INTENTIONAL INVESTING

ASSOCIATION OF CHARITABLE FOUNDATIONS

THE PRINCIPLES, PRACTICALITIES AND PITFALLS

WHETHER AND HOW TO DEVELOP A CHARITY'S INVESTMENT STRATEGY WITH ITS VALUES AND AIMS IN MIND

RICHARD JENKINS
KATE ROGERS

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We advocate intentional investing, which means that trustees have thought about the management and use of their charity's assets so that their approach supports the delivery of their charitable aims. They are able to explain their approach and, as far as possible, anticipate and review the impact of their decisions in terms of their mission and values, beneficiaries, and supporters.

This report aims to help trustees identify what is right in their context.

WHY THIS REPORT NOW?

- To cut through detailed technical guidance that leaves many charity trustees unsure how to find the approach that is right for them
- To present a range of views and practices, putting the focus on the discretion and options that trustees have
- To add to a series of ACF reports on charity investment governance.

RESEARCH APPROACH

- 286 respondents to a survey of charity investors
- Focus group discussions in London and York with charity practitioners including trustees and senior staff
- In-depth consideration by an expert reference group
- Desk research
- Individual conversations, interviews and contributions by charity investment practitioners
- Case studies.

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Richard has a degree in Scots and English law from the University of Dundee and has further graduate and post-graduate degrees from the Universities of Oxford and Leeds. As a Civil Servant in 2002 he led implementation of key funding elements of the 2002 Treasury cross-cutting review into the role of the voluntary and community sector in the delivery of public services. He has been a Trustee of a grant-making endowed charitable foundation, Chief Executive of an educational charity, and holds a law society accredited certificate in mediation.

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Kate is chair of the Charity Investors' Group (CIG), recently working with HM Treasury, the Charity Commission and the Financial Conduct Authority on establishing the new Charity Authorised Investment Fund structure announced in the 2015 budget.

Kate regularly writes on charity investment in the sector press. With CIG and Charity Finance Group she produced a guide to written investment policies. In 2013 she co-authored *For Good and Not For Keeps*, with Richard Jenkins, published by ACF.

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We owe particular thanks to the members of our Reference Group for sharing so generously their insight, knowledge and expertise.

We are deeply grateful for the participation of those who responded to our survey or offered to take part in further research and those who attended our focus groups. Without their openness, and that of the numerous others whom we have spoken with, we could not have written this report. Special thanks are due to those who provided case study material: James Fitzpatrick; Chris Mills; Jackie Turpin and Fiona Young.

We would like to thank all those who have provided additional support, content, references, and expert views. There are too many to name, but among them the following deserve special mention: Jon Hoare of ShareAction; Giles Neville and Alexia Zavos of Cazenove Charities; the Joseph Rowntree Charitable Trust for kindly hosting a focus group.

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Finally, we extend our thanks to Charity Finance Group and the National Council for Voluntary Organisations for help in promoting the survey.

EXECUTIVE SUMMARY

Only trustees can decide whether and how to reflect their charity's mission and values in its investment strategy. Research for this report found that doing so is becoming increasingly mainstream.

IS THERE A TENSION BETWEEN MAKING MONEY AND DOING GOOD?

Put simplistically, while charities are driven solely by their charitable aims, the performance of the stock market is fundamentally driven by financial objectives. For some charity investors this creates tensions. The law requires that trustees in all circumstances manage their assets with the sole purpose of furthering their charitable aims. However, as our case studies illustrate, what is right for one charity is not going to be the case for another. Therefore, rather than telling trustees what to do when investing their money, this report aims to help them identify what is right in their context. The fold-out section at the back of this report distils our key research findings to help trustees find the right approach for their charity.

MANAGING INVESTMENTS WITH MISSION IN MIND IS BECOMING INCREASINGLY IMPORTANT

Charities need funding to support their activity. Many rely on voluntary donations, legacies or earned income to support their day-to-day mission. In some cases, when it's not appropriate to spend the money as they receive it, or in the case of a very large gift, trustees invest it for future or on-going benefit. How charities do that varies in practice.

Some trustees feel that their mission or values entail no specific approach to managing their investments beyond keeping a firm eye on seeking the best financial return they can reasonably make while taking account of risks. However, a survey carried out for this research found a substantial increase in recent years in the number of charities choosing to manage their investments in ways that specifically reflect their mission or values. 59% of the 286 charity investors who replied to the survey in 2014 had a policy in place or plans to implement one, compared with only 23% with a policy five years before. This research suggests therefore, that for charity investors, thinking about their investments with their mission in mind has become increasingly important.

THERE ARE MANY DIFFERENT DRIVERS AND MANY DIFFERENT CONTEXTS

There are many drivers for that change. Participants in focus groups undertaken for this report suggested that improved regulatory guidance has helped: it makes it clear that the law does not require charity investors to pursue investment returns at the expense of their charitable mission, their organisation's reputation, or in ways that could alienate donors or beneficiaries.

Participants also cited new generations of trustees joining boards who felt that investment practice should align with the charity's mission, values or wider social goals. Discussions revealed that board conversations improved when strategic decisions were taken – as they should be – by the whole board and not just by a minority of those who had investment expertise. It could be therefore that more charities are looking at their investing and programme activity holistically. What such joined-up discussions seem to unlock is the range of possibilities trustees have at their disposal when they consider how best to use all their assets to pursue their mission. Those assets include financial and non-financial assets, such as a charity's reputation, the know-how of trustees and staff, their networks, and trustees' ability to gather key stakeholders together.

THERE ARE A NUMBER OF APPROACHES

If a charity's trustees take an in-principle decision to reflect its mission and values in its investment strategy, they have a number of ways of doing that and must balance a range of practical factors.

We found four main approaches taken by those who wished to manage their investments with their charity's mission in mind. By far the most common, comprising 78% of survey respondents who had a policy, were approaches that **exclude** specific industries or companies from an

> **There can't be one answer for all charities, as there are myriad drivers and contexts.**
>
> Focus group participant, London

> **The question trustees now ask themselves is 'we have an asset, so how do we best use that to achieve our aims?'**
>
> Focus group participant, London

investment portfolio – with tobacco being the most popular exclusion. A more contemporary example is the campaign calling on trustees to 'divest' from carbon-based energy industries.

By contrast, 34% of respondents with a policy in place aimed positively to **select** companies that align with their aims or rate well in terms of environmental, social and governance (ESG) factors.

22% of respondents were seeking to **influence** companies' behaviour by engaging with them or using their share-voting rights to affect company policy. Finally, 17% of the total survey population had decided to use their assets to **deliver** tangible outcomes that directly related to their mission through social investment.

PRACTICALITIES NEED TO BE THOUGHT THROUGH

When deciding what approach, if any, to take charity investors will want to consider a range of practical factors.

One is to weigh up the possible effect any approach may have on investment returns, allowing for the fact that charity investors can take a financial 'hit' to protect their mission or reputation. Citing research, we present evidence to show that while 'sin stocks' in such industries as tobacco, alcohol, arms, and pornography have historically delivered premium returns, their overall contribution to portfolios means that the effect of their exclusion in financial terms can be minimal, depending on the number excluded. We also cite research that shows that investing in companies with positive ESG records can make good financial sense. Similarly, influencing and engaging with companies to improve their behaviour can be financially rewarding because successful engagement tends to enhance company value and therefore investment returns.

Practically speaking, nearly all charity investors will manage their investments indirectly, through investment managers and/ or their pooled funds. For very bespoke policies, therefore, compromises may need to be made in relation to the capacity of the manager's market to deliver them and the internal staff and governance time required for monitoring. Nonetheless, the market is developing and more pooled funds and services are becoming available.

Only trustees can be expert in what their charity's objectives require. Nonetheless, those who took part in this research stressed the importance of appointing managers who not only performed well in financial terms, but who could also empathise with the charity's distinctive mission and culture while communicating and collaborating effectively.

Practitioner discussions also highlighted the importance of collaboration between charities who, despite the relative smallness of their overall contribution to the investment market, have a powerful asset in their reputation to help influence corporate change.

GETTING GOVERNANCE RIGHT WILL HELP AVOID PITFALLS

In repeated conversations, practitioners stressed the importance of the whole board being involved in agreeing the investment strategy and having the right governance and staff structures in place to implement, monitor and review it. Experienced practitioners also called for humility when setting strategy, observing that there was not a single 'right' answer. Trustees should never see the 'perfect' as being the enemy of the 'good'.

On the basis of that sound advice, this report advocates **intentional investing** which means that trustees have thought about the management and use of their charity's assets so that their approach supports the delivery of their charitable aims. They are able to explain their approach and, as far as possible, anticipate and review the impact of their decisions in terms of their mission and values, beneficiaries and supporters.

KEY PRINCIPLES

1. Charity trustees are obliged to use their resources in ways that best meet their charitable objectives.
2. Charity trustees are not obliged to pursue investment returns at the expense of their charitable mission, their organisation's reputation, or in ways that could alienate donors or beneficiaries.
3. Removing certain industries or companies from your charity's investment portfolio needn't significantly impact on financial returns.
4. Positive action to target or enhance sustainable business practice can also be financially rewarding.
5. Charity trustees don't have to manage their investments to reflect their organisation's values or objectives.
6. There is no 'one size fits all' answer.

THE CHARITY INVESTMENT LANDSCAPE

While charities are driven by charitable aims, the performance of the stock market is driven primarily by financial objectives. For some charity investors this creates tensions.

WHY DO CHARITIES HOLD INVESTMENTS?

Most charities need funding to support their activity. Many rely on voluntary donations, legacies or earned income to support their day-to-day mission. In some cases, when it's not appropriate to spend the money as they receive it, or when they receive a very large gift, trustees invest it for future benefit. Investing often means trustees give up some measure of direct control over their money. And, in the simplest terms, while charities are driven primarily by their charitable aims, the performance of the stock market is fundamentally driven by financial objectives. For some this creates tensions. This report examines what those tensions are and proposes key principles and questions to help trustees decide what practice is right for their charity.

THE INVESTMENT LANDSCAPE

Charities invest for a variety of reasons; as reserves, to use the returns to fund their ongoing charitable activities, or to build up assets for future charitable expenditure.[1] Whatever their reason, rather than spending all of their funds immediately on their charitable aims, charity trustees have chosen to invest in companies, governments and financial institutions, with all the complexity, risks and opportunities for future benefit that this may bring. To manage that complexity, trustees often entrust the charity's assets to investment experts – advisers and managers – to invest on their behalf and manage their investments on a day-to-day basis.

Trustees can't delegate their responsibility for deciding how best to use their assets, so managers' actions are governed by the trustees' investment policy.[2]

The written investment policy will set out what the charity is aiming to achieve with its investments and provides a framework for making investment decisions. It will also set out how much risk the trustees are prepared to take in relation to their investments, as all investment activity involves accepting some degree of risk. As part of that decision, trustees will need to consider what mix, or 'portfolio', of different types of investments will best meet the trustees' financial objectives and risk appetite, because different types of investments, like equities, government or corporate bonds and property, perform in different ways.

Trustees may ask for expert help in implementing their policy, working with investment managers to decide what sort of assets to invest in, for example, whether to use 'pooled funds', where different investors' assets are managed as one investment pot to achieve scale and efficiency.

In most cases investment managers make the day-to-day decisions of what to buy, and when to sell specific investments in response to the movements and fluctuations of the investment markets.

The investment manager's aim is to meet their client's investment objectives. They provide regular feedback to trustees on how their investment portfolio is performing against this aim.

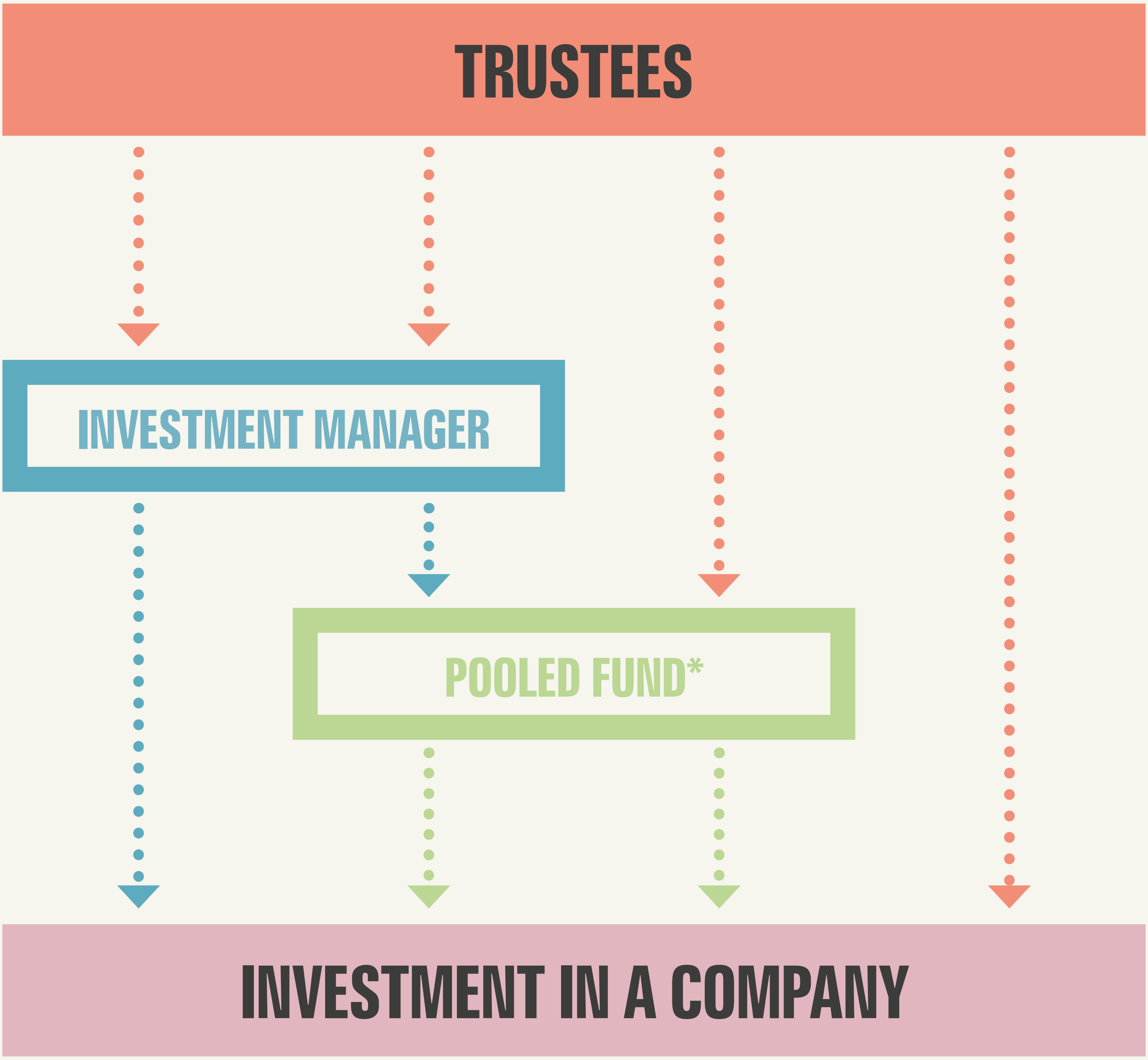
Trustees are therefore several stages removed from the individual companies in which their charity's capital is invested. So trustees, apart from the few charities that invest on their own behalf, generally give up the day-to-day management, and often knowledge, of exactly where their money is invested. They rely on investment experts' skill to ensure that – at the very least – their money is being managed in accordance with their policy.

Charity trustees will often invest in a range of companies that are producing financial returns by pursuing their own objectives. These objectives won't be the same as the aims or objects of the charity. Only trustees can determine the degree to which they can and can't compromise their own mission or values when formulating their investment strategy, and even whether they want to use their assets not just to generate financial returns but directly to further their charitable aims.

TRUSTEES' PROXIMITY TO THEIR INVESTMENTS

Trustees don't have direct control over their assets – to a greater or lesser extent they rely on a series of intermediaries to invest in the various companies and assets that generate financial returns.

> **A lot of boards are well short of knowing the impact of what they currently do – neither trustees nor advisers are expert. Trustees can feel disempowered.**
>
> Focus group participant, London



*Pooled funds are managed by investment managers.

CHARITY INVESTORS AND THE LAW

Trustees' overriding duties are to use their charity's assets to deliver the purposes for which the trust was created, and to be prudent when doing so.

CHARITABLE OBJECTIVES ARE AT THE HEART OF ALL ACTIVITY

There are general legal duties – 'fiduciary obligations' – on all those who have been entrusted with assets on behalf of others. Their central thrust is that trustees' main duty is to deliver the purpose for which the trust was created and to be prudent when managing the resources of the trust.[3] While for pension and private trusts, and for some charities, that may well indeed be aiming for the best risk-adjusted financial return, a charity's overriding purpose is to deliver a set of charitable objectives and so, in the words of an earlier court judgement, achieving maximum risk-adjusted financial return is only a 'starting point'.[4] Trustees may therefore use their assets in a range of ways in order to best serve their charitable objectives, taking account of any restrictions on their use of the charity's assets which may be set out in its governing document – for example, whether trustees must preserve the capital value in perpetuity.

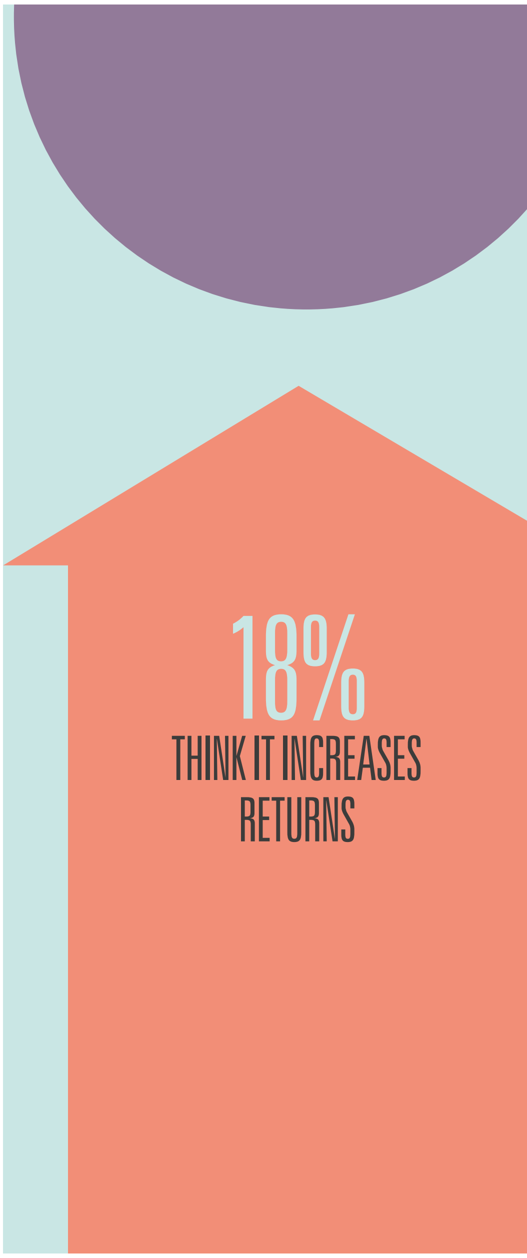
The Charity Commission for England and Wales has set out in guidance what legal powers trustees have when investing, and what factors they must take into account when doing so.[5] Charities in Scotland are regulated by the Scottish Charity Regulator (OSCR) and in Northern Ireland by the Charity Commission for Northern Ireland (CCNI). The law in the different countries rests on similar principles and a shared case law tradition.

Charity trustees are able to take action to avoid investing in ways which conflict with their charity's aims or which might damage the charity's reputation so as to alienate supporters or beneficiaries, even if excluding those investments entails making a below market rate of return. That means trustees can 'screen out' from their portfolio certain industries or companies.

Trustees can also positively select industries to align with their mission, while making a financial return. There is increasing exploration of the ways charity trustees can invest to directly deliver something positive for their mission – known as 'social investment' – even, in some cases, trading financial gain for a social return that delivers the charity's aims.

Trustees can't delegate setting their charity's investment strategy. They must take advice however if as a board they don't have sufficient investment expertise.

The law doesn't require trustees to manage their investments in ways that align with their charity's values or objectives – it does however give them power to do so. The questions facing trustees are, what is their intention and what options do they have?



> **There can't be one answer for all charities, as there are myriad drivers and contexts.**
>
> Focus group participant, London

> **The question trustees now ask themselves is 'we have an asset, so how do we best use that to achieve our aims?'**
>
> Focus group participant, London.

IS THERE A TENSION BETWEEN DOING GOOD AND MAKING MONEY?

We asked charity investors what effect managing their investments to reflect their charitable objectives, values or wider social goals would have on investment returns.

57%
THINK IT MAKES NO DIFFERENCE TO RETURNS

25%
THINK IT REDUCES RETURNS

MISSION AND VALUES – INVESTMENT OPTIONS

There are many terms to describe 'ethical' and 'responsible' investment approaches. We don't attempt to define them all, but group the most common into four main approaches.

1600s
EXCLUDE
76%

1980s
SELECT
34%

EVOLVING APPROACHES

Approaches to reflecting a charity's values or mission through its investments have evolved over the years. We use our survey data to illustrate how commonly each approach is used by today's charity investors.

EXCLUDE

Approaches that focus on excluding certain investments were used as early as the 1600s by the Quakers but were more widely adopted in the 1970s. These approaches, often known as **negative screening** focus on avoiding harm by 'screening out' companies whose activity directly conflicts with a charity's aims or values, or whose activities would alienate supporters or beneficiaries. Most frequently these are investments relating to the manufacture of armaments or tobacco, or the publication of pornography. This is the most common charity investment practice, chosen by 76% of those survey participants with an investment policy that reflects their charity's mission or values.

A more contemporary version known as **divestment** tends to be linked to campaigns or movements, like the exclusion of apartheid South Africa in the 1970s or the campaign to divest from carbon-based energy which began around the mid 2010s.

SELECT

Increasingly adopted in the 1980s, 'inclusionary' approaches are those where investors seek to select investments that specifically align with their aims or a wider social goal. 34% of our survey participants with a policy that reflects their charity's mission or values reported that they select investments. This might involve:

Positive screening by targeting investments in companies whose business or practices align with the charities aims, values or a wider social good.

Best-in class favours companies that have historically performed better than their peers within a particular sector based on environmental, social and governance factors **(ESG)**.

Responsible investment practice integrates the analysis of ESG factors within the mainstream investment process, thereby influencing all investment decisions.

> Whether you own 100% or 10% or 1% or 0.1% of an arms company, you still own part of that company. Everything that company does is being done in your name.
>
> Research participant, York

> Responsible investment means different things to different people.
>
> Focus group participant, London

> Responsible investment carries with it the implication that others are irresponsible, and that's not necessarily the case.
>
> Focus group participant, York

2000s
INFLUENCE
22%

2010s
DELIVER
17%

INFLUENCE

More recently, an increasing number of investors are seeking to use their share ownership rights to influence and change company behaviour in line with accepted best standards of environmental, social or governance practice or in ways that reflect the charity's objectives, values or wider social goals. This takes seriously the fact that shareholders have a stake in the company they invest in and can use this to influence the way the company is governed. This influence can be exerted by:

Engagement uses shareholding rights to initiate direct communication with companies to improve corporate behaviour. Influence may be enhanced by collaborating with other investors or may achieve extra leverage through investment managers who manage large blocks of shares.

Voting uses share voting rights to back or oppose certain policies at company AGMs.

22% of our survey participants with a policy that reflected their mission, values or wider social goals said they aimed to influence the companies they invested in.

DELIVER

Social investment aims to deliver tangible outcomes that directly contribute to a charity's mission while at the same time achieving a financial return. Social investment has received more attention and wider uptake in recent years, but there is a long history of some charities providing, for example, repayable finance to beneficiaries. 17% of our survey participants said that they had made social investments, an increase of 50% compared with those numbered in ACF research 15 months before.

LIKELIHOOD OF INVESTING WITH MISSION AND VALUES IN MIND

286 charity practitioners responded to our survey. Over 80% were grant-makers and nearly 80% depended on investment returns. The results give a unique insight into the behaviour of these sorts of organisations.

UNIQUE RESEARCH INTO CHARITY INVESTORS

ACF and Cazenove Charities carried out a survey of charity investors in late 2014, with the cooperation of Charity Finance Group and the National Council of Voluntary Organisations. 286 charity professionals or trustees responded to the survey, with over 80% of them describing themselves as grant-makers and just under 80% citing investments as their primary or secondary source of income. 59% of survey respondents said that they had already decided to manage their investments to reflect their charity's values, objectives or wider social goals. The results of the survey aren't representative of all charities, but they do give a unique insight into the behaviour of these sort of organisations.

Among organisations that were most likely to have a policy were those with defined objectives, and those with a strong values base – such as the promotion of religion, peace and conflict resolution, overseas development and social justice and human rights.

Organisations whose focus one might say was more 'pragmatic', such as science and technology, higher education or arts and culture, were less likely to have a policy.

Respondents to our survey who were dependent on public appeals for their income were much more likely to have an investment policy that reflected their charity's values, objectives or wider social goals than those who had 'independent' incomes derived from investments.

LESS LIKELY

HISTORY AND OBJECTS:

General Objects
Pragmatic
Grant makers
Older

RESOURCE BASE:

Financially independent
Less assets
Less staff

ATTITUDE:

Believes policy reduces returns

59%

OF CHARITY RESPONDENTS HAD DECIDED TO MANAGE THEIR INVESTMENTS TO REFLECT THEIR CHARITY'S VALUES, OBJECTIVES OR WIDER SOCIAL GOALS.[6]

MORE LIKELY TO INVEST WITH MISSION IN MIND IF DEPENDENT ON PUBLIC FOR INCOME

HISTORY AND OBJECTS:

Specific Objects
Values based
Operating
Younger

RESOURCE BASE:

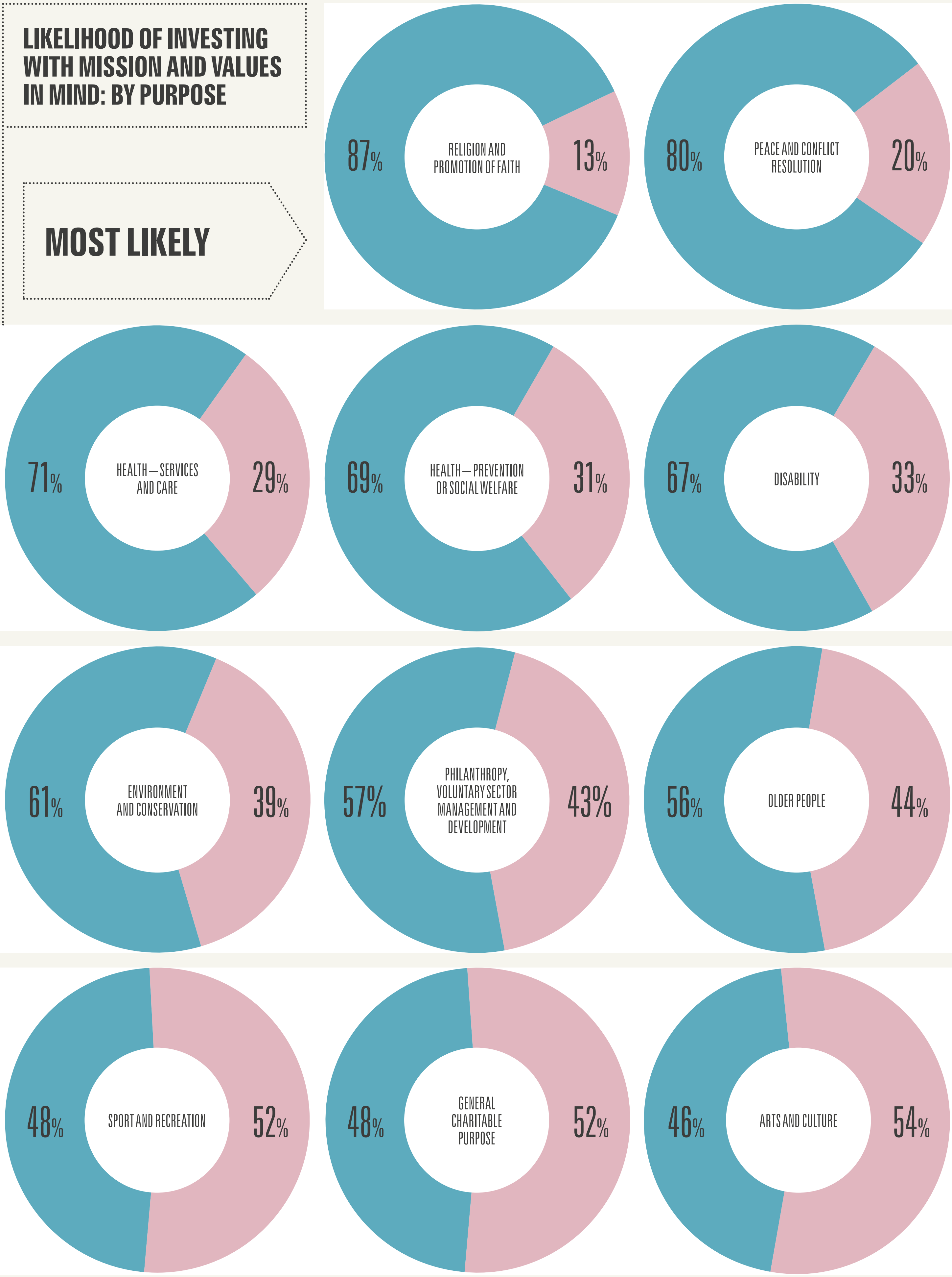
Financially dependent on public
More assets
More staff

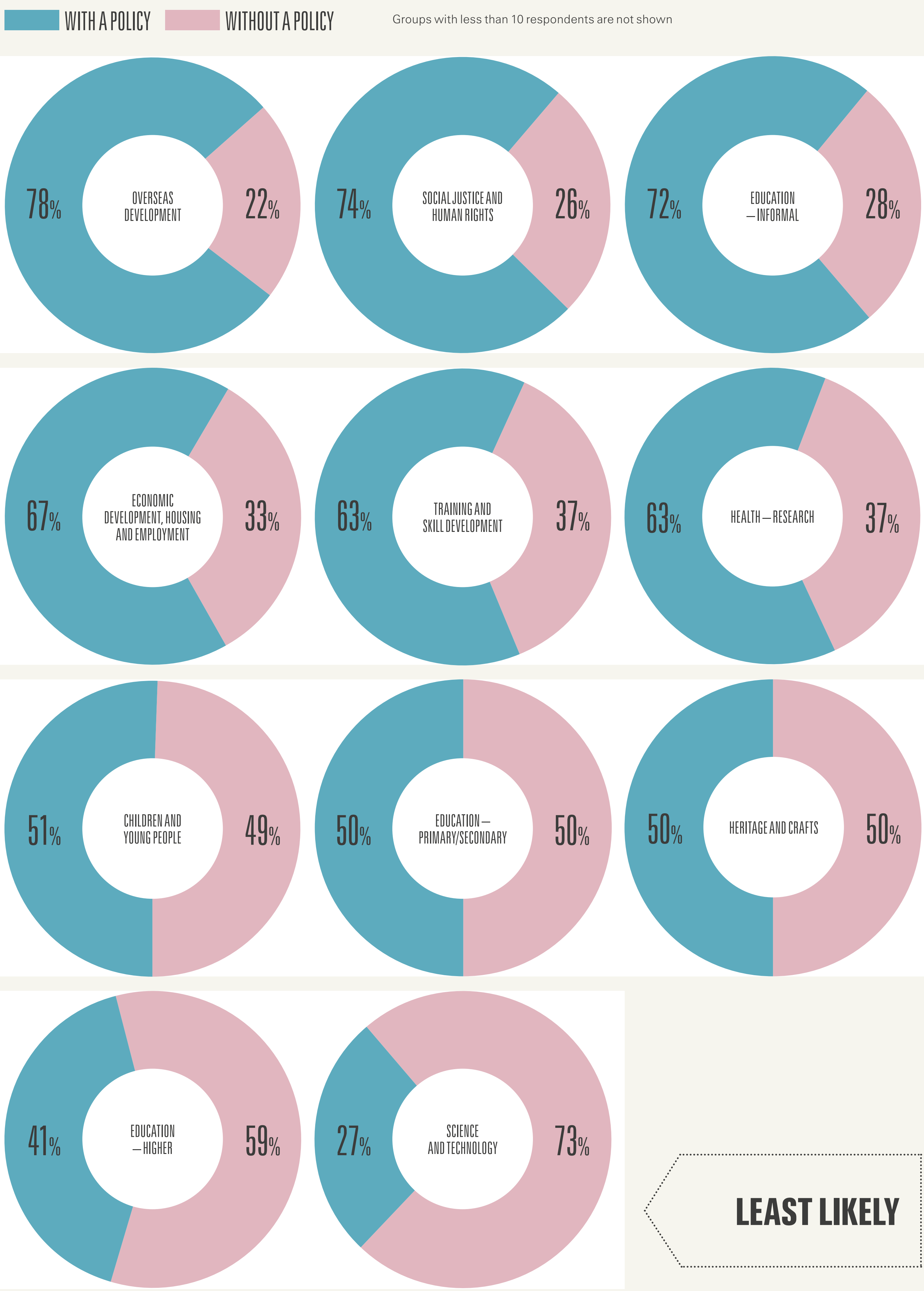
ATTITUDE:

Believes policy improves returns

MORE LIKELY

LIKELIHOOD OF INVESTING WITH MISSION AND VALUES IN MIND: BY PURPOSE

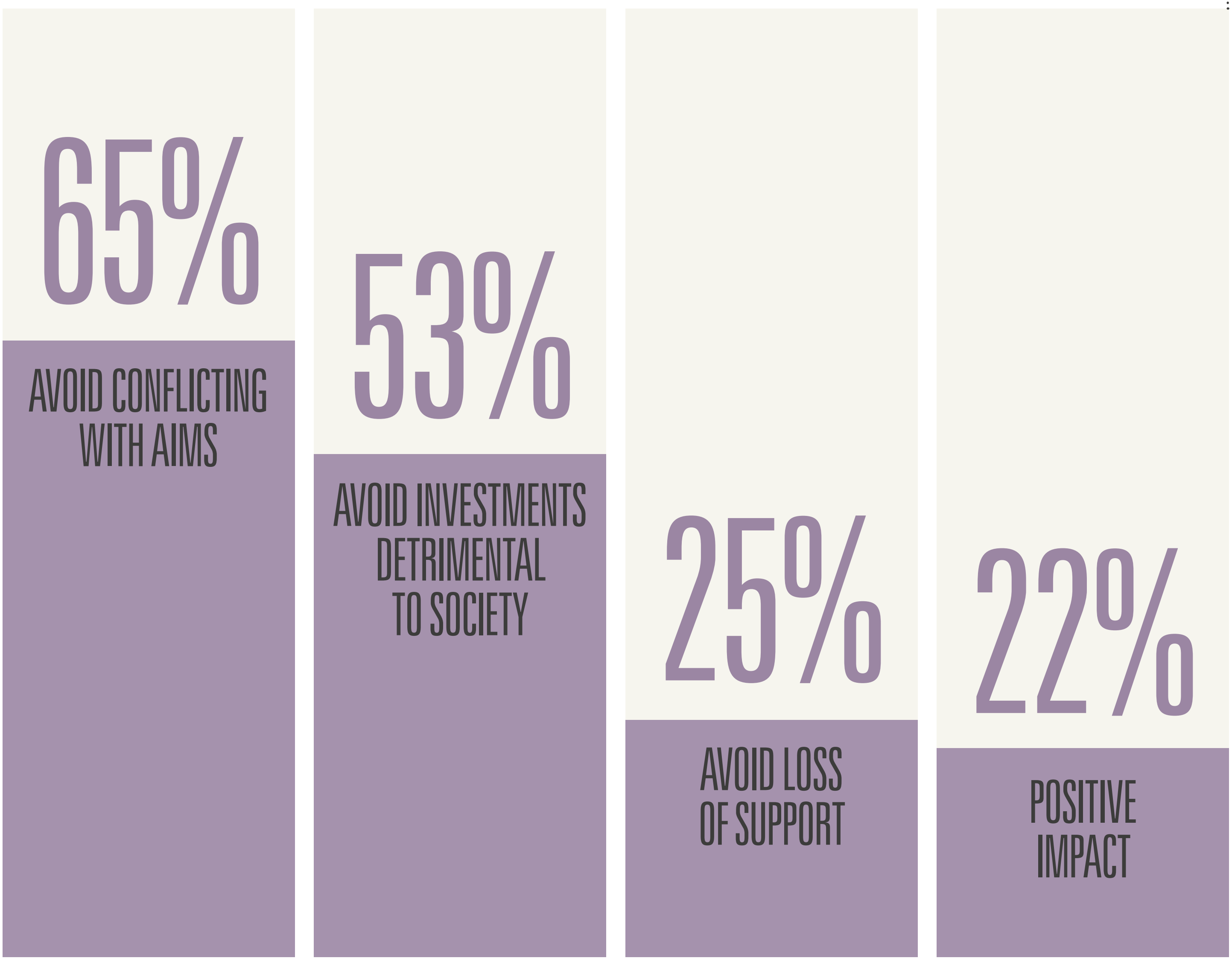



WITH A POLICY
WITHOUT A POLICY
Groups with less than 10 respondents are not shown
OVERSEAS DEVELOPMENT
78%
22%
SOCIAL JUSTICE AND HUMAN RIGHTS
74%
26%
EDUCATION – INFORMAL
72%
28%
ECONOMIC DEVELOPMENT, HOUSING AND EMPLOYMENT
67%
33%
TRAINING AND SKILL DEVELOPMENT
63%
37%
HEALTH – RESEARCH
63%
37%
CHILDREN AND YOUNG PEOPLE
51%
49%
EDUCATION – PRIMARY/SECONDARY
50%
50%
HERITAGE AND CRAFTS
50%
50%
EDUCATION – HIGHER
41%
59%
SCIENCE AND TECHNOLOGY
27%
73%
LEAST LIKELY

WHAT DRIVES ATTITUDES AND BEHAVIOURS?

Our research sheds light on the reasons why trustees choose, or don't choose, to manage their investments in ways that explicitly reflect their charitable mission or values.

REASONS TO ADOPT A POLICY



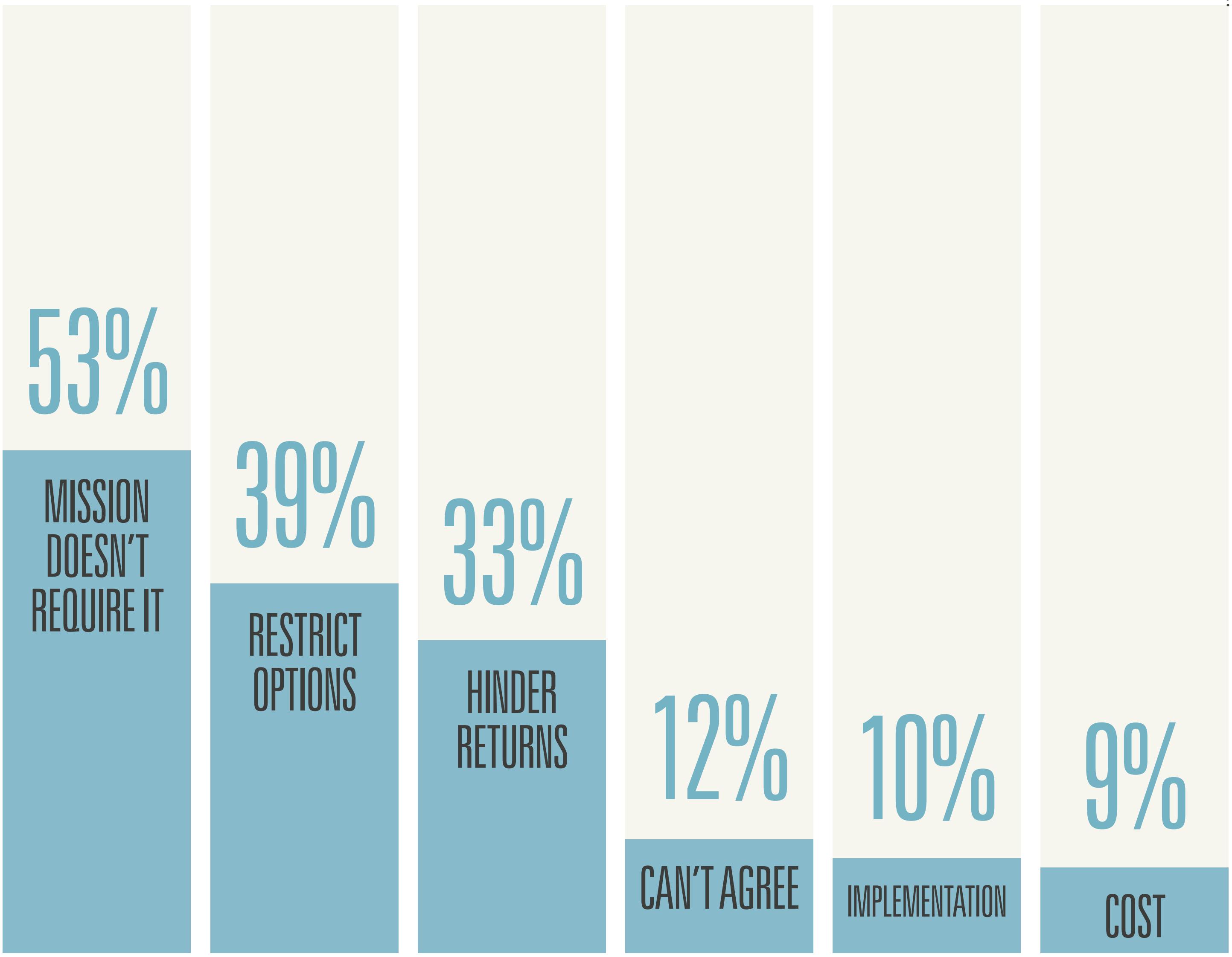
> For charities to be good citizens requires no higher standard than any member of the public.
>
> **Focus group participant, London**

> How we spend our money as individuals expresses who we are. The same is true of charitable foundations.
>
> **Focus group participant, York**

> When we have more money, we can do more good.
>
> **Focus group participant, London**

> There are more advisers and products than there were thirty years ago, so it's easier now.
>
> **Focus group participant, York**

REASONS NOT TO ADOPT A POLICY



THE EFFECT ON RETURNS

While 'sin' stocks provide premium returns, excluding them can have a minimal effect on investment returns. Selecting companies with good practices and influencing others to improve can be financially rewarding.

SIN PAYS…

A common belief is that excluding certain investments damages overall returns. 'Sin stocks' such as tobacco, armaments, alcohol, gambling and pornography are thought to offer attractive financial returns, and so some argue that screening them out from investment portfolios disadvantages beneficiaries in financial terms by reducing returns.

SIN STOCKS HAVE BEEN SHOWN TO GENERATE BETTER RETURNS OVER THE LONG TERM

Recently published research[7] examined the long term evidence and found that 'sin' can pay. For example, the analysis of long-term returns from tobacco shares shows these companies outperforming the market by 3% each year in the UK over the 85 years from 1920 to 2014.

+3% per year better performance of UK tobacco companies as compared to the UK market from 1920-2014.

Dimson, Marsh and Staunton, February 2015[7]

It is worth highlighting that the tobacco sector currently represents only 5% of the UK equity market, suggesting a 0.2% per annum performance headwind for those excluding this sector, based on history. A similar pattern of outperformance of other 'sin' stocks can be seen across different countries and markets over the long term.

Why might this be? The research proposes that fewer people want to own 'sin' stocks, and that this is reflected in a lower price. It is well documented that companies whose shares have a low price relative to how profitable the company is, are likely to generate the best financial return for investors. This 'valuation argument' could explain the better historic returns shown by 'sin' stocks. It can also be argued that these stocks provide reliable returns in economic downturns because during such periods consumer demand for their goods and services often remains stable while spending elsewhere falls.

Excluding a group of stocks or sectors from a portfolio restricts the 'universe' or range of options for asset managers; with the result that either overall returns might drop, income may be limited, or the portfolio might experience greater 'volatility' – short-term fluctuations in value. These are factors that trustees will have to take into account when tracking the performance of their investments.

However, it is worth remembering that 'sin stocks' only ever make a partial contribution to a diverse investment portfolio. Research by Andrew Ang (2014)[8] examined the forward looking impact of exclusions on a global equity portfolio and found that the risk and return penalty of screening is minimal, as these stocks tend to represent a relatively small proportion of the market. However, the larger the exclusion list, the larger the potential impact on the expected risk and return.

'Sin stocks' only ever make a partial contribution to a diverse investment portfolio.

100% of the academic studies agree that companies with high ratings for CSR and ESG factors have a lower cost of capital

Sustainable Investing, DB Climate Change Advisors, June 2012

+2% per year better performance of the 'high sustainability' portfolio as compared to the 'traditional' portfolio

Harvard Business School, November 2011[10]

AND SO DOES VIRTUE…

While policies that exclude certain stocks can be detrimental to returns, policies that help investors to select and improve companies through influence can be shown potentially to enhance value.

Research[9] published in 2012 examined more than 100 academic studies of sustainable investing around the world. It found that taking into account environmental, social and governance (ESG) policies when selecting investments can improve returns. The majority of studies showed that companies with strong environmental, social and governance policies tended to offer better financial performance whilst also potentially being more sustainable in the long run.

These 'good' companies are deemed to be lower risk investments compared to those with similar financial characteristics, but with less sustainable business models. Lower risk companies are more profitable because they benefit from a lower 'cost of capital', meaning that they pay less for investment capital when they want to grow or expand.

However, the same research[11] that explained the success of 'sin' stocks by their lower valuations highlighted that the converse could be true; that the selection of 'good' companies might bias investments towards higher valuations and lower future returns. This emphasises the importance of the integration of both financial and ESG factors in investment decisions.

It can also explain why policies that seek to influence and improve corporate behaviour can have a positive impact on returns. As a company's behaviour improves, it becomes lower risk and, in theory, moves from a lower valuation 'socially bad' stock, to a higher valuation 'good' stock – increasing its value in the process.

IN SUPPORT OF ENGAGEMENT[12]

7%

IMPROVEMENT IN PERFORMANCE IN THE YEAR FOLLOWING A SUCCESSFUL ENGAGEMENT

18%

SUCCESS RATE OF ENGAGEMENT, WITH AN AVERAGE LENGTH OF 1 – 2 YEARS

Academic evidence suggests that engagement can enhance returns, but that success rates are low and positive change can take a considerable amount of time to effect. Research suggests that, in the past, engagement has been more effective when done in private[13] , something to be balanced against the desire for transparency in both voting and engagement practices.

Because voting and engagement policies can be resource intensive, often it is the larger investors with the assets and the access to company management, that are most active and influential. For most charity investors this means that engagement usually happens through their investment managers.

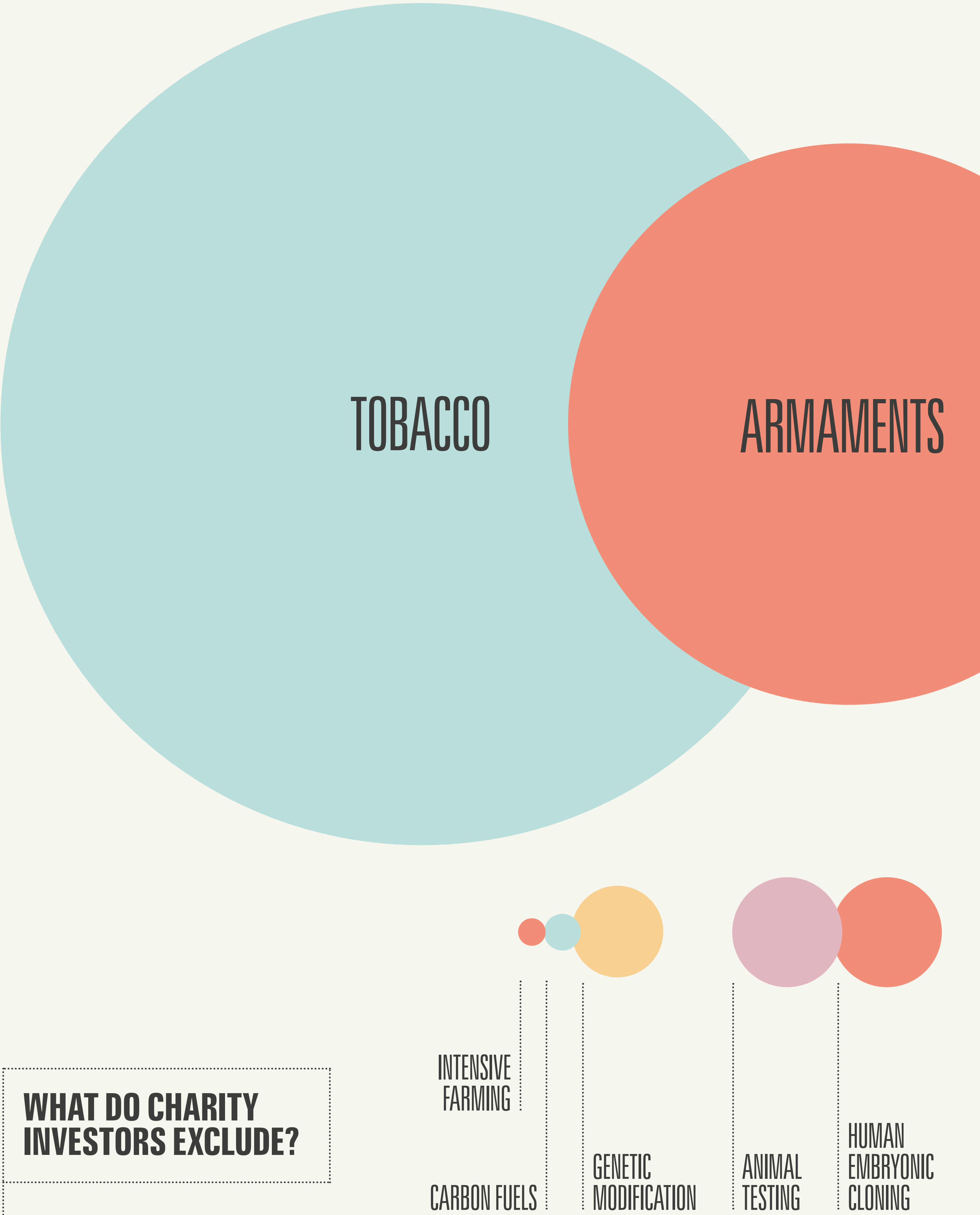
On the other hand, more charities are beginning to collaborate with each other, recognising that in their brand and reputation they have a further asset to lever that may allow influence beyond that based on the scale of their shareholding alone.

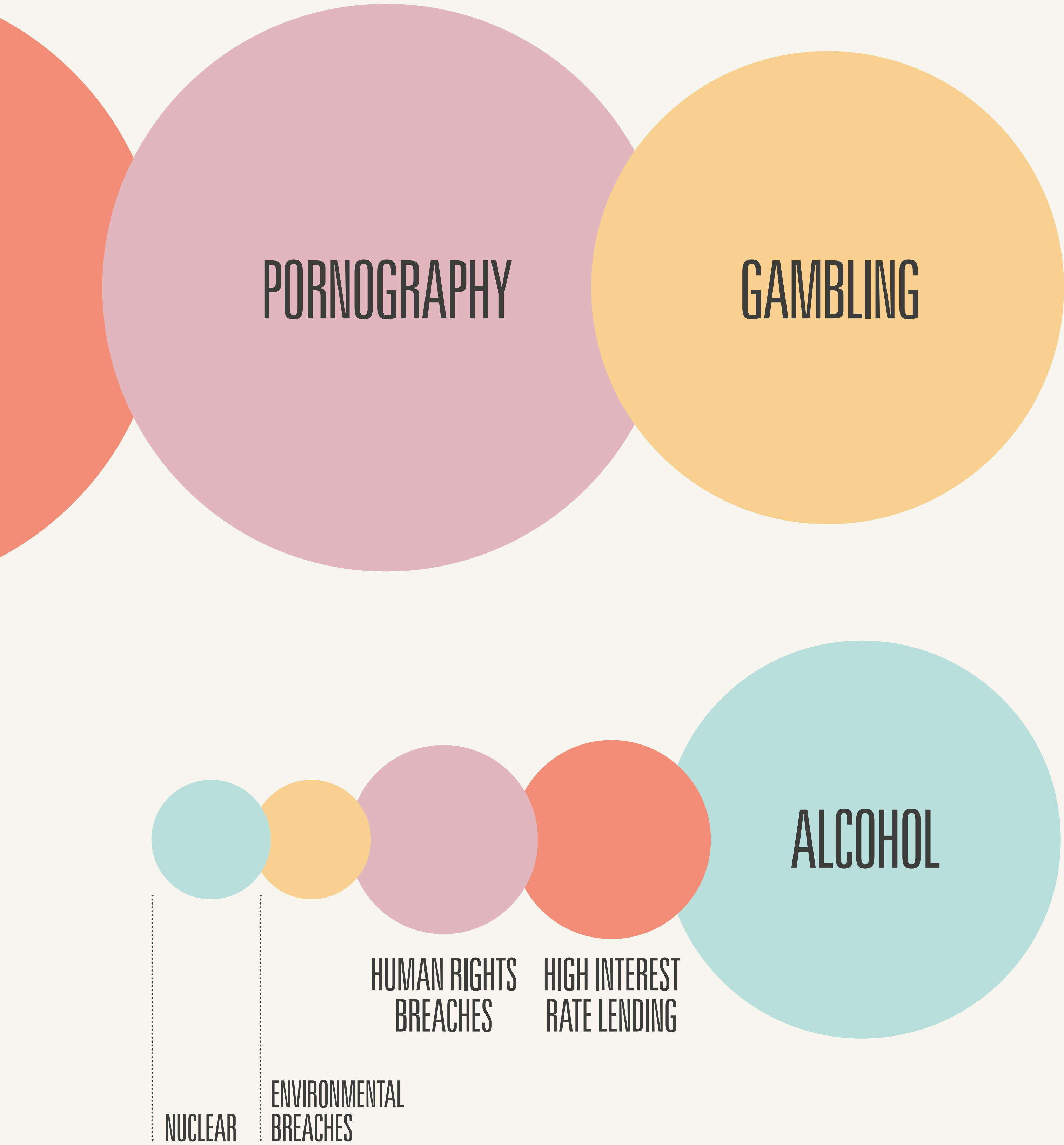
THE VALUE OF COLLABORATION

A good example of responsible investment at work is the shareholder project on the Living Wage led by the charity ShareAction. Since 2011, co-ordinated investor engagement with the boards of FTSE 100 companies has led to 24 such firms becoming accredited Living Wage employers. Thousands of the poorest workers in the UK are better off as a result.

The value of collaboration between responsible investors has been highlighted by foundations in the Charities Responsible Investment Network.[14] Members share knowledge and experience around responsible investment, receive training, and work together to influence companies in their portfolios on social and environmental issues.

WHAT DO CHARITY INVESTORS EXCLUDE?




PORNOGRAPHY
GAMBLING
ALCOHOL
HUMAN RIGHTS BREACHES
HIGH INTEREST RATE LENDING
NUCLEAR
ENVIRONMENTAL BREACHES

FROM MINORITY INTEREST TO MAINSTREAM PRACTICE

Thinking about investments with mission in mind has moved from being a minority concern to an accepted part of mainstream charity practice.

FROM MINORITY TO MAJORITY

Previous chapters show that thinking and practice has changed over the years on whether and how trustees might incorporate charitable objectives, values or wider social concerns into the management of their investments. Our evidence suggests that the pace of change is quickening, so that thinking about investments with mission in mind has moved from being a minority concern to being an accepted part of mainstream practice.

Among those responding to our survey, in 2009 only 23% had a policy in place to manage their investment in ways that reflected their mission or values. By 2014 that number had increased substantially, with a majority – 59%, now having a specific policy in place or planning to implement one.

Our survey suggests therefore, that for charity investors, thinking about their investments with their mission in mind has become increasingly important. We think there are a number of possible drivers for that change.

YOUNGER TRUSTEES WITH DIFFERENT IDEAS

Focus group participants reported again and again that new, younger, trustees joining their boards typically had different attitudes. 'It seems to be simply taken for granted that of course we should have a responsible investment policy', one participant observed.

MORE READILY AVAILABLE PRODUCTS

Another driver seems to be the increasing number of products available for charity investors. That growth may be related to better evidence that charity investors need not necessarily sacrifice financial returns when attempting to invest in line with their charitable objectives or values. It is also likely to be in response to increased demand from investors and evolving best practice among investment managers who recognise that integrating environmental, social and governance factors into the investment process is a way of adding long-term financial value as well as being better for society and the planet.

PUBLIC OPINION

A poll[15] of people who worked for, volunteered for or donated to charities found that 78 per cent of those surveyed agreed that they would think worse of a charity if they knew it had funds invested in activities contrary to its specific work and values.

This gap between the expectations of those who support charities and what current charity practice actually is creates a space for more questions to be asked of charity trustees by potential donors and beneficiaries.

INCREASED INFORMATION

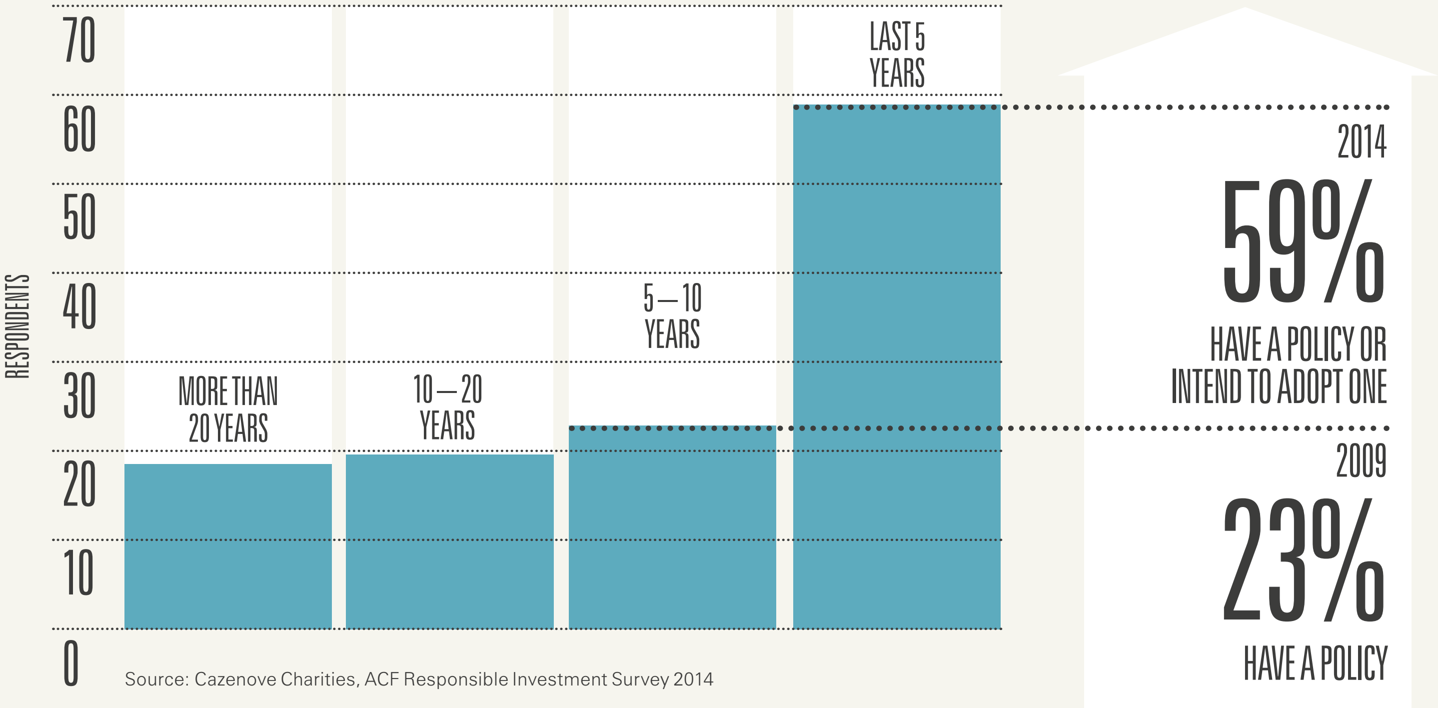
The internet makes it possible for individuals to trace the impact of investments in ways simply not open to previous generations. Further momentum is added by social media campaigns, which can shine a spotlight on the actions of individual industries or companies. Campaigns soon come to the attention of investors themselves – or they have their attention drawn to them by the media.

NEW PERSPECTIVES FOLLOWING THE FINANCIAL CRISIS

The financial crisis which began in 2008 revealed the inner workings of the financial system in ways that left the public and investors alike asking important questions about how their money was being used. The changed views of corporates, and of corporate ethics, resulting from the crisis has driven change in the investment management industry and among charity investors, with much greater demands for transparency, accountability and information about the impact of investments on society.

REGULATORY CHANGE

Regulatory changes may also be providing a trigger point for trustees to think about their investments. The Charity Commission's updated guidance has made the options clearer to trustees. And the new Statement of Recommended Practice on charity accounting (The SORP),



Source: Cazenove Charities, ACF Responsible Investment Survey 2014

active from January 2015, now requires charities to state 'the extent (if any) to which it takes social, environmental or ethical considerations into account in its investment policy.'[16]

FROM INDIVIDUAL MISSION TO WIDER SOCIAL CONCERNS

Regardless of the external drivers for change, one thing has not changed: the core of trustees' legal duties is to do the best they can to serve their charitable objectives.

As our timeline showed, there has been a development in practice over the years. Arguably, history has come out on the side of those pioneering new ethical or responsible approaches. At first greeted with scepticism, many of these approaches have, as our survey suggests, now become accepted aspects of mainstream practice. And not just for charity investors alone – international standards, such as the principles for responsible investment, have become standard for institutional investors of all kinds.

This forward trajectory forms a key strand of the argument put forward by those advocating for investors to take account today of the way the industries they support shape the future – with perhaps climate change providing the single most compelling focus. Taking account of future generations of beneficiaries, campaigners argue, means tackling now those factors which will adversely impact on their livelihoods in the future, not least the sustainability of the earth's ecosystem on which we all depend.

The Law Commission[17] has considered the argument that taking a short-term approach to investments and factoring out such concerns works against the longer-term considerations trustees should have in mind when thinking about their beneficiaries. In the context of pension funds, whose overriding purpose is to provide a financial return, the Law Commission found that trustees could take into account a range of wider social issues when setting investment strategy, but only if beneficiaries suffered no financial detriment.

The question remains, then, about the way these arguments touch charity trustees. In some cases they may have charitable objectives or values that justify suffering that detriment either because investment practice conflicts with those aims, because they will suffer reputational damage by continuing to invest in companies in ways that might alienate their supporters or beneficiaries, or because tackling the issue contributes directly to their charitable mission. Might this distinctive perspective make charity trustees more likely than other investors to take such factors into account?

Whatever the case, as our final section shows, trustees must balance a range of considerations – of both a principled and practical nature – when deciding what is right for their specific charitable aims.

CAMPAIGN FOR DIVESTMENT FROM FOSSIL FUELS

'Divestment' is the opposite of investment. While investment means buying investments in order to generate financial returns, 'divestment' means removing particular equities, bonds or funds. Fossil fuel divestment seeks to avoid investing in fossil fuel companies. One measure suggests that there are 200 publicly-traded companies that hold the vast majority of listed coal, oil and gas reserves. Other interpretations concentrate only on the most carbon-intensive businesses.

The divestment campaign has gathered pace since it began in 2013. The rationale for the campaign is both values driven, because investments shouldn't contribute to climate change, and financial, on the basis that the reserves held by these companies are 'stranded' and cannot be burned without exceeding the international climate change target to stay below 2 degrees warming.

FINDING THE APPROACH THAT'S RIGHT FOR YOUR CHARITY

There is no 'one size fits all' approach for charity investors, but certain common principles and questions can help trustees find the approach that is right for their organisation.

KEY PRINCIPLES

1. Charity trustees are obliged to use their resources in ways that best meet their charitable objectives.
2. Charity trustees are not obliged to pursue investment returns at the expense of their charitable mission, their organisation's reputation, or in ways that could alienate donors or beneficiaries.
3. Removing certain industries or companies from your charity's investment portfolio needn't significantly impact on financial returns.
4. Positive action to target or enhance sustainable business practice can also be financially rewarding.
5. Charity trustees are not obliged to manage their investments directly to reflect their organisations values or objectives.
6. There is no 'one size fits all' answer.

WHAT OUR RESEARCH SHOWS...

So far in this report we've found that the law for charity investors is permissive when it comes to reflecting a charity's values or objectives in managing their investments.

Trustees don't have to make maximum investment returns regardless of the damage that may cause to their mission or at the risk of alienating supporters or beneficiaries. What trustees must do is keep in mind the purposes for which their charity was set up and, rather than pursuing personal values, have in mind their ultimate beneficiaries' needs when they manage their charity's investments.

Our research showed that in practice charity investors adopt a wide range of strategies, ranging from simply making financial returns a priority, to excluding some companies or industries from their portfolios, from using more active tactics such as selecting companies with good environmental, social and governance records, to using their voting rights or engaging directly with businesses to improve their practices. They may also use their investments to directly deliver their mission.

Market research shows that in doing so, the rapidly increasing numbers of charity investors who are managing their investments in ways that reflect their organisation's values or objectives are not necessarily sacrificing returns. Evidence even suggests that, in some cases, the pursuit of responsible business practices can be positive from a financial as well as a values perspective.

Anecdotal evidence suggests that increasing numbers of investment advisers are developing products and services to meet such customer demand.

The question then is what approach is right for your organisation? The final part of the report highlights some of the things trustees might bear in mind when deciding, and identifies some questions to provoke board discussion.

STARTING AND ENDING WITH YOUR CHARITABLE OBJECTIVES

The first – and final – place for trustees to look in determining how to manage their charity's investments is the charitable objectives as set out in the governing document. The answers may not be obvious and implementation may be difficult. However, in deciding how to proceed, the key is always to keep the needs of the charity's ultimate beneficiaries in mind when designing a charity's investment policy.

> **The focus of [an] investment policy should be on using the charity's capital to do good rather than merely preventing it from doing harm.**
>
> **Comic Relief Investment Review Panel Recommendations[18]**

> **For charities to be good citizens requires no higher standard than any member of the public.**
>
> **Focus group participant, London**

> **Personally I would not invest in tobacco, but our charity is active in [a country] where tobacco is a vital export earner.**
>
> **Survey respondent**

The risks of negative consequences stemming from investment practices that are perceived to run counter to your mission or values are particularly pronounced for charities that depend on public support for their income.

This is also a concern for organisations that wish to maintain the support of individuals or groups that they would like to work with in the future.

However, it's important to think about investments in positive terms too, and consider the range of ways that trustees can harness all of the charity's assets to deliver its objectives. Crucially, these assets will include non-financial assets alongside those listed on the balance sheet, such as the organisation's convening power, the skills and expertise of staff and trustees, the time that they have to devote to tackling an issue, and the organisation's reputation to name a few.

INTENTIONAL INVESTING

We advocate 'intentional investing' which means that trustees have thought about the management and use of their assets so that their approach supports the delivery of their charitable aims. They are able to explain their approach and, as far as possible, anticipate and review the impact of their decisions in terms of their mission and values, beneficiaries, and supporters.

Our research suggests that alongside their financial objectives, increasing numbers of trustee boards believe it is important to think about the impact of their investments on achieving their charitable mission and the need to maintain credibility with key stakeholders.

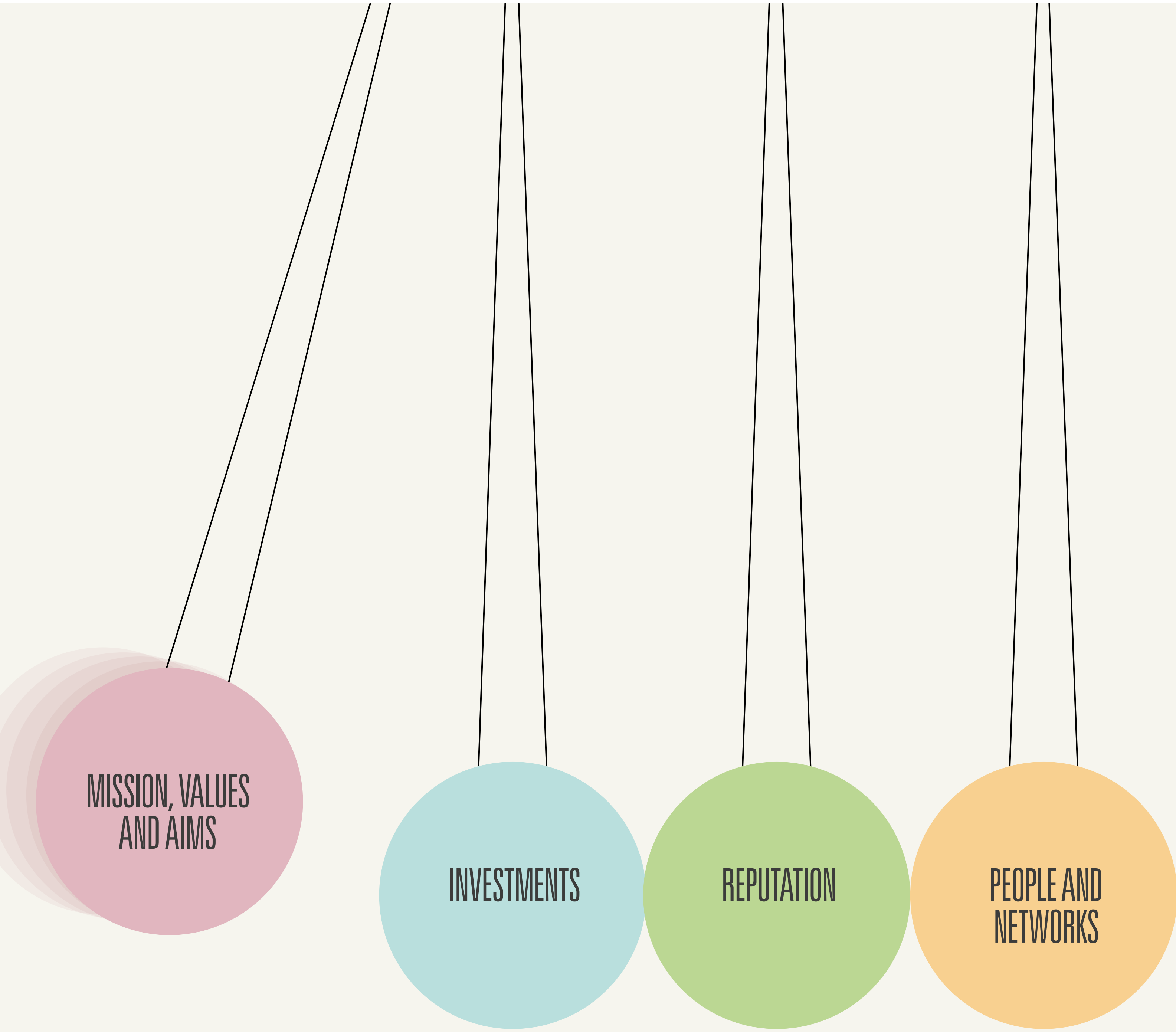
For some organisations it is a matter of principle to express the values that underpin their organisation through all aspects of their operation. Some of these may pioneer new approaches. Others will focus more on the financial returns as the best way to serve their mission.

Whatever trustees' approach, in order to clarify their intention, they have to reconcile principles with what's practical in their context, as well as take action to avoid pitfalls when implementing their strategy. The following pages look at these important aspects.

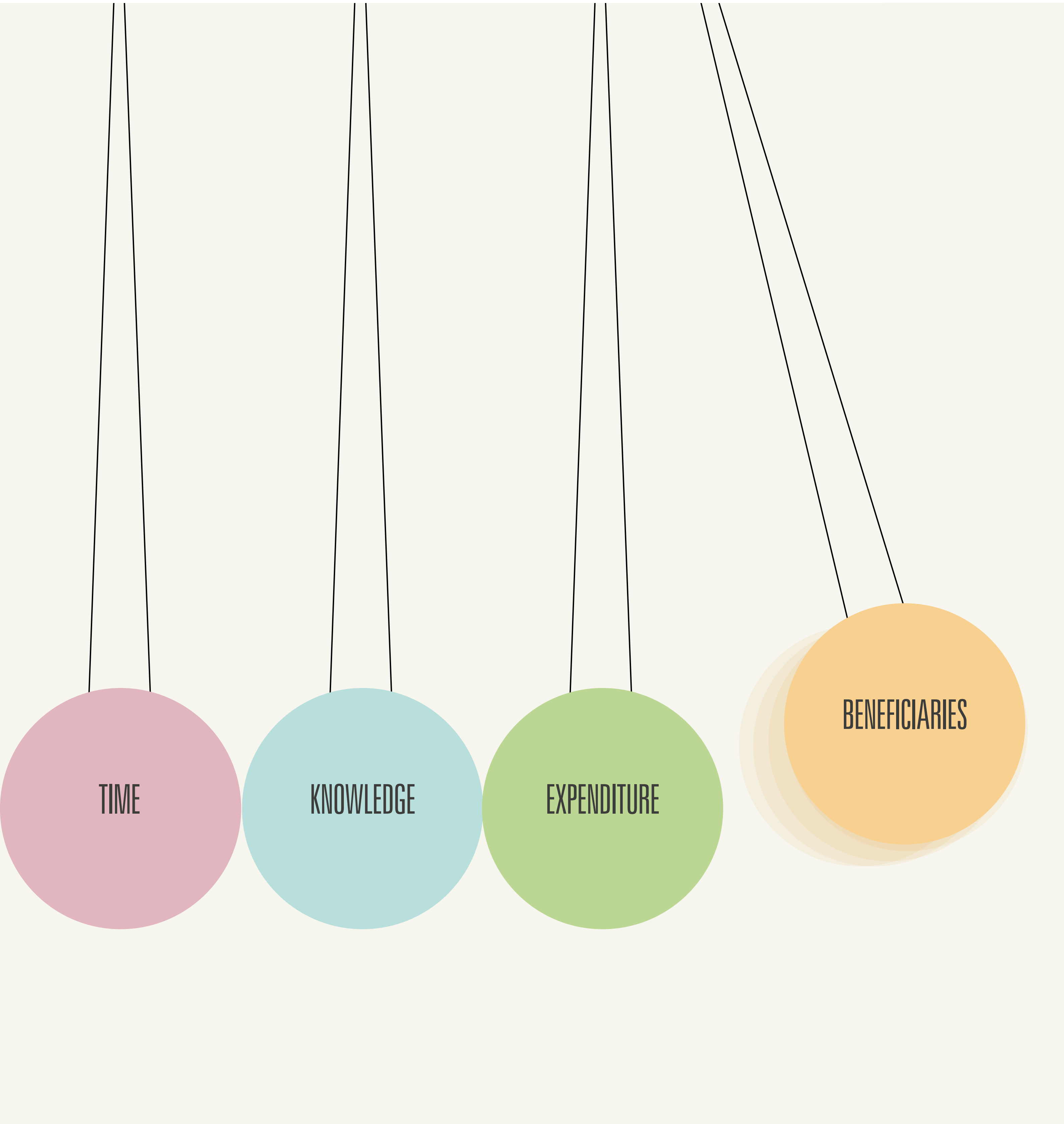
For grant-making trusts, the easy default is to keep the business of making money from the endowment separate from programme activity. However, our research suggests that when these two conversations are brought together, and boards engage holistically with their charitable objectives, applying their principles culture and values to all their assets, then discussion quickly moves from what can't be done to discovering possibilities for positive action.

KEY QUESTIONS

- Do we make investment decisions separately from decisions about our charitable activities?
- Do we have any constraints or restrictions on our investment activity in our governing document?
- Are there areas where we can see our investment activity conflicting with what we are trying to achieve or stand for as a charity? In what ways and how much do they impact?
- How would supporters feel if they understood our investment strategy? How would those that we are trying to help feel?
- As an organisation, what assets do we have at our disposal – financial and non-financial – and are we making the most of them to achieve our mission?
- Are we missing any opportunities in the way that we use our assets – could we use them more intentionally?



INTENTIONAL INVESTING – USING ALL OF THE ASSETS TO DELIVER THE CHARITABLE AIMS


TIME
KNOWLEDGE
EXPENDITURE
BENEFICIARIES

BALANCING PRACTICALITIES

Trustees need to consider a number of practical factors if they decide explicitly to reflect their charity's mission or values in its investment strategy.

WHAT IS THE RIGHT BALANCE FOR YOUR ORGANISATION?

Trustees have to balance a number of practical issues if they decide to manage their charity's investments with its mission in mind. Often this involves balancing principles and aspirations against cost and time.

Sometimes it's about understanding what's possible. In practice charity investors adopt a wide range of strategies, and usually rely on an investment manager to implement some or all of them.

RESTRICTIONS, RETURNS AND VOLATILITY

Much of the debate around screening certain investments out of portfolios has centred on whether doing so will reduce financial returns.

Research shows that this needn't necessarily be the case. Investors may achieve similar returns if they can find substitute stocks that perform a similar function – in investment terms – to those excluded, although that becomes harder the more industries that are excluded.

Reducing the size of the investment universe significantly could expose the portfolio to greater risk or more short-term volatility meaning that, while in the long term investors can reasonably expect to make the same overall returns, they may have a bumpier ride doing so.

For charity trustees who have a long-term perspective, this may not matter – but it is something to be aware of in governance terms so that trustees can stick to their strategy when the going gets, perhaps temporarily, tough.

THE MANAGERS MARKET

Charity trustees can't delegate their investment strategy to anyone else, though they must take advice if as a board they don't have sufficient expertise. However, trustees often delegate the management of their investments to investment managers to invest on their behalf.

Trustees' aspirations must therefore meet with market reality, and the extent to which a charity's values and objectives can be reflected in stock selection will depend on what the investment managers have to offer. This is particularly the case for those charities with smaller amounts of assets to invest.

Sometimes it can be difficult to reconcile the conversations between investment managers, who focus on financial returns, with trustees who are managing multiple perspectives and the concerns of stakeholders such as beneficiaries and donors. It's therefore important to examine whether your investment manager's approach aligns with your organisational views.

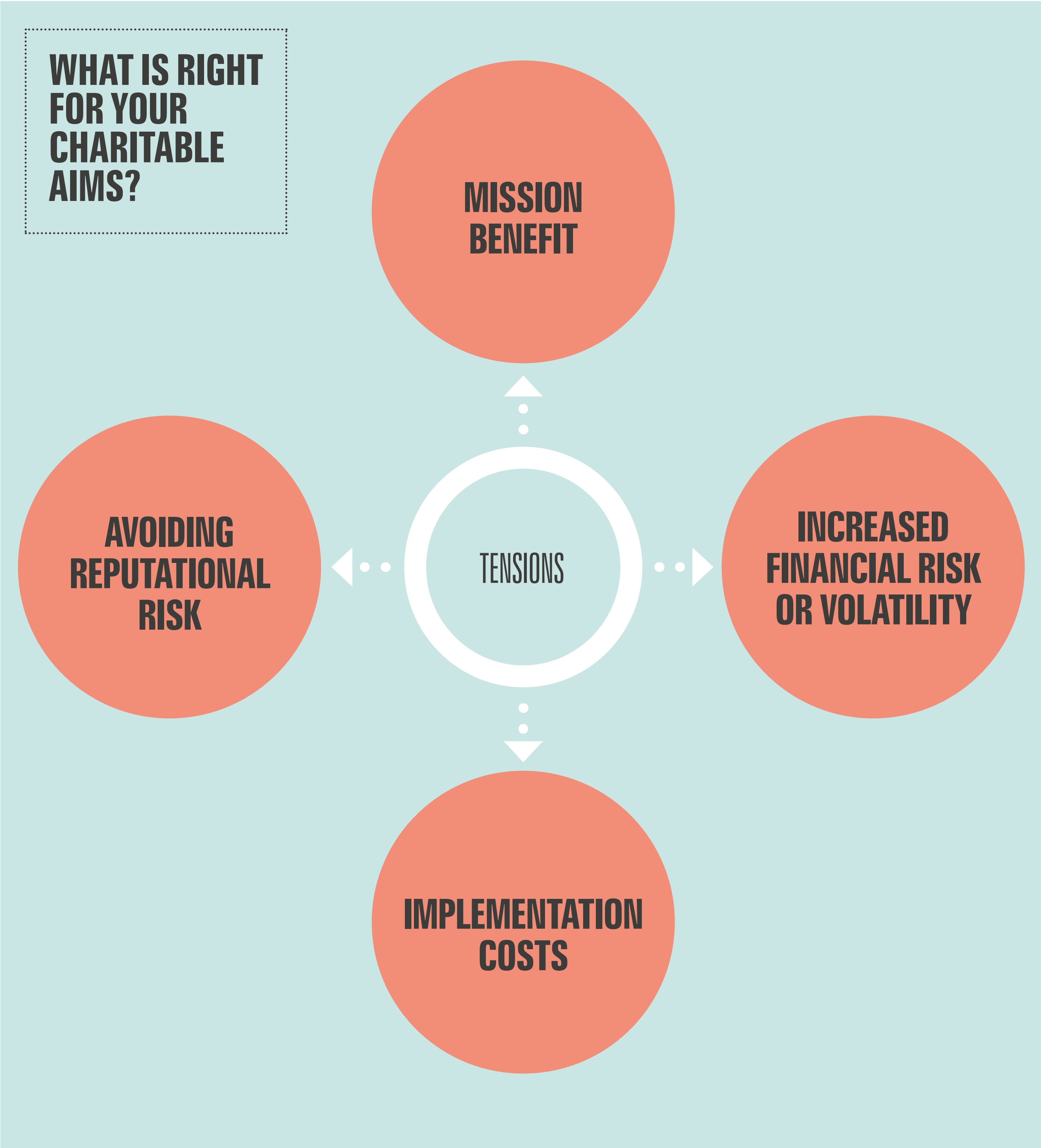
Only trustees can be expert in what their charities' objectives demand, and ultimately it is up to them to select managers with whom they can communicate and collaborate effectively.

PRODUCTS, PROXIMITY AND COSTS

Charity trustees are dependent not only on what managers there are in the market, but also on the products available. Pooled funds, for example, offer efficient ways of accessing expertise and achieving scale, but trustees may have little knowledge about the specific companies in which they are investing on a day-to-day basis.

When adopting exclusionary policies it's also important to consider whether you want to exclude entirely investments in companies that produce, manufacture, distribute or sell the product or service you want to avoid, or whether you simply want to limit your exposure. This can be done through setting a 'tolerance level' on the amount of corporate revenues or on the total exposure within the portfolio. So, for example, a charity wanting to exclude tobacco products from its investment portfolio may nonetheless still choose to invest in supermarkets that distribute and sell them.

Generally, the more bespoke investors want their investment strategy to be, the more resource intensive it will become to implement and manage both internally and externally. This may mean that charities with smaller investment portfolios will depend on pooled products, of which there are an increasing number, but which nonetheless will need to chime with their approach.


WHAT IS RIGHT FOR YOUR CHARITABLE AIMS?
MISSION BENEFIT
AVOIDING REPUTATIONAL RISK
TENSIONS
INCREASED FINANCIAL RISK OR VOLATILITY
IMPLEMENTATION COSTS

STAFF AND GOVERNANCE RESOURCES

Creating and implementing a policy takes time and expertise. Trustees are obliged by law to take expert advice in deciding their investment strategy when as a board they don't have sufficient expertise to do so themselves. A thoughtful investment strategy considers both the financial objectives as well as how best to use the assets to meet the needs of the beneficiaries.

A few larger charities also pay for supplementary, specialist, advice to help them monitor and engage with investment managers – both in terms of their financial performance and also in terms of any approaches they may adopt to incorporate their charitable mission or values into their investment policy.

However, there are only so many actions charities can delegate – and it takes staff and board time to understand and engage with experts and investment advisors – particularly if there is a knowledge gap to bridge. Trustees need to understand the governance resources required to act on the advice and information they receive.

PRINCIPLES FOR RESPONSIBLE INVESTMENT (PRI)

The United Nations-supported Principles are voluntary and aspirational. They offer a menu of possible actions for incorporating environmental, social and governance (ESG) issues into investment practices across asset classes. Investors become signatories to demonstrate publicly their commitment to responsible investment, to collaborate and learn with their peers about the financial and investment implications of ESG issues, and to incorporate these factors into their investment decision-making and ownership practices. They commit to report on their activity each year. There are currently over 1,300 signatories, comprising asset owners, investment managers and service providers. 14 of the top 20 charity investment managers are signatories.

STEWARDSHIP CODE

Since the financial crisis, the Government has been trying to encourage all asset owners and asset managers to act as stewards of their investments through both engagement and voting. The Government introduced a Stewardship Code in 2010 aimed at 'firms who manage assets on behalf of institutional shareholders such as pension funds, insurance companies, investment trusts and other collective investment vehicles.' The code makes it compulsory for asset managers to publish statements indicating the extent to which they have complied with the Stewardship Code's principles. A second version of the Stewardship code was launched in 2012 encouraging asset owners to publish statements as well.

PRACTICALITIES TO CONSIDER

EXCLUDE

- How will we identify the investments we wish to screen out?
- How significant does the harm need to be to trigger exclusion – any exposure or a proportion of activity or revenue?
- Do we want to exclude direct or indirect investments, or both?
- What impact if any will our policy have on the risks and returns of the whole portfolio?
- If an investment becomes unacceptable, how might we remove it? Immediately, or over time to minimise financial risk?

SELECT

- Which aspects of our charitable activity are best aligned with our investments?
- Will our policy affect our choice of manager? For example, if they integrate ESG and financial factors into their stock selection, or they are signatories to (UN) PRI.

INFLUENCE

- What aspects of our charitable activity are likely to be achieved through engagement and voting?
- Is it best to work through investment managers, in collaboration with like-minded investors, or both?

DELIVER

- What aspects of our charitable mission are likely to be achieved through investing?
- How can we ensure that our staff and board have the right skills and capacity to make social investments?
- How will we go about identifying the suitable opportunities that deliver our charitable objectives?
- What sort of commitment do we want to make, and what are we looking for in return – in terms of social impact? In financial terms?

NOT MAKING THE PERFECT THE ENEMY OF THE GOOD

Investing is complex and during our research even the most principled investors reported that implementing their approach entailed a degree of compromise. That's not surprising – not least because, when investing, trustees are putting their money into a range of organisations that are producing investment returns by pursuing their own objectives. When formulating their investment strategy, only trustees can determine what they can and can't compromise in terms of their charity's mission or values. What is generally true is that they will have to have the conversation about what they can realistically achieve, bearing in mind the charity's financial objectives.

KEY QUESTIONS

- What are the consequences of implementing our desired policy position, in terms of resources, fees, supplementary advice, impact on returns and exposure to risk?
- How do the range of managers and existing products compare with our needs?
- How does our investment manager's investment approach align with our organisational objectives and values?
- How do the costs of taking action compare with the reputational and mission risks of *not* acting?
- How will we monitor and review our approach?

We have found difficulties in the past with managers who want to talk about returns when you want to talk about reporting on implementation of the responsible investment policy. So it comes down to selecting the manager who both performs and who is also on your wavelength.

Focus group participant, York

AVOIDING THE PITFALLS

Investment policy reviews might include whether and how to manage the charity's investments with its values and mission in mind.

MAKING SURE YOUR STRUCTURES ARE FIT FOR PURPOSE

In starting out it's important to ensure that your investment policy is right for the circumstances of your charity and what you're trying to achieve. Investing is never easy, even when you have a clear financial goal. Incorporating other, mission-related, concerns into your charity's investment policy adds an additional layer of complexity. Whatever approach you adopt, our research suggests some things that can help you avoid pitfalls so that your charity's investment strategy serves its objectives and not the other way round.

GET GOVERNANCE RIGHT AND INVOLVE THE WHOLE BOARD

The key thing to get right for all investing is to ensure that the charity's written investment policy is backed up by the right governance structures so that the organisation can stay on course when the going gets tough.

Trustees as a whole hold the fiduciary duties to ensure that they are using their resources prudently and in ways which are loyal to the charity's objectives. They cannot delegate those responsibilities to anyone, and so strategic discussions and decisions should be made and understood by the whole board rather than a sub-committee alone.

Our research suggested that things could go awry for organisations when they have separate governance structures to set investment and programme strategy. Instead, considering the charity's use of resources with mission in mind helps safeguard the organisation from unintentionally thwarting its mission or damaging its reputation, and can even open up possibilities for doing further good. During our research practitioners highlighted again and again how important it was to engage in strategic conversations those trustees who might be expert in the mission of the charity but 'lay' when it came to financial or investment matters.

Even in terms of ongoing oversight, where perhaps a sub-committee deals with investment matters on a rolling basis, whatever overall approach to investment was taken, our research participants reported how helpful it was to have a trustee present who was not necessarily financially expert but was well-versed in the mission and values of the organisation to maintain an alertness to the concerns of beneficiaries and potential supporters.

CHOOSE THE RIGHT PARTNERS

Only trustees can make the strategic decisions contained in the investment policy. However, as well as seeking advice from investment managers, who arguably ought to be able to meet the full range of their client's needs, trustees can also seek specialist advice from individual consultants or organisations offering expertise in particular areas.

When it comes to implementation, charity trustees may wish to seek help with monitoring, although this is something they should also be able to ask of their investment manager. Trustees may also wish to share experience and collaborate with other organisations sharing similar aims – for example, the Church Investors Group represents institutional investors from many mainstream church denominations and church-related charities who come together on issues of common concern.

The important thing for trustees is to be clear about the reasons for seeking support, what the costs might be, including trustee or staff time, and how this enhances or obscures trustees' fiduciary obligations.

REVIEW YOUR POLICY

It is important to maintain focus when implementing an investment policy because, from a financial perspective, one of the worst things investors can do is to sell investments when their market price dips. That is why strong governance is important, so that trustees avoid over-reacting to market volatility in a way that compromises their longer-term objectives. On the other hand market cycles evolve and even organisational objectives change, so all investment policies need to be reviewed from time to time.

Possibilities are one thing. Trustees also have to think about what's practical in their context, and take action to avoid foreseeable pitfalls.

Your best is never good enough.

Focus group participant, London

A policy is a living thing. It's complex, technical, and hard to do. The point is that it's a live thing that makes you have conversations.

Focus group participant, London

Investment policy reviews might include whether and how to manage the charity's investments with its values and mission in mind.

Our research highlighted how much of a 'living thing' trustees feel this aspect of their investment policy is – recognising that it takes account of a changing society and company actions as well as beneficiary and donor attitudes. These factors are amplified by the increasing amount of information that is available through greater transparency and instant information transfer in the information age.

COMMUNICATE WELL, WITH HUMILITY AND REALISM

This changing context and the variety of factors that trustees must balance mean that there is no perfect achievement of trustees' intentions. So much depends on things beyond our control, that some would say the best trustees can do is to be clear about their aims, properly communicate them, and accept that they will fall short of achieving them. In that sense intention is always aspirational – and action is less about being able to get it right than committing to a continuous journey of improvement, often characterised by learning from mistakes.

KEY QUESTIONS

- How do we involve all trustees in creating our overall investment strategy so that it serves the mission of our charity and not the other way around?
- How do we monitor and review our strategy? Is our governance strong enough to understand and withstand market fluctuations?
- Do we know when to seek expert help and where to get it?
- Which other organisations share similar objectives? What might the costs and benefits be of sharing experiences or collaborating?
- How clearly has our investment policy been communicated and understood: internally by trustees and staff, and externally by supporters and beneficiaries?

END NOTES

[1] See *For Good and Not For Keeps*, Jenkins R., and Rogers, K., ACF, London, 2013.

[2] For more guidance on written investment policies, see *Writing your charity's investment policy: A guide*, Charity Finance Group and Charity Investors' Group, 2012.

[3] For a fuller discussion of trustees' duties, see *The Governance and Financial Management of Endowed Charitable Foundations*, Chapter 2, Jenkins, R., ACF, London, 2012.

[4] Harries v Church Commissioners [1992] 1 WLR 1241, discussed in paras 3.58 to 3.67 of *Social Investment by Charities*, Law Commission, Consultation Paper No. 216, 2014.

[5] Charity Commission for England and Wales, CC14.

[6] Source: ACF, Cazenove Charities Survey September 2014. Figure includes those charities who have adopted or are planning to adopt a policy but have yet to finalise.

[7] *Responsible investing: Does it pay to be bad?* Elroy Dimson, Paul Marsh and Mark Staunton, London Business School, February 2015. Published in the Credit Suisse Global Investment Returns Yearbook 2015.

[8] Cited in Dimson, Marsh and Staunton, see note 7.

[9] *Sustainable Investing, Establishing long term value and performance*. DB Climate Change Advisors, June 2012

[10] Robert G Eccles, Ioanniss Ioannou and George Serafeim, Harvard Business School, 4 November 2011. Equally weighted portfolio 1993 – 2010.

[11] See note 7.

[12] Dimson, Karakas and Li (2015), primary sample of 2,152 engagement sequences for 613 US listed public firms between 1999 – 2009

[13] *Responsible Investment and the Norwegian Government Pension Fund Global.* Dimson, Kreutzer, Lake, Sjo, Starks, November 2013

[14] www.shareaction.org/charityinvestment

[15] EIRIS and Holly Hill (2011) *What is the UK public's opinion of charitable investments?* Available at: www.eiris.org

[16] Charities SORP (FRS 102), 1.47. Financial Review

[17] See *Fiduciary Duties of Investment Intermediaries*, The Law Commission, Command Paper No. 350, 2014.

[18] From the *Comic Relief Investment Review Panel Recommendations*, March 2014. bit.ly/1nU8SSh

RESOURCES

There are many expert, advisory and consultancy organisations as well as peer practitioner groups. Here are some you may find helpful.

EXCLUDE AND SELECT

Charity Socially Responsible Investment (SRI)
charitysri.org

Divestinvest
divestinvest.org

Ethical Investment Research Services (EIRIS)
eiris.org

Ethical Screening
ethicalscreening.co.uk

FTSE4Good
ftse.com/products/indices/FTSE4Good

Go Fossil Free
350.org

MSCI (Morgan Stanley Capital International Indices)
msci.com/esg-integration

INFLUENCE

Carbon Disclosure Project
cdp.net

Church Investors Group
churchinvestorsgroup.org.uk

Ecumenical Council for Corporate Responsibility
eccr.org.uk

Institutional Investors Group on Climate Change
iigcc.org

ShareAction's Charity Responsible Investment Network
shareaction.org/charityinvestment

DELIVER

Big Society Capital
bigsocietycapital.com

CAF Venturesome
cafonline.org

Ethex
ethex.org.uk

Global Impact Investing Network
thegiin.org

Social Impact Investors Group c/o
admin@acf.org.uk

Social Finance
socialfinance.org.uk

Social Stock Exchange
socialstockexchange.com

OTHER RESOURCES

Stewardship Code
bit.ly/1HpzZiM

United Nations Principles for Responsible Investment
unpri.org

UK Sustainable Investment and Finance Association
uksif.org

CASE STUDIES

There is no 'one size fits all' approach for charity investors. What is right in one context is not going to be the case in another.

JOSEPH ROWNTREE CHARITABLE TRUST

EXCLUDE

SELECT

INFLUENCE

DELIVER

Objectives: The Trust uses grant-making to tackle the root causes of conflict and injustice, aspiring to place Quaker values of equality, truth, peace and sustainability at the heart of everything.

Investment assets: £200m

Approach: Trustees aim to use the Trust's investment assets, and their shareholding rights, to contribute to the objectives of the Trust.

Detail: The investment policy excludes companies whose activities conflict with the Trust's grant programmes, although trustees recognise that boundaries are not always clear-cut and that nuanced decisions need to be made. Excluded industries include armaments, gambling, tobacco, new generation nuclear power stations, and government bonds issued by states with high military expenditure or oppressive regimes. Extractive industries with poor human rights or environmental practices are also avoided.

Trustees select companies that take a responsible approach to their activities. In doing so trustees believe that they are acting in the charity's long-term financial interest and the interests of society at large.

Trustees also engage with companies, directly, through their fund managers, collaboratively with other charities, and exercise their share-voting rights. They expect fund managers to do likewise. Trustees are open to selling shares and/or changing their fund managers if they receive inadequate responses to their concerns.

Significant governance and staff resource is dedicated to the successful implementation of this investment policy. Trustees engage fund managers whose responsible investment policies are compatible with their own, and who are signatories to the FRC UK Stewardship Code and (UN) PRI.

The trustees are prepared to make social investments which strongly correlate with their grant programmes.

THE MARR-MUNNING TRUST

EXCLUDE

Objectives: The Trust uses grant-making to reduce the impact of poverty and disadvantage in countries outside the UK.

Investment assets: £13m in total, with a £12m property portfolio generating the majority of income and £1m managed by an investment manager in a segregated portfolio.

Approach: Trustees have reviewed and reframed their policy, which currently aims to maximise financial returns while taking account of risks. The new policy is that assets should be invested in line with the aims of the Trust, and that investments may be excluded if perceived to conflict with the Trust's purposes.

Detail: As the Trust is working with disadvantaged communities, trustees have decided to exclude direct investment into companies that could be perceived in any way to impact adversely on these communities or disadvantage any minority groups whose representation the charity is seeking to support.

The Trustees are considering implementation of this policy, wondering for example whether oil, mining and armament companies directly conflict with their aims and whether indirect exposure through a fund is more acceptable than direct exposure. One of the questions Trustees are considering is whether aligning investments with the Trust's aims might reduce financial returns or cost more in management fees and governance time but deliver an associated non-financial return with an equivalent or greater measurable value.

To be able to examine these questions fully the trustees have recruited financial expertise to the board and have commissioned independent external advice.

SEE WHAT'S RIGHT FOR YOUR CHARITY OVERLEAF

THE RACING FOUNDATION

FOCUS ON FINANCIAL RETURN ONLY

Objectives: The Foundation aims to achieve a lasting legacy for the sport of horseracing through making grants to charities associated with the UK horseracing and thoroughbred breeding industry.

Investment Assets: £81m

Approach: Shortly after the Foundation was established in 2012, the trustees actively considered whether and how to reflect their aims and values in their investments and concluded that their policy required no special approach beyond investing for maximum risk-adjusted return.

Detail: Policies to exclude potential investments were not thought to be required as trustees could see no strong relationship between the activities of companies they might invest in and any particular harm done to the people and thoroughbred racehorses that the Foundation exists to benefit.

For example, although gambling and alcohol addiction affect people working in the horseracing industry, there is no empirical evidence to suggest that such issues are more prevalent in the community than in wider society.

Furthermore, as the racing industry relies on bookmakers (through levy collection and sponsorship) and drinks companies (through sponsorship and as suppliers to racecourses), it was felt that the exclusion of such companies could in fact conflict with the economic success of the racing industry, to the detriment of Foundation beneficiaries.

Trustees have also considered setting up a social investment fund to directly deliver the Foundation's aims. However, the current priority is to establish the core grant-making function, and trustees sense that most beneficiaries will have access to loan finance from other sources.

The policy will be reviewed and may change and adapt in the future.

THE TUDOR TRUST

EXCLUDE

SELECT

INFLUENCE

DELIVER

Objectives: The Trust is a responsive grant-maker although trustees especially want to help smaller, community-led groups that support people at the margins of society.

Investment Assets: £260m

Approach: Trustees intend as far as possible to align their investment behaviour with their charitable aims. However in doing so they are pragmatic and accept that these issues are seldom clear-cut. They accept that, when investing, they are not looking for perfect organisations. However they will also identify areas of investment incompatible with the mission of the Trust and do not want to have holdings which conflict with the aims of the Trust.

Detail: The Trust's approach has developed since finally moving their investments from original founder stock in the late 1980s.

The current policy excludes tobacco, pornography, armaments and gambling.

In terms of selecting, influencing and voting, Trustees feel that they do not have the resources to do this themselves across the entire portfolio, and so they rely on carefully selecting the right managers whose values and approach align with the Trust's.

Trustees therefore leave day-to-day decisions to their two managers but regularly ask them to report on their activity, challenging them where necessary. Trustees observe that, because the relationship with the managers is so important to them, finding the right chemistry and values in the tendering process is of paramount importance.

The Trust is a recent member of the Charities Responsible Investment Network and supports the development of the social investment market.

WHAT'S RIGHT FOR YOUR CHARITY?

This road map shows what options might be right for your charity depending on your specific intentions and context.

INTENTIONAL INVESTING

'Intentional investing' means that as a trustee board you have thought about the management and use of your charity's assets so that: your approach supports delivery of your charitable aims; you are able to explain your approach; and, as far as possible, you anticipate and review the impact of your decisions in terms of your charity's mission and values, beneficiaries and supporters.

PRINCIPLES, WHICH APPLY TO YOU?

- SOME INVESTMENTS CONTRADICT OUR AIMS
- SOME INVESTMENTS RISK ALIENATING SUPPORTERS OR BENEFICIARIES
- WE WOULD LIKE, AND ARE ABLE TO, ALIGN SOME INVESTMENTS WITH OUR AIMS WITHOUT SACRIFICING RETURNS
- WE WOULD LIKE, AND ARE ABLE TO, INVEST IN WAYS THAT DIRECTLY DELIVER OUR AIMS
- IT IS IMPORTANT FOR US TO INVEST IN WAYS WHICH LEAVE A POSITIVE SOCIAL FOOTPRINT
- NONE OF THE ABOVE

OPTIONS TO CONSIDER

- EXCLUDE
- SELECT
- INFLUENCE
- DELIVER
- FOCUS ON FINANCIAL RETURN ONLY

PRACTICALITIES TO CONSIDER

— INVOLVING THE WHOLE BOARD
— GOVERNANCE AND STAFF TIME
— IMPLEMENTATION BOUNDARIES
— IMPACT ON RETURNS
— IMPACT ON DIVERSITY OF PORTFOLIO
— BENEFITS OF COLLABORATION
— CHARITABLE BENEFIT
— COST
— AVAILABILITY OF INVESTMENTS
— SUITABILITY OF MANAGERS

HAVE YOU CONSIDERED USING ALL OF YOUR ASSETS?

ABOUT ACF

The Association of Charitable Foundations (ACF) is the membership association for foundations and grant-making charities in the UK. For 25 years we have supported trusts and foundations; respecting and safeguarding their independence, and helping them to be effective in the many ways that they use their resources.
www.acf.org.uk

ASSOCIATION OF CHARITABLE FOUNDATIONS

ABOUT CAZENOVE CHARITIES

As the largest charity investment manager in the UK, we are the trusted partner of over 700 charities. We are fortunate to be able to offer a broad range of services, backed by the resource and strong investment performance of a leading global investment group.
www.cazenovecharities.com

CAZENOVE CAPITAL MANAGEMENT

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