Children & Families
Commission of Orange County

Agenda Item No. 9
July 3, 2013 Meeting

DATE: June 18, 2013

TO: Children and Families Commission of Orange County

FROM: Christina Altmayer, Executive Director Christina Altmayer

SUBJECT: Investment Policy and Fiscal Sponsorship

SUMMARY:

Consistent with the Bridgespan Group recommendations, the Commission has increasingly worked to shift its portfolio from sustaining programs to catalytic investments. The objective of the catalytic funding was to make one-time investments that would secure critical community services for approximately 10 years. Catalytic investments have some inherent level of risk as the Commission makes payment in advance of services rendered. To mitigate this risk, the Commission's catalytic agreements include specific security provisions such as liens against capital projects, letters of credit and/or use of a fiscal sponsor responsible for maintaining, investing, and disbursing funds to the funded agency consistent with the contract terms.

The reliance on a fiscal sponsor has been used for several catalytic investments, including HomeAid Orange County's Emergency Shelter program and The Center for Autism and Neurodevelopmental Disorders. Recently, the Commission has been challenged to identify a cost-effective fiscal sponsor that can comply with the Commission's investment policies. This report provides a summary of the challenges specific to utilizing a fiscal sponsorship model to secure catalytic funds and potential options to address these challenges. This discussion is relevant to the current catalytic investment with Healthy Smiles as well as potential future catalytic investments.

BACKGROUND

The catalytic investments were successful in allocating Commission funds to secure investments for young children, making impactful system changing investments, and providing long term support for priority Commission initiatives. To meet these priorities, the Commission staff worked with outside counsel and the grantees to structure the catalytic agreements to include two options for the disbursement of funds:

1. **Engaging a fiscal sponsor** who will receive the Commission funding on behalf of the grantee and distribute the funding to the grantee in accordance with the schedule, budget, and scope of work defined in the agreement. The agreement provides the fiscal sponsor with two options for fund management: 1) invest in accordance with the fiscal sponsor's own investment policy, but requires the fiscal sponsor to guarantee against any loss to the principal of the grant; or, 2) invest in accordance with the Commission's investment

policy, in which case the fiscal sponsor would not be liable for any investment losses against the principal fund balance.

2. **Submitting a form of security against the grant**, such as a letter of credit in the amount of the grant, or placement of the Commission in first position on a deed of trust. The security is retained by the Commission until the service payback requirements have been completed.

In the event that neither of the above options can be satisfied, the Commission can choose to move forward with a standard cost-reimbursement agreement. Currently, Healthy Smiles is drawing against their catalytic investment through a cost-reimbursement agreement in which a grantee incurs the expenses to operate the program and then receives reimbursement from the Commission.

Utilizing a fiscal sponsor has been increasingly challenging for the Commission as the anticipated partners, such as foundations, have been unable to comply with one of the two fund management options listed above. Commission staff has recently solicited input from foundations and other non-profit agencies to better understand the barriers for fiscal sponsors. From these conversations, it has become clear that limitations on the percentage of specific types of investments and requirements for the mandated diversification of maturity dates are the primary barriers. These limitations would require additional fund management that is not typical for foundations or the brokers/dealers they use to manage the foundation investments. Therefore, even when a foundation is willing to serve in this capacity, once they evaluate the costs to manage the Commission catalytic funds, it becomes cost prohibitive to do so.

OPTIONS FOR CONSIDERATION

After reviewing the Commission's security requirements and the barriers to executing these fiscal sponsorship agreements, staff has proposed two alternatives that could be examined further and provide potential alternatives that might offer a more cost-effective solution. Each of these options is described below.

Option 1: Allow waivers or exceptions to portions of the Commission's Investment Policy, consistent with the government code, in fiscal sponsorship agreements

The Commission's current contract requirements could be modified to allow for exemptions or waivers from the approved investment policy, allowing specific types of investments when deposited with a private entity through a fiscal sponsorship agreement. The fiscal sponsor would be limited to specific investments defined in a modified policy, but restrictions such as the number of maximum days to maturity and maximum percentage of types of investments and issuers could be adjusted. The adjustment would allow fiscal sponsors to invest in longer-term securities and not require the same level of diversification as maintained by the Commission. The costs of investing would be reduced for the fiscal sponsor by not actively managing an entire investment portfolio but holding a limited number of investments with maturity dates matching cash flow needs. Any investment gains or losses would be absorbed by the fiscal sponsor or funding recipient. Prior to implementing this change, the Commission would work with the Commission's on-call financial advisor to develop the specific waivers or changes to specific portions of the Commission’s investment policy for fiscal sponsorship agreements. Any changes or modifications to the investment policy would still require compliance with applicable government code.

Option 2: Create a special fund under the management of the County Treasurer
California state law allows local agencies and Joint Powers Agency consisting of at least one public agency from within the county to voluntarily participate in the Treasurer’s Investment Pool, the Orange County Investment Fund (OCIF). Fiscal sponsors would not have the ability to participate in the OCIF, but the Commission may request the Treasurer to manage specific investments appropriately invested in longer-term securities as allowed under Government Code. This option would match the maturity of the investments with cash flow needs. Investment maturity dates would not exceed five years at the time of purchase. Special trust funds would be created under the management of the County Treasurer and comply with the current Investment Policy. This may create some risk as the trust fund would likely be an affiliated fund of the Commission.

The initial intent for the use of a fiscal sponsorship during the catalytic investments was to provide multi-year programmatic funding for key initiatives and result in a reduction in the Commission’s fund balance. While the first option allows for the Commission to meet this objective, it may increase the risk on the principal allocation. Option 2 reduces the investment risk, but may increases some risk since funds would likely be reported as an affiliated fund of the Commission. Commission direction and input is requested on the two options that staff has developed.

Based on Commission direction, staff will conduct further analysis and return to the Commission with recommendations for formal action. Analysis will ensure compliance with all investment restrictions consistent with state code and solicit the input of the County Treasurer, who was affirmed as the Commission’s Treasurer for FY 2013/14 in May 2013.

STRATEGIC & FISCAL SUMMARY:
The strategies have been reviewed in relation to the Strategic Plan and are consistent with relevant goals. No funding action is requested at this time.

RECOMMENDED ACTIONS:
Receive report and provide continued policy direction to staff.

Contact: Kim Goll