

# OCIO SOLUTION



## HEALTH SYSTEM REDUCES POST-CONSOLIDATION COMPLEXITY BY DEVELOPING AN INTEGRATED RISK FINANCIAL FRAMEWORK

### The organization

A large, private academic health system composed of nationally ranked hospitals and academic programs. With more than 30,000 employees, 4,400 faculty, 8,300 students, and 1,680 medical staff, these constituent organizations work together to provide quality patient care, as well as education to future healthcare professionals. The Investment Office is led by the chief investment officer (CIO), who oversees more than \$4 billion of non-qualified and qualified assets and \$2.2 billion of defined contribution assets.

### Challenge

Over the past five years, the organization has been steadily growing larger in size, acquiring or merging with four other healthcare organizations and one university, and taking on the management of additional assets. With this hefty organizational expansion, the investment program more than tripled, from \$1.3 billion to over \$4 billion in non-qualified and qualified assets. The organization now had a mix of defined benefit plans, extended working capital pools, short-term pools, and long-term pools to manage. Each asset pool played a different role within the investment program, which required unique strategic asset allocations, investment objectives, liquidity profiles, and time horizons. All of this created an additional layer of complexity for the CIO to manage.

The addition of each subsidiary organization’s multiple, unique asset pools resulted in a highly complex (and complicated) structure for the overall organization’s CIO to navigate, as illustrated in [Exhibit 1](#).

### Exhibit 1: Legacy investment program - Umbrella organization

SUBSIDIARY ORGANIZATION 1	SUBSIDIARY ORGANIZATION 2	SUBSIDIARY ORGANIZATION 3	SUBSIDIARY ORGANIZATION 4	SUBSIDIARY ORGANIZATION 5
Long-term pool	Long-term pool	Long-term pool	Defined benefit plan	Endowment pool
Defined benefit plan	Defined benefit plan	Defined benefit plan	Short-term pool	
Short-term pool	Short-term pool	Short-term pool		
	Extended working capital pool	Extended working capital pool		


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At its height, there were 14 asset pools within the organization's investment program. With the organizational expansion, the complexity of aligning each pool's investment objectives with the umbrella organization's new financial goals increased dramatically. Moreover, each pool had its own unique suite of investment strategies—including commingled funds, separate accounts, and proprietary funds from a third-party consultant. At one point, the CIO was singlehandedly delegating to over 130 managers across \$4 billion of capital.

Along with the numerous managers and pools of capital, the organization was juggling a complex web of vendor relationships. Each legacy investment program had its own investment advisor, auditor, trustee, and custodian. Moreover, the organization had multiple layers of costs to pay, including:

- Investment management fees
- Custody fees
- Advisory fees
- Internal staff oversight expenses
- Investment-related audit expenses

Managing the impact of this expansion on the larger organization, its investment program, and its financial statements presented challenges to the CIO's time and resources. The CIO envisioned a solution that would help manage this complexity by streamlining the investment program and simplifying investment operations. The organization also desired detailed and transparent analytics, direct investments in top-tier active and passive managers, and the ability to delegate reporting and administrative functions to an outsourced CIO (OCIO) provider. All of this was intended to improve implementation, mitigate risk, and reduce costs—while increasing manager oversight. Ultimately, the organization sought a partnership with an OCIO, in which the OCIO would assist with operational burdens; help manage multiple vendor relationships; set up a new, flexible portfolio platform; provide access to top-tier managers; and dynamically tilt the portfolio as needed—while allowing the CIO to have the final say over which manager(s) to hire, terminate, or adjust.



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## The objectives

- **Asset pooling:** Streamlining of 14 asset pools worth \$4 billion
- **Relationship pooling:** Simplification of a complex vendor relationship network
- **Added layer of manager oversight:** Direct access to a broad universe of active and passive investment managers and delegation of portfolio implementation
- **Investment consulting:** CIO oversight of several independent investment consultants to provide third-party oversight of the programs and investment managers
- **Reduced administrative burden:** Outsourcing of administrative and reporting functions
- **Increased buying power:** Reduction of manager and vendor fees
- **Risk mitigation:** Better understanding and management of risk in underlying investments


## The solution

In order to rationalize and simplify the complex legacy portfolio structures, the CIO developed an integrated risk financial framework (IRFF). The purpose of this framework was to catalog all the material enterprise risks that could impact the health system, capture the potential ways the health system could respond to those risks, and define an investment approach that sought to effectively quantify and manage those risks. This framework was designed to:

1. Identify potential claims on liquidity from the organization's operations, spending, debt, and investments
2. Assess the organization's ability to carry risk given its available financial resources, including unrestricted cash and investments
3. Provide a holistic view of organizational risk, thereby allowing the CIO to assess the implications of a risk-adjusted investment deployment strategy on the organization's overall financial health

With these principles in hand and the risk catalog quantified, the CIO approached Russell Investments, who has served as the organization's advisor and investment manager for many years, with the concept of developing a simplified investment deployment strategy. With intimate knowledge of the organization's goals and circumstances, we helped build a custom, multi-asset solution that is designed to provide the client's team with the operational support they need, while allowing them to retain authority over key strategic decisions.

The solution, which leverages Russell Investments' size and scale, greatly simplified the organization's investment program by paring it down from 14 separate pools to four consolidated asset pools that were identified as part of the client's IRFF efforts. Each pool has a target risk-return profile based on its liquidity requirements. The ultimate portfolio structure, illustrated in [Exhibit 2](#), combines all the defined benefit plan assets into a single defined benefit plan, and consolidates each of the separate short-term pools, long-term pools, and extended working capital pools into three main pools of capital.

 *The solution, which leverages Russell Investments' size and scale, greatly simplified the organization's investment program by paring it down from 14 separate pools to four consolidated asset pools...*

### Exhibit 2: New investment program – Umbrella organization

QUALIFIED ASSETS	NON-QUALIFIED ASSETS
A single, consolidated defined benefit plan	Short-term pool
	Long-term pool
	Extended working capital pool

## Benefits

Creating custom pooled funds significantly condensed the investment program and gave rise to an investment solution that is unique to the organization. This simplified structure allows each pool to have a unique asset allocation, which is composed of Russell Investments' researched "best-in-breed" active and passive strategies that are selected and approved by the client. Our solution saved the organization over 12 basis points in fees, which translates to a reduction of 28%. The new platform is also flexible and allows for continued portfolio enhancement—for example, the organization can screen for environmental, social, and governance (ESG) factors in its funds to reflect any of its unique beliefs. We have also established agreed-upon ranges around the strategic asset allocation targets for each portfolio. These allow us to make tactical tilts when needed to capitalize on opportunities designed to enhance return or mitigate risk.

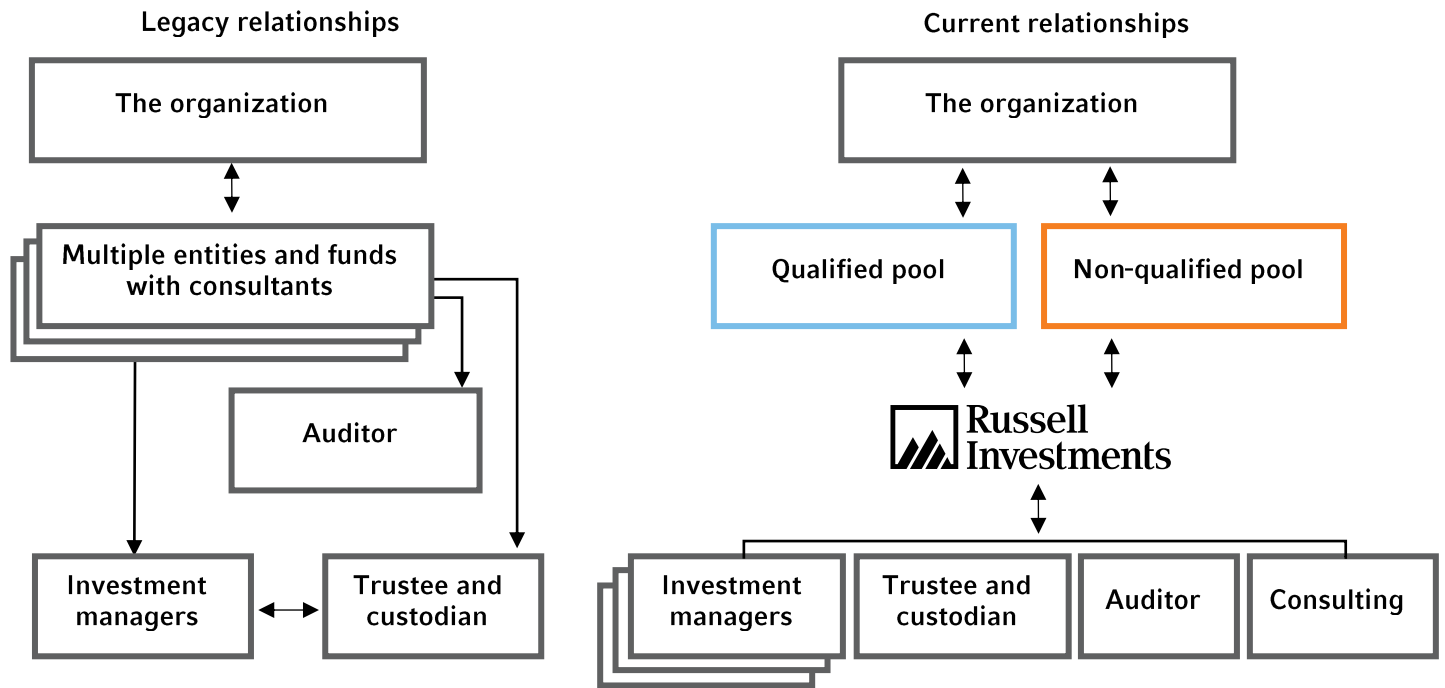
We believe our solution blends the best of the consulting model with the best of the OCIO model:

- **Consulting:** We advise on portfolio structure and manager selection while the client retains decision-making authority over hiring and terminating managers<sup>1</sup>, based on input from its independent investment advisors. If necessary, the client has the ability to identify a non-recommended manager, and Russell Investments will negotiate fees on behalf of the client.
- **OCIO:** We build the separate account fund structure for the client and assume responsibility for implementing the client’s strategic decisions and for performing many of the day-to-day operational aspects of managing a portfolio. We also provide detailed, transparent analytics and financial reporting. Additionally, we negotiate and contract with vendors and underlying managers, and the client benefits from lower manager and vendor fees thanks to our size and scale.

Pooling the administrative structure and vendor relationships also greatly reduced the organization’s operational burden. **Exhibit 3** illustrates the simplification of the client’s relationship network.

**Pooling the administrative structure and vendor relationships also greatly reduced the organization’s operational burden.**

**Exhibit 3: Consolidation of vendor relationships**



<sup>1</sup> This is a strategy designed for this specific client. Strategies may differ according to the client.

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## Roles and responsibilities

In the unique solution that we designed for the organization, the roles and responsibilities are broken down as follows:

RUSSELL INVESTMENTS	THE ORGANIZATION
Advises on portfolio structure and managers	Sets portfolio objectives (such as the benchmark and risk-return target) and constraints (such as the fee budget and any specific guidelines)
Negotiates fees and executes manager contracts	Approves asset class structure—including active and passive allocations, and strategic factor tilts
Performs ongoing manager research, guideline compliance, and operational due diligence	Approves specific managers and allocations
Prepares risk analytics and risk management reporting	Has access to risk analytics and risk management tools
Provides cash flow management, security valuation and fair value reporting, counterparty and brokerage services, recordkeeping, and transition management	

### Results

By working with Russell Investments, the organization was able to streamline its multiple asset pools, retain control where desired, decrease the complexity of its investment program, and reduce expenses. By grouping the organization's various asset pools into two legal entities and four underlying consolidated asset pools, and leveraging our scale, we were able to increase the client's buying power with managers and vendors, saving them over 12 basis points in fees—which represents a reduction of 28%. The organization also benefits greatly from affordable access to our industry-leading manager research<sup>2</sup>, portfolio structure insights, and investment manager relationships.

In addition, our solution has reduced the organization's administrative overhead and risk by allowing it to delegate many day-to-day operational and administrative functions such as guideline compliance monitoring, risk analytics, managing frequent cash flows, and operational due diligence.

The organization has benefited from a deepened relationship with Russell Investments as its investment provider. By delegating increased levels of administrative discretion to Russell Investments, the CIO and staff now have additional time and resources to focus on higher-level, strategic, and value-creating decisions that will allow the portfolios to better support the organization's overall financial goals.

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<sup>2</sup> Over a 28-year period from 1995, an average of 77% of our 'hire' ranked products have outperformed their benchmark over rolling 5-year periods, with an average performance for all 'hire' ranked products of 1.47% above benchmark. Source: Internal Russell Investments analytics data from January 1, 1995 through December 31, 2022.

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# QUESTIONS?

Call Russell Investments at **866-739-7979**  
or visit [russellinvestments.com/healthcare](https://russellinvestments.com/healthcare)

## ABOUT RUSSELL INVESTMENTS

Russell Investments is a leading global investment solutions partner providing a wide range of investment capabilities to institutional investors, financial intermediaries, and individual investors around the world. Since 1936, Russell Investments has been building a legacy of continuous innovation to deliver exceptional value to clients, working every day to improve people's financial security. Headquartered in Seattle, Washington, Russell Investments has offices worldwide, including New York, London, Sydney, Tokyo, and Shanghai.

### IMPORTANT INFORMATION

This case study represents a unique situation faced by a large private academic health system seeking an outsourced services provider to manage a complex mix of DB plans, extended working capital pools, short-term pools and long-term pools. Case studies are problem-solving stories. We select a situation that is indicative of problems clients in this category are facing. The recommendations described do not represent a standard strategy or set of recommendations made for all advisory clients with similar issues. Each client has unique requirements, challenges, and constraints, and our advisory solutions are tailored to each client's specific needs. Every client's situation, experience and needs are different, and Russell Investments does not imply that the solution herein is appropriate for any other client.

The case study provided is for illustrative purposes only and is meant to provide an example of a type of financial issue a client may have and our process and a methodology to address it. Individual client results will vary based on individual circumstances and market conditions. The results presented were based on a period of fluctuating marketing conditions and the underlying asset allocation, market criteria and assumptions, or the investment advice/strategy followed may have changed materially. There is no guarantee that all clients will experience the same results.

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Please remember that all investments carry some level of risk, including the potential loss of principal invested. Although steps can be taken to help reduce risk, it cannot be completely removed. Investments typically do not grow at an even rate of return and may experience negative growth. As with any type of portfolio structuring, attempting to reduce risk and increase return could, at certain times, unintentionally reduce returns.

Diversification does not ensure a profit and does not protect against loss in declining markets.

Each product in our hire lists is compared to the relevant Russell Investments assigned benchmark and universe to determine product level excess returns for each quarter. All product level quarterly excess returns are geometric excess returns. Product level quarterly excess returns are then averaged across all products in the hire list to determine an average hire list quarterly excess return. Averages are only calculated for hire lists that consist of at least three hire rank products for the given quarter. The average quarterly excess returns by hire list are then annualized to determine the hire list 5-year annualized rolling excess returns. Each 5-year annualized return requires 20 contiguous quarters of non-missing quarterly averages. If the 5-year annualized average excess return for a hire list is greater than zero, then the hire list is considered to have outperformed over that time period.

The Hire List Success chart shows the percentage of defined coverage areas where the hire list mean return exceeded the hire list index return or the universe median return for the five-year periods ending on the dates shown. Manager products are included and excluded as our product ranks change over time; not all products are continually hire ranked over these indicated time periods.

Russell Investments' ownership is composed of a majority stake held by funds managed by TA Associates, with a significant minority stake held by funds managed by Reverence Capital Partners. Certain of Russell Investments' employees and Hamilton Lane Advisors, LLC also hold minority, non-controlling, ownership stakes.

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