFA ESG Investing Certificate Program). FGA’s work has been cited in documentation and policy recommendations to the Securities & Exchange Commission’s (SEC) Asset Management and ESG Subcommittees.
Christopher K. Merker, Ph.D., CFA

Christopher K. Merker, PhD, CFA, is a director with Private Asset Management at Robert W. Baird & Co. He holds a PhD in investment governance and fiduciary effectiveness from Marquette University, where he has taught the course “Sustainable Finance” since 2009. Executive director of Fund Governance Analytics (FGA), an ESG research partnership with Marquette University, he is a recent member of the CFA Institute ESG Working Group, an international committee developing ESG investment product disclosure standards, publishes the blog, Sustainable Finance, which covers current topics around governance and sustainability in investing, and is co-author of the book, The Trustee Governance Guide: The Five Imperatives of 21st Century Investing.
Sarah Peck, Ph.D.

Associate Professor of Finance at Marquette University, Dr. Peck is the co-inventor of the Fiduciary Effectiveness Quotient (FEQ)™. Her research interests are in the area of ownership structure, leveraged buyouts, board of directors, and other topics in corporate governance. She has published in the *Journal of Financial Economics*, *Journal of Corporate Finance*, *The Journal of Forensic Accounting*, among other journals in finance and accounting.

She serves regularly as a speaker and panel participant in the area of ethics, divestment, and socially responsible investing. From 2007 to 2014, she was a trustee for the Milwaukee County Pension Board with over $1.8 billion in assets, and Chair of its Investment Committee. Dr. Peck served as Department Chair from 2004 to 2014. She is member of the American Finance Association, The Financial Management Association, The American Finance Association, and the CFA Society Milwaukee.