



# REPORT

To: ONE Joint Investment Board  
From: Judy Dezell, Co-President/Co-CEO, ONE Investment  
Date: April 22, 2024  
Re: Business Rationale for the Outsourced Chief Investment Officer (OCIO) Model  
Report: ONE JIB 2024-021

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## 1. RECOMMENDATIONS

It is recommended that the Board:

1. Receive the report.

## 2. SUMMARY

There are several compelling reasons for ONE Investment and ONE JIB to move to an OCIO model that:

1. Will better meet the needs of large investors, while also benefiting small and medium-sized investors;
2. Enables the scaling up of the Prudent Investment Program as more and larger municipalities join the program;
3. Eliminates the constraints caused by limited staffing at ONE Investment; and
4. Will provide Participating Municipalities with significantly enhanced services, at the same or lower cost. Specifically, Philips, Hagar & North (PH&N) will offer a much broader range of investment options, allowing for more customization of municipal portfolios and has the capacity for in-depth analysis, including asset allocation studies, risk management, investment strategy, and performance monitoring, beyond what ONE Investment is currently able to offer.

## 3. BACKGROUND

### **Support for the municipalities looking to invest has evolved over time**

ONE Investment is a small not-for-profit organization supporting the municipal sector to fund their long-term capital plans and their municipal asset management plans (for physical infrastructure) through investment returns. Before becoming a separate not-for-profit organization in 2020, the One Fund program, as it was then known, was light touch for LAS and CHUMS staff. All mission critical functions were outsourced to experts that could deliver a high-quality product. The One Fund program was designed for investments under the Legal List, where the municipal treasurer makes decisions about investment products.

However, it was clear to staff that there was a gap in investment knowledge in the

municipal sector, as well as a need for unbiased investment advice. This was reinforced by a growing emphasis on asset management plans and longer-term capital planning. Around this time, the province was also contemplating legislation to make the prudent investor standard available to municipalities through the *Municipal Act*. ONE Investment and the Investment Advisory Team<sup>1</sup> are products of the need within the sector and the opportunity that the prudent investor standard gave municipalities. The sector has embraced these changes. What has not changed is the need to rely on third party service providers to deliver high-quality investment products to the municipal sector.

## **Growing assets under management is a shared strategic goal of ONE Investment and ONE JIB**

In 2022 ONE Investment and ONE JIB worked together to develop a shared strategic plan. The strategic plan was approved by both boards in the Fall of 2022 with a vision of being the leading investment solutions partner for the Ontario municipal sector. Its goals included growing assets under management (AUM), increasing the number of participating municipalities, improving municipal engagement and conversion through education and training, and developing profiles of municipalities to understand investment maturity.

It is in the context of the first goal – growing AUM by approximately \$3 billion between 2023 and 2028 - that the concept of the Outsourced Chief Investment Officer (OCIO) Offering<sup>2</sup> was developed. There were two complementary paths to achieving the goal – 1. attract a lot more small and medium-sized municipalities to the Prudent Investment Program and 2. work to attract municipalities with more than \$500 million in money not required immediately. Work continues today on attracting small and medium-sized municipalities while development of the OCIO Offering is designed to attract larger municipalities. Both paths create resourcing challenges for ONE Investment that need to be addressed to sustain a high-quality offering that municipalities expect.

### **Why use an OCIO model?**

An outsourced chief investment officer (OCIO) is an investment firm that manages investment portfolios on behalf of individuals, endowments, foundations, or pensions. In the case of ONE Investment, it would be outsourcing – as it already does both under Legal List and Prudent Investment Programs – investment functions to the OCIO to take on the responsibility of managing municipal investment portfolios. What would be new in the Prudent Investment Program would be the OCIO partner also making investment decisions and monitoring investment performance of the funds consistent with ONE JIB's approved Investment Plans, as per the *Municipal Act*.

OCIO firms also provide a range of investment services that ONE Investment currently cannot, such as: asset allocation, investment strategy development, risk management, manager selection, performance monitoring and reporting. The OCIO firm would work closely with ONE Investment, ONE JIB and the municipalities to understand municipal investment objectives, risk tolerance and any other preferences the municipality may have identified. The investment strategy would be developed by the OCIO in alignment with all

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<sup>1</sup> The Investment Advisory Team is ONE Investment staff with knowledge in municipal finance and investment industry experience that team up to help municipalities work through their long-term investment objectives and translate it into investment strategy.

<sup>2</sup> The OCIO Offering was originally called the Large Municipality Offering.

this information. Partnering with an OCIO firm allows ONE Investment to leverage the scale these firms offer to access specialized investment expertise, make more timely investment decisions, and offer a lower cost for investment to large municipalities. The OCIO will provide a wide variety of investment options that can be accessed very quickly if desired. Entities that engage an OCIO do so to allow them to focus on the strategic direction of the organization while improving investment outcomes.

The OCIO Offering uses an OCIO model to provide the scale and specialization larger municipalities are looking for while resolving a key concern about how to avoid overwhelming ONE's staff capacity. PH&N, ONE Investment's OCIO partner, was identified through a competitive RFP process that has been supported by an Evaluation Committee that included representatives from ONE JIB.

PH&N has gained significant experience through its long-standing relationship with the Municipal Financing Authority of British Columbia which has helped inform both the design of ONE Investment's OCIO Offering and reduced the need for ONE to explain the general needs of municipalities. PH&N staff are instead focused on what is unique here in Ontario and what ONE Investment wants to achieve with its OCIO Offering.

Work on the OCIO Offering started in the Fall of 2022. Since that time, it has become clear to ONE Investment that changing the business model of the Prudent Investment Program for all investors to the OCIO model is the preferred method of scaling up and providing the best Prudent Investment Program at the best value for all Participating Municipalities.

#### 4. ANALYSIS

##### **ONE Investment staff capacity has reached its limit**

Work for ONE Investment staff in supporting the existing 11 Participating Municipalities has been automated as much as possible for efficiency, but tasks like quarterly performance reporting commentary take a significant amount of time from staff that could instead be focused on supporting the needs of existing investors or onboarding new investors. The annual review of a municipal Investment Policy Statement is also a labour-intensive exercise. As the number of municipalities joining ONE JIB grows, there will need to be increased focus on supporting this annual cycle to meet *Municipal Act* requirements. Staff are also looking at ways to streamline the annual review for ONE JIB because its workload will also increase as the number of Participating Municipalities increases.

##### **ONE Investment made a business model choice to attract larger municipalities to its Prudent Investment Offering**

To attract larger municipalities, ONE Investment was faced with a choice of either significantly expanding its staff complement to attract the large investors or, as it has always done, hiring the expertise required to attract and support large investors. ONE Investment chose to hire the expertise through an OCIO Offering. That does not mean that ONE Investment is ruling out the creation of in-house expertise, but right now it is critical to

provide the depth of expertise in areas such as asset allocation studies and breadth of investment options sought by large municipalities.

At the same time, ONE Investment was seeking a prudent investor product offering that could be scaled to the small and medium-sized municipalities that already invest through the Prudent Investment Offering and those looking to join. The OCIO model helps address the capacity challenges ONE Investment is already experiencing due to the growth of the Prudent Investment Program.

### **Under the OCIO model the Prudent Investor Program will remain viable even if a large municipality withdraws**

Some large municipalities were concerned about harming ONE Investment's business model if they joined and then one or more decided to exit the Prudent Investment Program and set up their own municipal investment board in the future. By using the existing ONE JIB, the \$100 million in money not required immediately test within the *Municipal Act* has already been met by the Founding Municipalities. If a large municipality decides to leave ONE JIB in the future, the Prudent Investment Program will continue to be viable.

### **ONE Investment is committed to maintaining a strong governance framework**

ONE Investment is ONE JIB's agent with obligations that it is committed to appropriately resourcing. Drafting reports that provide the right details for ONE JIB to make informed decisions takes time. Appropriately supporting ONE JIB is a priority for ONE Investment. Relying on PH&N to undertake the quarterly performance analysis required for municipalities along with rebalancing and other similar functions will free up time for ONE Investment staff to focus on the key governance requirements such as municipal Investment Plans and assessing PH&N and its selected fund managers performance. It is also important to note the OCIO business model will continue to have a strong focus on a comprehensive compliance framework which is fundamental to the good governance tone ONE JIB has established.

### **The OCIO Offering will also allow aggregation of AUM to maintain or reduce investment fees**

In the case of the OCIO Offering, there are two categories of costs that make up the entire fee paid by municipalities. The first is the investment management operational costs that include the costs associated with management of PH&N's funds plus fund audits, custodial services, and all additional services provided by the OCIO including client performance reporting and asset allocation studies. As AUM grows, this category of fees will be allocated over a larger asset base and will therefore decrease as a percentage of assets. ONE Investment has negotiated the best price possible. As AUM grow under the OCIO Offering the average fees per dollar invested will decline. This means as new AUM is invested in the OCIO Offering by any municipality, the average fees for all Participating Municipalities will tend to decrease. ONE Investment has negotiated a sizeable discount at \$2.5 billion of AUM and also at \$8.8 billion. This fee structure motivates ONE Investment to work to attract as many large investors as possible to provide the best Prudent Investment Program at the best value possible for all municipalities.

The second category of costs is to meet *Municipal Act* requirements – ONE Investment refers to them as governance fees. These costs include ONE JIB and all the operational costs ONE Investment incurs to support ONE JIB and the OCIO offering, such as Board Secretarial costs, Integrity Commissioner, Closed Meeting Investigator and human resources to support municipal investors and ONE JIB. These fees are also based on the AUM of the municipality. For municipalities with over \$1 billion in AUM there is a cap on governance fees.

Once fully transitioned to the OCIO model, the 11 existing Participating Municipalities will pay fees less or equal to their current fees for an offering with more investment options, assuming their AUM remains similar.

**The rollout of the OCIO Offering will take place over 18 to 24 months**

ONE Investment recognizes that changes to its current operations will be needed to achieve scale for the Prudent Investment Offering. The OCIO Offering provides a path forward to achieve scale and maximize the existing resources ONE Investment has by leveraging the resources PH&N brings to the table.

Currently, the plan is to fully transition to the OCIO Offering as the only Prudent Investment Offering in three phases – see Figure 1. ONE Investment staff will bring forward to the September meeting of ONE JIB details around what will need to be considered in transitioning the existing 11 Participating Municipalities to the new business model. With input from ONE JIB, ONE Investment staff will then bring a full transition plan to ONE JIB for approval in November 2024.

*Figure 1 - OCIO Offering Roll Out*

	Q2 2024	Q3 2024	Q4 2024	Q1 2025	Q2 2025	Q3 2025
<b>Phase 1:</b> First Large municipality onboarded						
<b>Phase 2:</b> New smaller municipalities onboarded						
<b>Phase 3:</b> Start transitioning existing 11 Participating Municipalities						

**5. CONCLUSION**

By introducing the OCIO model, ONE Investment is leveraging an investment already made into a complex governance structure, preserving staff resources and providing

municipalities with a broader range of investment choices. The intent is to support the shared strategic goal of growing AUM and helping municipalities fund their long-term capital plans and their municipal asset management plans (for physical infrastructure) through investment returns.

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