REDINGTON

CHARITY COMMISSION GUIDANCE

June 2022

Private and Confidential

ISO/IEC 27001 Information Security Management

QAS Institute and Faculty of Actuaries Quality Assurance Scheme

WHAT IS THE CHARITY COMMISSION GUIDANCE (CC14) ALL ABOUT?

Charities invest so that they can further their charitable aims. They can invest in a number of ways to achieve their aims, and there are specific legal duties and decision making processes attached to each.

This guidance sets out the legal and good practice framework for the investment of charity funds. This was released in 2011 with a few proposed changes in 2021 by the Charity Commission.

It acts as the ultimate replacement for the commission's 3 previous publications, which are Investment of Charitable Funds: Basic Principles (2004), Investment of Charitable Funds: Detailed Guidance (2003) and Charities and Social Investment (2003).

Why was it set up?

Set out to help make better decisions about investing charity funds so that they can further their charitable aims/goals.

What does it include?

Decision framework that covers the legal duties and principles as well as the associated risks of charity investments.

Who is it for?

Trustees and those who help trustees make investment decisions on the charities' assets.

OVERVIEW – TYPES OF INVESTMENT

Financial Investment

To yield the best financial return within the level of risk considered to be acceptable - this return can then be spent on the charity's aims.

Programme Related Investment

Use a charity's assets directly to further its charitable aims that may produce some financial returns.

Mixed Motive Investment

To justify an investment that is neither a financial investment nor a PRI as it is still in the best interests of the charity.

OVERVIEW – TYPES OF INVESTMENT
FINANCIAL INVESTMENT

What are the requirements for trustees?

1. Know, and act within, the charity's abilities to invest;
2. Exercise care and skill when making investment decisions;
3. Select investments that are right for their charity;
4. Take advice from expertise in investment matters unless they have a good reason for not doing so;
5. Follow the legal requirements if they are going to use someone to manage investments on their behalf;
6. Review investments from time to time; and
7. Explain their investment policy in the annual report.

What should the trustees also consider?

1. Decide on the overall investment policy and objectives for the charity;
2. Agree the balance between risk and return that is right for their charity; this may include a wide range of factors that will impact on return including ESG factors;
3. Have regard to other factors that will influence the level of return, such as the environmental and social impact of the companies invested in and the quality of their governance;
4. Be aware that some investments may have tax implications for the charity;
5. Invest any permanently endowed funds in a way that helps them to meet their short and long-term aims; and
6. Decide whether to adopt an ethical, socially responsible or mission related approach to investment and ensure that it can be justified.

What should charities with permanent endowment consider when making financial investments?

Charities that have a permanent endowment must keep the capital fund invested. Only the income earned from the investment of the capital fund can be spent on the charity's aims. In this way, trustees can aim to ensure that their investment portfolio will enable them to further the charity's aims both now and in the future.

OVERVIEW – TYPES OF INVESTMENT
PROGRAMME RELATED INVESTMENT (PRI)

How does this differ from financial investments?

PRI is different from financial investment in that the justification for making a PRI is to further the charity's aims (not to generate a financial return): this means that charities are not bound by the legal framework for financial investment.

What does this mean for the trustees?

Trustees must:

1. Be able to show that the PRI is fully used to further the charity's aims;
2. Ensure that any benefits to private individuals are necessary, reasonable and in the interests of the charity; and
3. Consider reasonable and practical ways to exit from a PRI if it is no longer furthering the charity's aims.

What form can a PRI take?

PRIs can take a wide range of forms and can be made to both charities and other types of organisation. They can range from:

- relatively small sums of money provided as loans to another organisation or individual, for example a housing deposit, buying new equipment or renovating a property; to
- large sums invested in complex high profile projects, for example regeneration projects.

Should trustees take advice when making PRIs?

There is no legal obligation to take advice. Much will depend on whether the trustees feel comfortable and competent enough to make decisions on PRIs.

OVERVIEW – TYPES OF INVESTMENT MIXED MOTIVE INVESTMENT

How does this differ from financial investments and PRI?

Where an investment cannot be wholly justified as either a financial investment or a PRI, it may be possible to justify it as a mixed motive investment.

What does this mean for the trustees?

Trustees should consider:

1. The justification for making the mixed motive investment that will need to be established before making the investment;
2. The suitability of a mixed motive investment for the charity;
3. Whether there is a need to take professional advice before making the investment; and
4. Whether any private benefit arising from the investment will be acceptable.

THE LEGAL FRAMEWORK FOR FINANCIAL INVESTMENT

Can all charities make financial investments?

A charity's specific powers of investment may depend on its constitutional form. The charity commission breaks this into:

Unincorporated charities have a 'general power of investment'. This allows trustees to invest the charity's funds in any asset that is specifically intended to maintain and increase its value and/or produce a financial return. The governing document may set out additional provisions, restrictions or exclusions on the types of investments a charity can make; these may take priority over, or affect, the general power of investment.

Charitable companies investment powers are normally set out in its articles of association and are usually similar to the general power of investment referred to above. Where a charitable company acts as a trustee of an unincorporated charity, the 'general power of investment' applies.

What must trustees consider when making financial investment decisions?

Trustees must:

1. Use their skills and knowledge in a way that is reasonable in the circumstances ('the duty of care').
2. Consider how suitable any investment is for their charity; trustees must be satisfied that:
    i. An investment type or class is appropriate for the charity;
    ii. The investment within that type or class is appropriate for the charity;
    iii. Consider the need to diversify investments;
    iv. Take advice from someone experienced in investment matters where they consider they need it; and
    v. Review investments (and their investment manager) from time to time, changing them if necessary.

PROVIDING ADVICE TO CHARITIES

What arrangements should a charity put in place to make decisions about investments?

Charities trustees have overall responsibility for investment decisions. However, trustees should:

1. Deliberate whether it might be helpful to have a trustee with investment knowledge on its board, or whether establishing an internal investment committee might be useful.

2. Detail their investment approach and document key decisions.

3.Decide what frequency they should review the investments.

What advice must be taken by the trustees?

Trustees must take and consider advice from someone experienced in investment matters before making investments and when reviewing them, unless they have good reasons for not doing so. They may decide not to take advice if they conclude that it is unnecessary, or inappropriate in the circumstances.

PROVIDING ADVICE TO CHARITIES

Should a charity manage investments itself or use the services of an investment adviser or manager?

The charity's trustees should decide whether it would be more efficient to manage their investments by:

- Managing their investments themselves where they have necessary expertise;
- Using advisory investment firms; or
- Using discretionary investment firms

When deciding this approach, trustees should consider:

- Whether they have the skills required;
- The amount they are able to commit for investment; and
- The cost of this.

What should trustees consider when appointing investment managers

If a charity decides to use an investment manager(s), its trustees should:

- Satisfy themselves that an investment manager can perform effectively in line with their investment objectives and policy; and
- Consider how the services offered by a number of different managers meet their needs.

As trustees have overall responsibility for the investment of a charity's funds, it is best practice to have:

- A written agreement or contract with any investment manager appointed; and
- An investment policy for the charity which clarifies the responsibilities and remit of the investment manager.

It is worth noting a trustee is not liable for any act or default of the investment manager unless he or she has failed to comply with their duty of care.

SETTING A CHARITY'S INVESTMENT OBJECTIVES

Purpose: A charity needs to be clear about what it wants to do, how it intends to do it and what the timescale for delivery will be. These considerations will govern how it decides what its investment objective will be.

How should a charity set its investment objectives?

1. Determine the considerations, examples include:

- Immediate financial needs.
- Future spending commitments.
- Whether the charity has restricted funds.
- Longer term organisational objectives.
- Past patterns of expenditure and anticipated demand for the charity's support as an indication of future trends.
- Unplanned changes in activity or events that may impact on the charity.

2. Identify funds that:

- Need to be available on instant access.
- Can be used for short term investment.
- They can afford to tie up for longer periods of time.
- Will be used to react to unplanned events.

What risks should a charity consider when making investments?

Capital Risk	Liquidity Risk	Market Risk	ESG Risk	Tax Risk	Counterparty Risk	Valuation Risk

What should an investment policy include?

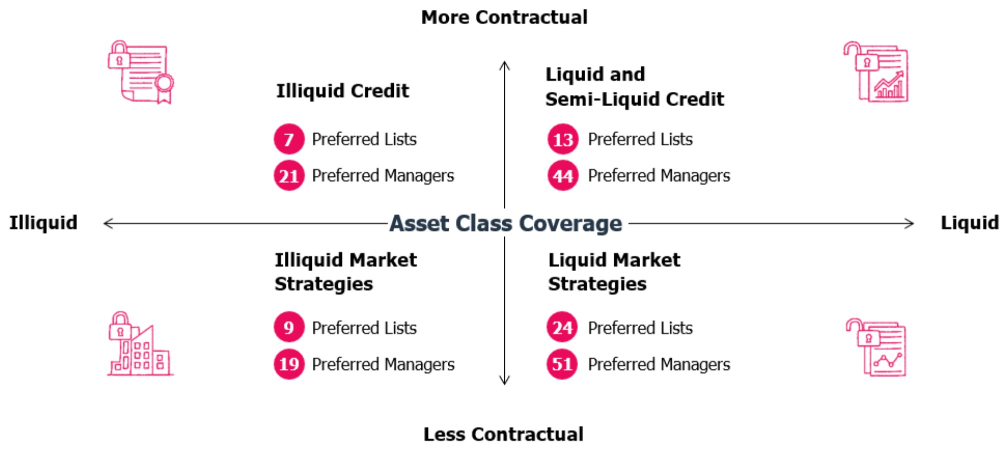
1. Scope of its investment powers
2. Charity's investment objectives
3. Attitude to risk
4. How much is available for investment, timing of returns and the liquidity needs
5. The types of investment it wants to make (this might include ethical considerations)
6. Who can take investment decisions
7. How investments will be managed and benchmarks and targets set by which performance will be judged
8. Reporting requirements for investment managers

WHAT CAN CHARITIES INVEST IN?

Overview: Trustees can make financial investments in any asset that is specifically intended to maintain and increase its value and/or produce a financial return.

What to consider when deciding the asset class to invest in?

1. How suitable any investment is for their charity - this will be influenced by the charity's attitude to risk across its investment portfolio.
2. The need to have a mix of assets in their portfolios - this can protect the charity's investments from sudden variations in the market and reduce the risk of the loss.



Trading vs investing

If trustees purchase an asset with the intention of selling it for a profit after a short amount of time, it is likely to be considered as trading. This is important because:

- A charity itself can only undertake trading activity when this is directly furthering or supporting its aims; and
- Profits made from trading are not always subject to tax relief.

Collective investment schemes

Collective investment schemes are investment vehicles where the assets of individual investors are pooled together with other investors. These investments can reduce investment risk in a more cost effective way.

A collective investment scheme which many use is called a Common Investment Fund (CIF).

CIFs are regulated charities themselves and only charities established in the UK can invest in CIFs.

CIFS give charities of any sizes to ability to invest in a tax efficient and diversified way with exposure to many asset classes.

MONITORING A CHARITY'S INVESTMENTS AND PERFORMANCE

What should a Charity's trustees monitor?

Trustees must keep their investment portfolio under regular review. Reviews must cover:

- How investments are performing; and
- The service provided by the investment manager, if one is used.

Reviews should also incorporate internal arrangements for managing a charity's investments.

How should investment performance be monitored?

Trustees should decide on a system of target returns (e.g. benchmarks) against which they can measure the performance against. The precise nature of these benchmarks and targets will vary for each charity. Trustees may wish to take expert advice from an independent organisation on this.

If investments are underperforming, trustees should seek to understand whether it is for an acceptable reason. Similarly, if funds are performing significantly above average, trustees should ensure that it is not because the charity is exposed to greater risks than it is prepared to accept.

How and when should the service provided by the investment manager be reviewed?

Trustees must consider:

- Whether the terms under which the investment manager is acting are suitable;
- How well the manager is performing;
- Whether the manager continues to be a suitable person to carry out the function;
- Whether the terms of the appointment remain appropriate; and
- Whether the manager is complying with the policy statement.

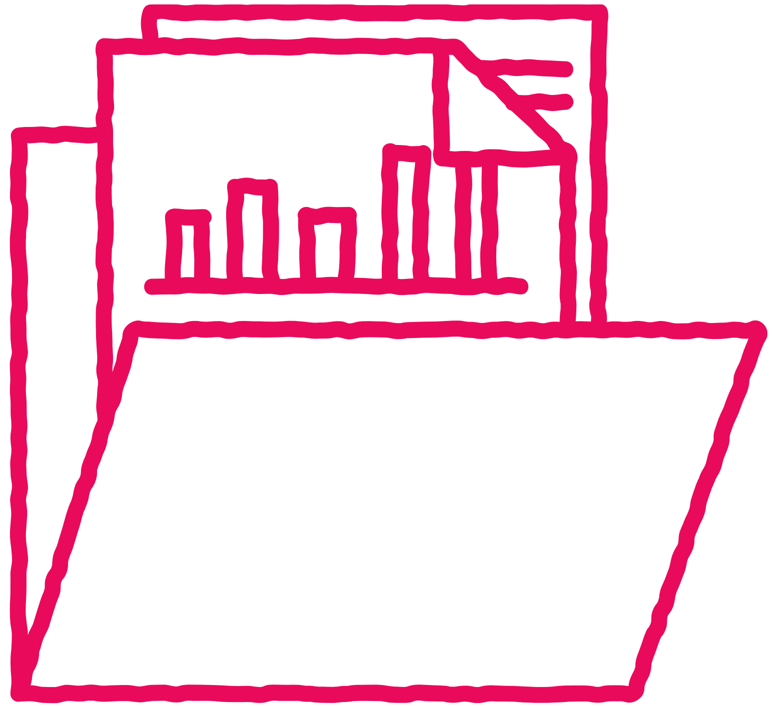
Trustees may decide to hold reviews on a regular basis or they may hold one in response to other events.

THE TOTAL RETURN APPROACH

What does this mean?

Under this approach, the form in which investment return is received (e.g., income, dividend and capital growth) does not matter. As such, investments are managed to maximise the total investment return.

Charities that do not have permanent endowment can adopt this approach without the commission's consent.



What does this mean for the trustees?

This gives trustees greater flexibility in achieving the investment objectives as it focuses on return rather than balancing capital growth and income.

As a result, trustees are free to allocate an appropriate proportion of the total return (e.g., 10% of the capital growth) as income. This income can then be spent on furthering the charitable aims. Any unallocated return is carried over and reinvested as capital.

WHAT DOES ETHICAL / RESPONSIBLE INVESTMENT MEAN FOR A CHARITY'S FINANCIAL INVESTMENTS?

What does the current guidance stipulate with regards to ethical investments?

Trustees of any charity can decide to invest ethically, even if the investment might provide a lower rate of return than an alternative investment. Ethical investment means investing in a way that reflects a charity's values and ethos and does not run counter to its aims. However, a charity's trustees must be able to justify why it is in the charity's best interests to invest in this way. The law permits the following reasons:

- A particular investment conflicts with the aims of the charity;
- The charity might lose supporters or beneficiaries if it does not invest ethically; or
- There is no significant financial detriment.

Is the current guidance changing?

In January 2020, the Charity Commission began a listening exercise to help it understand the barriers that may deter trustees who wish to make responsible investments from doing so. As a result, the Charity Commission has developed an updated draft of the opening sections of the guidance: these include an explanation of trustees' ability to adopt a responsible investment approach. For the meantime, this remains a draft whilst the Charity Commission seeks to understand whether it will provide greater clarity about the discretion trustees have to make responsible investments and to reassure trustees that they can decide to adopt a responsible investment approach in most circumstances.

What does the draft wording specify?

Trustees can decide that rather than just focusing on the financial return of an investment, their approach will also take into account the charity's purposes and values.

All charities can take this approach, but charity's must:

- Base decisions on what's best for the charity; and
- Follow the rules (set out below) for a permanent endowment (or if a charity has a duty to invest).

Trustees can take a responsible investment approach even if there is no apparent direct conflict with a charity's charitable purposes, if trustees can show this is in the best interests of the charity.

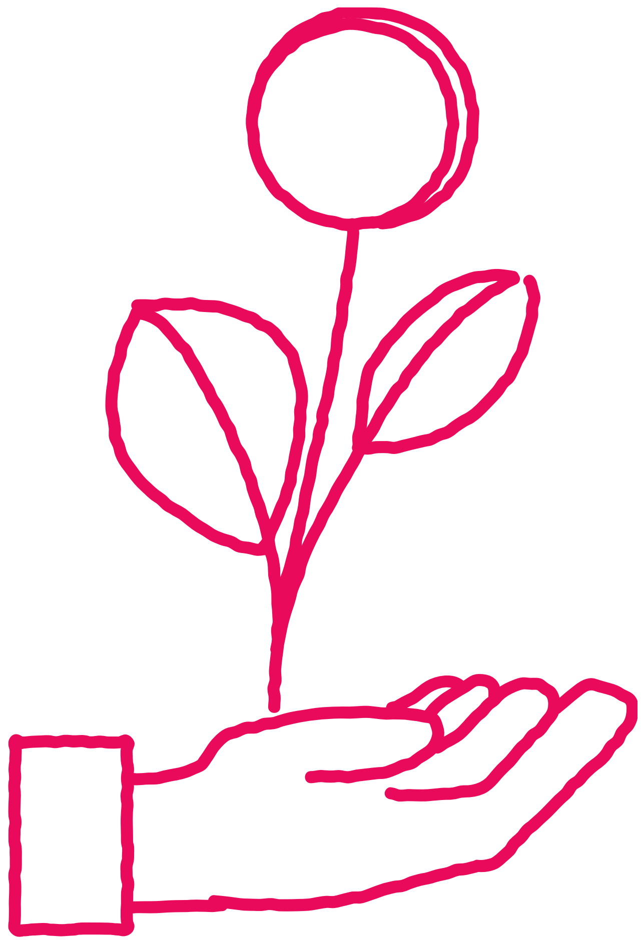
WHAT DOES ETHICAL / RESPONSIBLE INVESTMENT MEAN FOR A CHARITY'S FINANCIAL INVESTMENTS?

What are the extra rules for a permanent endowment?

These different rules apply to a permanent endowment because it is subject to a duty to invest. Permanent endowment's must aim for the best financial return within the level of risk that has been decided is appropriate for the charity.

Permanent endowments can still take a responsible investment approach if:

- Trustees are satisfied that this is clearly in the best interests of the charity, and
- One or more of the following applies:
    - Trustees are avoiding an investment that conflicts directly with the purposes of the charity;
    - The charity might lose supporters or beneficiaries if trustees don't take a responsible investment approach;
    - Taking this approach would not bring a significant financial downside;
    - The charity's governing document allows or requires a responsible investment approach; or
    - Trustees have clear and compelling reasons about why the charity should follow a responsible investment approach.



CONTACTS

Tom Wake-Walker
Director

tom.wake-walker@redington.co.uk

Tara Gillespie
Head of Global Assets

tara.gillespie@redington.co.uk

FINANCIAL NEWS
INVESTMENT CONSULTANT OF THE YEAR
2021

PIPA AWARDS
INVESTMENT CONSULTANT OF THE YEAR
2021

CORPORATE ADVISER
BEST DC INVESTMENT ADVISER
2021

PENSIONS FOR PURPOSE
BEST BLOG CONTENT
2021

PROFESSIONAL PENSIONS UK PENSIONS AWARDS
DC INNOVATION OF THE YEAR
2020

PENSION INSIGHT DC AWARDS
BEST INNOVATION IN DC
2017

EUROPEAN PENSIONS AWARDS
RISK MANAGEMENT FIRM OF THE YEAR
2017

FINANCIAL NEWS AWARDS FOR EXCELLENCE
INVESTMENT CONSULTANT OF THE YEAR
2017

LONDON STOCK EXCHANGE
1000 COMPANIES TO INSPIRE BRITAIN
2016

EUROPEAN PENSIONS AWARDS
CONSULTANCY OF THE YEAR
2016

Disclaimer

For professional investors only. Not suitable for private customers.

The information herein was obtained from various sources. We do not guarantee every aspect of its accuracy. The information is for your private information and is for discussion purposes only. A variety of market factors and assumptions may affect this analysis, and this analysis does not reflect all possible loss scenarios. There is no certainty that the parameters and assumptions used in this analysis can be duplicated with actual trades. This document is based on information available to Redington Ltd at the date of publication and takes no account of subsequent developments after that data. Further, any historical exchange rates, interest rates or other reference rates or prices which appear above are not necessarily indicative of future exchange rates, interest rates, or other reference rates or prices. Neither the information, recommendations or opinions expressed herein constitutes an offer to buy or sell any securities, futures, options, or investment products on your behalf. Unless otherwise stated, any pricing information in this document is indicative only, is subject to change and is not an offer to transact. Where relevant, the price quoted is exclusive of tax and delivery costs. Any reference to the terms of executed transactions should be treated as preliminary and subject to further due diligence.

Please note, the accurate calculation of the liability profile used as the basis for implementing any capital markets transactions is the sole responsibility of the Trustees' actuarial advisors. Redington Ltd may estimate the liabilities if required but will not be held responsible for any direct, indirect or consequential loss or damage howsoever sustained as a result of inaccuracies in that estimation.

Additionally, the client recognises that Redington Ltd does not owe any party a duty of care in this respect.

Redington Ltd are regulated by the Financial Conduct Authority. Redington Ltd do not advise on all implications of the transactions described herein. This information is for discussion purposes and prior to undertaking any trade, you should also discuss with your professional tax, accounting and / or other relevant advisers how such particular trade(s) affect you. All analysis (whether in respect of tax, accounting, law or of any other nature), should be treated as illustrative only and not relied upon as accurate.

Redington Limited (6660006) is registered in England and Wales. Registered office: One Angel Court, London, EC2R 7HJ.

Floor 6, One Angel Court, London EC2R 7HJ
+44 (0)20 7250 3331
www.redington.co.uk