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How to set an Investment Policy

This guide has been developed to assist Charity's who are seeking to Invest their reserves and tales them along the journey from making the decision to invest and then settling an investment policy. This guidance should be read in conjunction with our helpsheet on 'understanding investment jargon'.

Why do Charities invest?

Charities usually invest to generate a return to help them carry out their objectives. This ranges from largescale investment by charities wholly reliant on investment income, to the investment funds that form part of a charity's reserve buffer. Increasingly, charities are looking to invest funds not just to generate a return, but also to deliver their charitable objectives. These are known as social investments (formerly terms ethical or mixed motive investments). An example is a loan to a subsidiary company where the subsidiary's activities either directly deliver or support the charitable objective.

All charities can make investments, and powers to invest usually come from your governing document and / or the law.

Your charity's investments powers depends on its structure - whether it is incorporated or not, but in practical terms. Virtually all charities undertake some form of investment as they have the power to do so.

What are your Responsibilities when making Financial Investments?

As a trustee, you have overall responsibility for the investment of the charity's funds. This responsibility cannot be delegated. When making investment decisions you should use your skills and knowledge in a way that is reasonable in the circumstance (the 'duty of care').

During its last revision CC14 imparted the importance of this duty of care and strongly advocates the use of experienced individuals and concludes that, in order to act within the law, Trustees must take advice from someone experienced in investment matters unless they have good reason for not doing so.

There are some specific trustee duties the charity commision expects you to adopt when making financial investments, these are:

- Considering whether the investments are suitable for your charity and whether they will meet its investment objectives
- Considering the need to diversify investments, if appropriate to your charity, to spread the risk
- Taking advice from someone experienced in investment matters, unless you have a good reason for not doing this
- Reviewing you charity's investments at appropriate intervals

Setting Investment Objectives

Trustees should approve an investment policy. The policy is the framework in which investment decisions are made. The policy may be very simple, for example if the charity has limited funds to invest, or more sophisticated, for example, if the charity has significant permanent endowment to invest.

When setting the policy you need to be aware of the immediate, short, medium and long term plans and financial needs of the charity. The policy will also set out the level of risk you are willing to take. You must be satisfied that the overall risk is right for the charity and its beneficiaries.

This doesn't mean avoiding risk completely. For example, if you are investing funds that you know the charity will need in the short to medium term, the level of risk should be low. However, for funds invested for the longer term, the level of risk can be higher because short term drops in the capital value of invested funds will not impact the charity's operational capabilities.

Investment policy

A good investment policy will cover:

• What is the charity trying to achieve by investing?

• Attitude to risk.

• How much is to be invested and for how long?

• The types of investment the charity wishes to make.

• How will liquidity be managed

• How investment decisions are made.

• How investment performance is measured.

• How will the charity invest responsibly

• Role of investment managers

Investment policies shouldn't exist in isolation. They need to be linked into a charity's risk management process as well as its reserves policy and business interruption plans.

Investment policies should be regularly reviewed, as a minimum annual, to ensure they are fit for purpose and continue to serve the best interests of the charity. It is clear that the Charity Commission expect all charities that invest to have a written policy. To help appendix B to this guide contains an example policy that you can use to help you start the process – but this must be tailored to your specific needs.

What can you Invest in?

Investments that are very high risk or controversial are unlikely to be suitable. If you would be uncomfortable with your investment decision being reported in the media, this is an indicator it is not a suitable investment for a charity.

The most common forms of investment charities make are cash deposits, equities, government securities, unit trusts and property. You should consider diversifying your investments as a means of managing risk. You can invest ethically, but you must be able to justify why it is in the charity's best interest.

Charity Commission guidance CC14 is permissive towards the inclusion of "non-financial factors" being included in financial investments, explaining that it is up to trustees to determine what is in the best interests of their charity. It highlights that this might include investment approaches that avoid certain assets or identify specific investments for their environmental or social performance and use influence to create change. The guidance notes that the 'Butler-Sloss case' is now the "leading case in relation to the law on investment decision-making by trustees". It has been helpful to clarify that investments conflicting with the charity's purpose or harm its reputation can be excluded, even if it there are anticipated financial implications, as long as the decision is in the best interests of the charity.

It has also been made very clear that "As trustees, you must not allow your personal motives, opinions, or interests to affect the decisions you make." This can be a tricky position to navigate but it is important for Trustees to document their thought process and decision making.

How should you make Investment Decisions?

The investment policy and key decisions, including rationale, should be recorded in writing.

When making decisions you need to consider whether external advice is required. Where the only investment is moderate cahs deposits. this is unlikely. However, for complex or significant investment decisions this is likely to be necessary indeed the most recent guidance shows that the Commission expects all investing charities to take professional advice when making and reviewing investments. You could also consider appointing a trustee with specialist investment knowledge. When obtaining advice, you must ensure the person is suitably qualified and impartial.

For equity investments, an investment manager may be used. Even if youare delegated some investment decisions to an investment manager, you must retain overall control. This can be achieved by ensuring the investment manager acts only in line with your instructions, which are determined by your investment objective and policy.

Ther should also be a regular review of the suitability and performance of the investment manager. Investments in subsidiaries should be appraised jut like any other investments.

Monitoring Performance

Investment performance must be monitored. The 'how' and 'when' should be set out in your investment policy. You should compare performance with benchmarks and objectives. If investments are under or overperforming, you should determine why and consider whether it is acceptable. If it is not, you should prepare to act.

Social Investments

These are investments made both for financial return and to help meet the charitable objective. As discussed the primary concern here is being able to demonstrate that making the investment is in the best interests of the charity, taking into account both the financial return and advancement of the charitable objective.

Social investments however, are not permitted where there is an inappropriate level of private benefit as a result of the investment.

This is where charities can make mistakes, so take care. For example, investing in a project with a trustee may make financial sense, but if the private individuals or private companies will also obtain significant financial reward from the investment, and therefore obtain a private benefit, this is unlikely to be an appropriate investment.

Bank Deposits

Don't forget cash is an investment policy. Consider:

• Access: You must ensure that access to funds is compatible with the charity's cash demand

• Which institution: Cash should only be deposited with reputable institutions. Other factors to consider will be the rates of interest, location etc.

• Protection: The Financial Services Compensation Scheme (FSCC) offers protection to account holders on the first £85,000 of funds. You should decide whether to limit deposits in each institution to £85,000. Note that the compensation is available per UK banking license. Some banks, if part of the same group, will share a license, meaning accounts with two seamingly different banks will only have £85,000 available, for example HSBC and First Direct.

How do I know if I am doing a good job?

Cazenove have developed a helpful checklist which you can self-evaluate your performance.

How we can help

We recommend that all charities review their investment policy to confirm it remains relevant and is being applied. If you need any help with drafting an investment policy or with any other areas, please don't hesitate to get in touch with your local firm member.

How should you make Investment decisions?

The Charity Commission and the OSCR expect the charity's written records to document any conflicts of interest and how the trustees have dealt with them. The usual way is to record the trustees' decisions in the minutes of their meetings and where there is a conflict, the written decision should record:

- The nature of the conflict.
- Which trustee or trustees were affected.
- Whether any conflicts of interest were declared in advance.
- An outline of the discussion.
- Whether anyone withdrew from the discussion.
- How the trustees took the decision in the best interest of the charity.

How do I know if I am doing a good job?

- Do you check for conflicts at the start of each meeting?
- Do you ensure that trustees think about their wider connections, including family and business interests?
- Do you fully record (in writing) any conflicts and discussion in dealing with the issue?
- Are you aware of what your charity's governing document says about trustee benefit?

Preventing the Conflict From Affecting the Decision Making

Having identified a conflict of interest, trustees must then only act in the charity's best interest. This means that trustees must consider the issue of the conflict so that any potential effect on decision making is eliminated.

In practical terms this means that the conflicted trustee must:

- Declare the conflict to the wider board.
- The wider trustees must then consider removing the conflict of interest.
- The trustees must follow their charity's governing document and the law.
- Where the trustee benefit is authorised in advance, the affected trustee must be absent from any part of any meeting where the issue is discussed. Note the trustee affected should not vote or be counted in deciding whether a meeting is quorate.

Did you know?

- The Charity Commission's main guidance is document CC29 "Conflicts of interest: a guide for charity trustees".
- Trustees can be paid by or can receive benefit from the charity.
- Conflicted trustees, who have withdrawn from a decision, cannot be counted when ensuring the meeting is quorate.
- Trustees can be conflicted due to their wider family, their own business interests and their wider family's business interests.

How we can help

Review your charity's procedures about how conflicts of interest must be handled (create one if it doesn't already exist) and consult your charity's governing document. If you would like any assistance with developing your conflict of interest procedures, please don't hesitate to get in touch with your local MHA member firm.

Please do not hesitate to contact us if you would like help on any aspect on Conflicts of interest.

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