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A Fine Balance: Aligning Fiduciary Duty with Your Strategic Mission in Continuing Care Communities

The popularity of communities designed for adults in retirement or even pre-retirement phases is rising. Whether it's salsa lessons, zero emissions buildings, gourmet cooking or entrance fees, community members are becoming increasingly discerning. As these communities evolve and grow in popularity to support the massive wave of retiring Boomers, so do the responsibilities faced by management teams and boards of directors of these non-profit organizations.

Being at the helm of Life Plan Communities ("LPC") and Continuing Care Retirement Communities ("CCRC") is a balancing act. You need to juggle priorities such as health care, investing, real estate, and insurance with the needs and well-being of your residents. As fiduciaries, you also need to safeguard and prudently manage the entrance fees that members pay in order to protect their capital.

Over the long term, LPCs and CCRCs also have a responsibility to grow capital as they market to a growing and increasingly demanding Baby Boomer target audience. Capital growth and access to capital are key to ensuring that you can serve your constituents while being mindful of the long-term viability and strength of your organization. After all, a well-run community is one of your best marketing tools. It's a virtuous cycle: effectively managing your capital enhances your ability to attract future capital.

Accountability to residents

Today, there is greater scrutiny and accountability when investing residents' fees as prospective residents and their families become savvier and more knowledgeable. You only have to look as far as articles such as "7 Ways to Judge a Retirement Community's Financial Health" in The New York Times (March 9, 2018). With access to more information than ever before, the Baby Boom generation is doing their due diligence. Comparison shopping different retirement communities is now par for the course, which may even include examining the financial health of different communities before they join.

In many cases, the entrance fee refund that residents expect is a legacy to their children or other beneficiaries. As a fiduciary, how do you ensure that your constituents can enjoy peace of mind while meeting your operational and strategic growth objectives? Importantly, how do you convince future residents or prospects that you are up to the task?

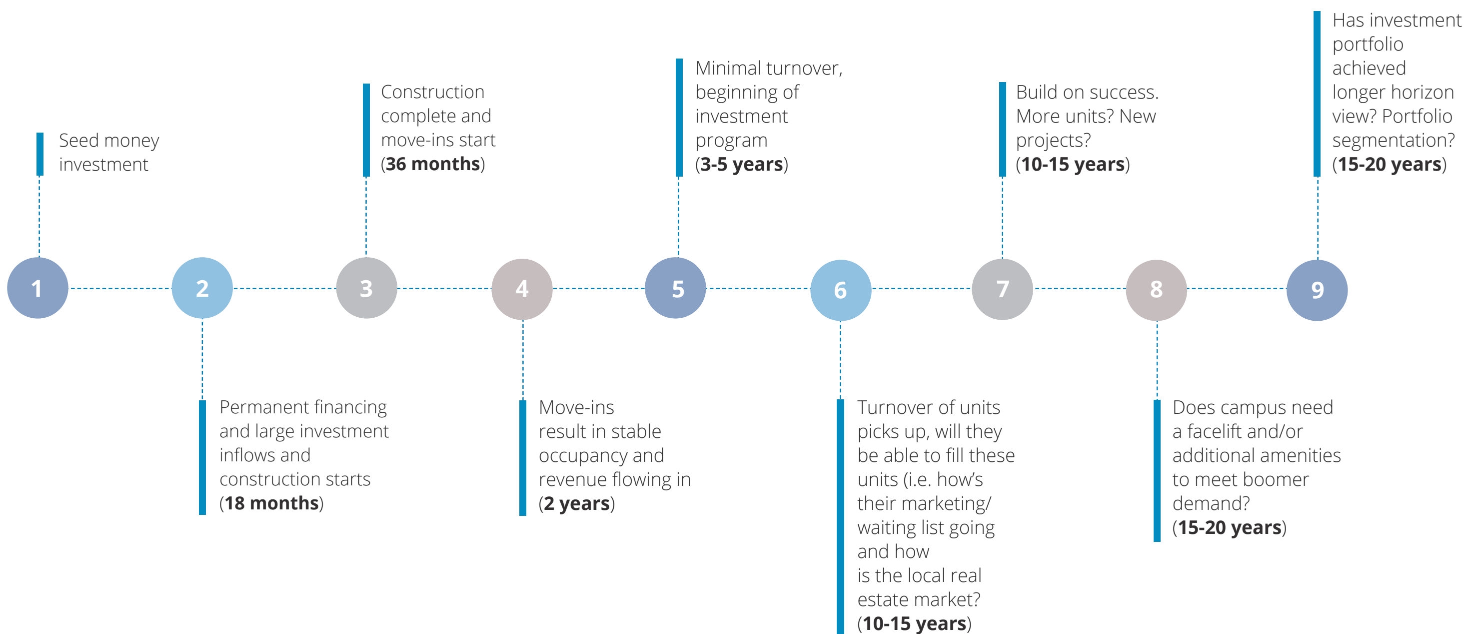
Starting with organizational fundamentals

A sound investment plan starts with the fundamentals of your organization. A more nuanced understanding and integrated perspective of your assets and liabilities are vital to crafting an asset allocation and investment policy that is aligned with both your fiduciary duties and your organizational objectives.

When we advise clients at Procyon, we start with a look under the hood of the organization — we thoughtfully analyze their financial statements (e.g., balance sheet, income statement, statement of changes in financial position). Getting down to these nuts and bolts, we often work with our clients to look at their capital base from an asset/liability perspective. We assess how well their enterprise can safely meet growth objectives and long-term obligations while balancing the need for potential drawdown and liquidity.

Financial statements provide an important litmus test that help to reveal how much risk can be tolerated at a community level. This will inform how management teams can manage risk to fulfill their fiduciary responsibilities. While fiduciary duty is relevant to the entire management team, the CFO is normally on the front lines. CFOs often need to articulate what's at stake to CEOs and other senior executives and board members — risk is one way to contextualize or frame this discussion. At the end of the day, risk needs to managed responsibly. Therefore, every investment decision should be made through the lens of how it affects community risk.

Life Cycle of a Life Plan Community



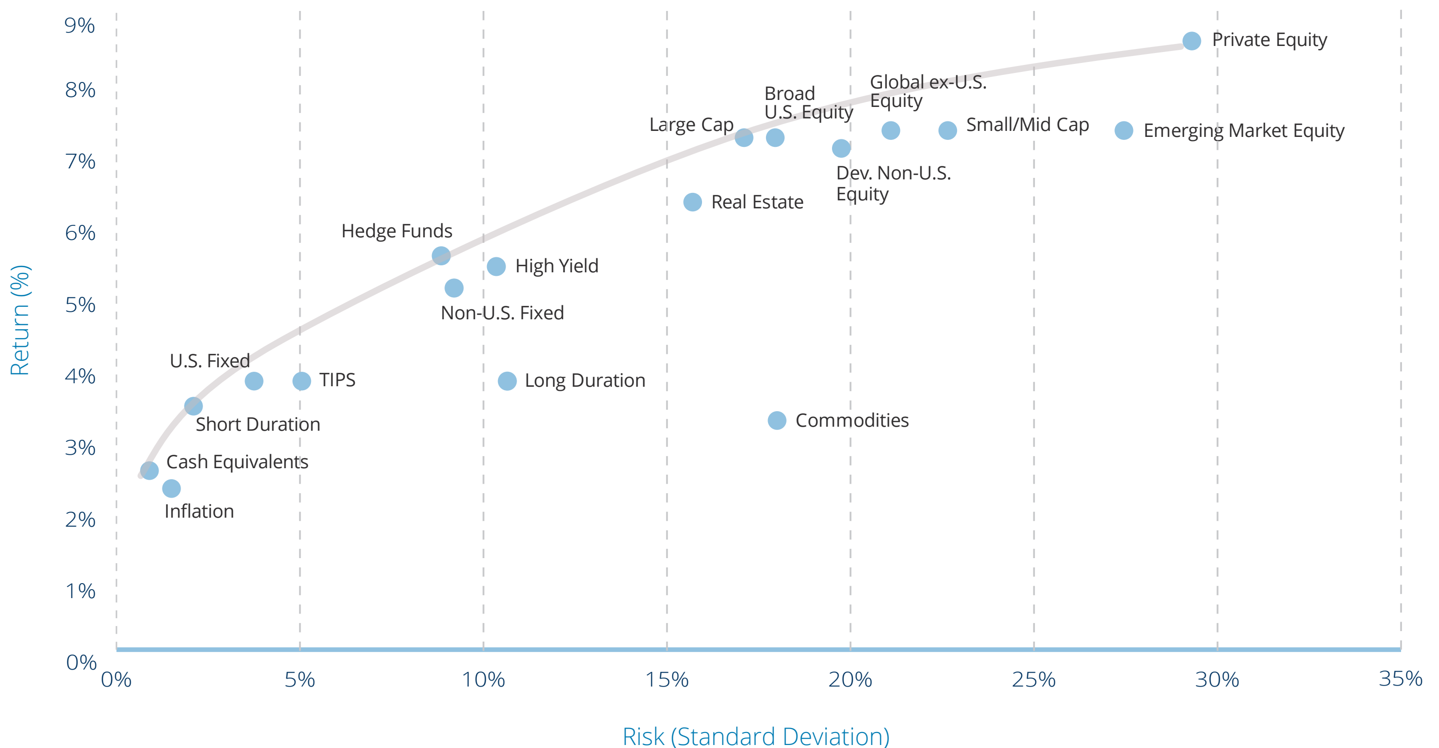
Asset allocation that aligns with risk appetite

Investment risk-reward should correlate to the risk of your enterprise to ensure your goals are aligned. We believe that taking an integrated, holistic approach is prudent. Crafted properly and thoughtfully, your asset allocation and investment policy will be a road map to ensure the long-term strategic viability of your organization and build an enterprise that endures and responds to the needs of residents.

In traditional asset allocation, equities tend to harbor a lot of the risk you take as an organization. The amount of risk your constituents and organization can tolerate helps to influence your asset allocation between equities, bonds and other asset classes — including those that can bridge the gulf between too risky and overly safe.

In a persistent low-return environment, a traditional mix of stocks and bonds alone may not be able to help accomplish your objectives. In fact, we believe that exposure to efficient combinations of asset classes as depicted below can play an important role to help dampen volatility and manage the need for return.

Look Beyond a Traditional Mix of Stocks and Bonds to Accomplish Strategic Objectives



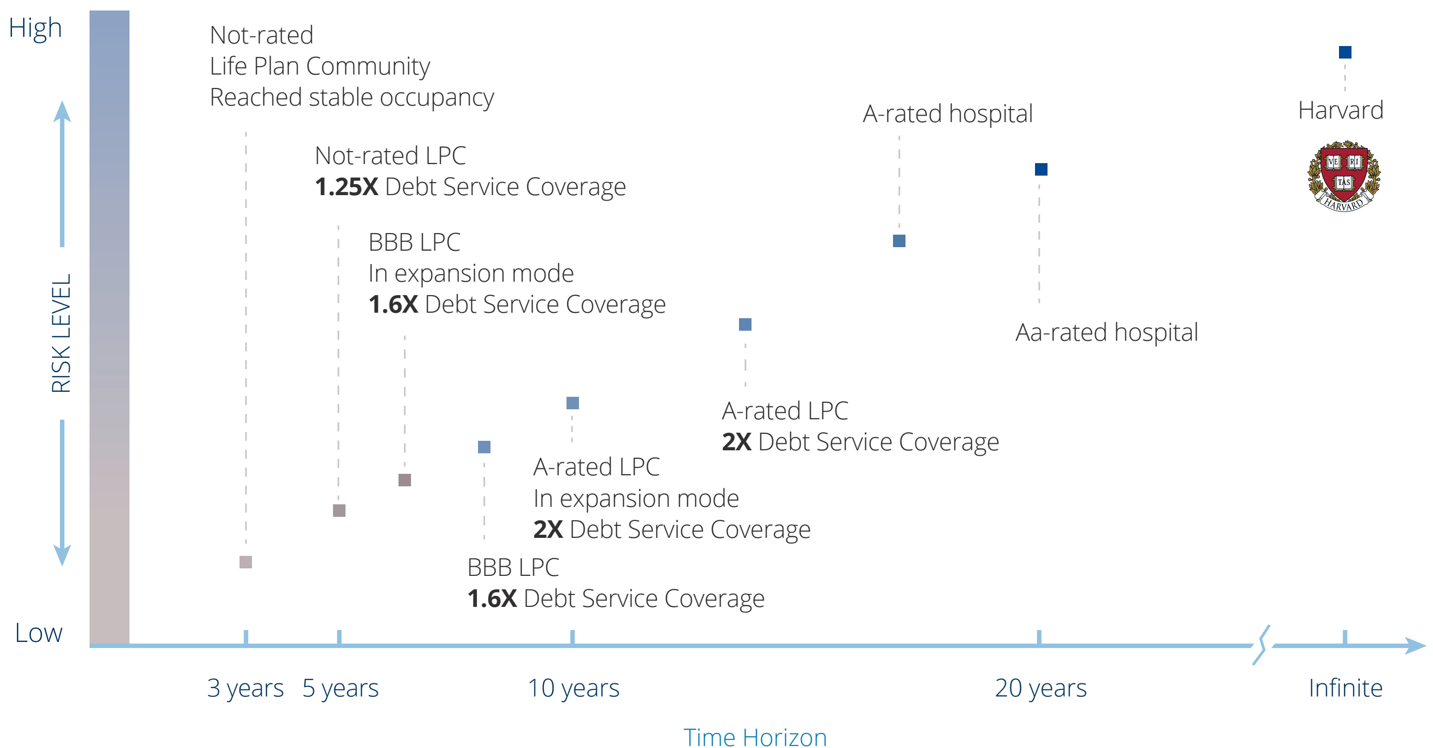
Why not look to Harvard?

Often, it's easy to think that money in CCRCs and LPCs can be managed like that of any other endowment. This is a bit of a misperception. Within an LPC or CCRC structure, there is money that the organization conceptually owes to its residents. In the case of a large university, such as the proverbial Harvard or Stanford endowment, you don't have to contend with drawdowns and technically have an infinite timeframe in which to invest. In the case of LPCs and CCRCs, you are often working with a pool of money that needs to account for refundable entrance fees. Therein lies the difference.

Drawdowns, which never come at the "right" moment, could have a significant impact on the ability of CCRCs and LPCs to meet promises to creditors and ultimately residents. Therefore, it's a good idea for management teams and CFOs to model how their capital base and financial ratios will be affected by these drawdowns and then stress-test the liquidity and potential volatility of their entire portfolio. We are currently in a period in which a long period of low volatility has lulled many people to sleep in terms of risk.

There needs to be sufficient liquidity within a CCRC's or LPC's portfolio to meet obligations or liabilities, keeping in mind that, going forward, markets may not be as forgiving as they have been. In this circumstance, it's important to invest with an expert that can manage a well-diversified portfolio that is sensitive to risk-return and drawdown considerations.

Risk Profiles of Life Plan Communities Versus Other Institutions



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Alignment of interests (and strategy)

How you view risk and invest your assets should be tied back to your organizational goals and mission. Prudent investment can help your assets work harder and serve your current and future constituents better.

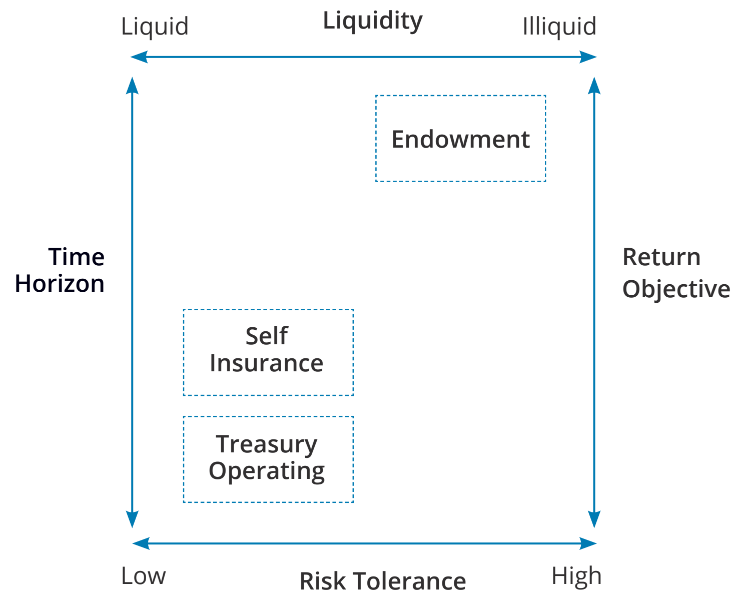
As a group, LPCs' and CCRCs' needs are thoroughly unique — further compounded by the unique needs of each community. It makes a significant difference when you choose a partner who truly understands CCRC and LPC structures and can be a vocal advocate at the table as part of your planning process.

To be in control of your organization and fiduciary duties is to be able to increase and decrease risk as necessary. This can be accomplished through a variety of strategic and tactical means, including segmentation of your portfolio. Your capital needs are never static, and partnership with someone who understands CCRC structures and their unique challenges and cash flow needs is mission critical.

Let's start the conversation

As a fiduciary to the assets of your residents, you want to arrive at a prudent, thoughtful allocation that manages risk responsibly for all stakeholders while aligning with your community's growth objectives. At Procyon Partners, we are a team of seasoned professionals who are familiar with the business models of CCRCs and LPCs and are in a position to help you achieve this balance.

Strategic Portfolio Segmentation is Contingent on Many Factors



Metrics	**Objectives / Goals**
• Days cash on hand • Debt service ratio • Operating ratio	• Market expansion • Campus improvement • Marketing

Call 1-844 PROCYON today

To get a customized assessment of your organization's risk tolerance and the strategies available to you. We'd love to help brainstorm solutions that suit your organization's risk profile and fiduciary goals.

Jim Jeffery

Managing Director, Senior Institutional Consultant

Jim Jeffery, Managing Director of Procyon Partners LLC, is a leading financial advisor to senior living organizations and high net worth families with more than 35 years' experience navigating financial and capital markets. Jim has a particular interest in the senior living industry, which dates from his experience as Executive VP & Head of Underwriting at Herbert J. Sims & Co, a leader in senior living finance. Specifically, for almost 20 years, Jim has been helping Life Plan Communities (Continuing Care Retirement Communities) develop Investment Policies that balance the assets and liabilities of these organizations. In addition, Jim's direct experience underwriting, structuring and re-structuring CCRC bond issues is invaluable in his role as financial advisor and consultant to senior living organizations.

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Disclosure

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