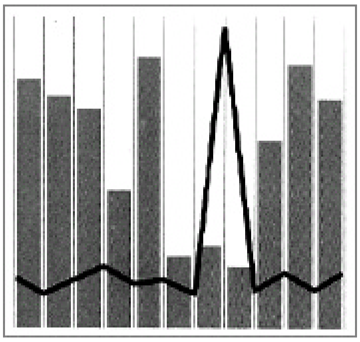
CHRISTIAN ETHICAL INVESTMENT GROUP

Charity Trustees and Investment Ethics



GUIDELINES FOR THOSE MAKING ETHICAL INVESTMENT DECISIONS

Charity Trustees and Investment Ethics
Guidelines for those making Ethical Investment Decisions

Contents

Introduction

Ethical investors apply a sense of moral responsibility to the world of investment. They seek not only good financial returns, but also high ethical standards from the companies which use their money. They may focus their attention on one or more of the many aspects of a company's activities:

the quality and usefulness of goods and services, corporate governance, rewards and conditions of service, the empowerment and training of employees, or the impact of the company on the wider community and on the environment.

Significant sums of money are invested by charities, churches and pension funds. Charities exist to do good. In seeking the good of their own beneficiaries they depend on, and contribute to, a wider climate of goodwill, moral conviction and responsible stewardship. Ethical concern about the investment of charitable funds is therefore natural and appropriate, yet Trustees are often uncertain how this relates to their primary duty to promote the interests of their cause.

This paper has been produced by the Christian Ethical Investment Group with the advice and assistance of those listed in the Appendix. Our aim is to encourage Trustees to develop ethical investment policies within the present framework of the law. In deciding their policy on ethical investment, Trustees need to consider the matters set out below under the following headings:

1. **Responsibility for the Policy**
2. **Stakeholders in the Policy**
3. **Scope of the Policy**
4. **Positive and Negative Ethical Investment Policies**
5. **Monitoring the Policy**
6. **Implementing the Policy**
7. **Communicating the Policy**
8. **The Legal Framework for Ethical Investment**

The questions which follow each section are not intended as an exhaustive list of the issues to be considered, but are offered as an important starting point for Trustees in formulating their policy.

1. Responsibility for the Policy

a) The Trustees are ultimately responsible for a charity's investment policy, and this responsibility must not be delegated, except where there are specific powers to do so in the Trust Deed.

b) The Charity Commission requires Trustees to draw up a written investment policy: The Trustees of every charity should draw up an investment policy for their charity, and set it out clearly in writing… This written policy should address the charity's needs and those of its beneficiaries in the short, medium and long term… The Trustees should ensure the Investment Manager does not depart from the investment policy without their express prior written approval… The policy should be agreed formally by all Trustees and reviewed annually. It is important that Trustees adopt policies that are prudent and cautious, bearing in mind the long-term nature of charity investments. This responsibility of the Trustees applies as much in the ethical policy as to any other dimension of the charity's operations. Trustees need to seek legal, financial and ethical advice, but their own responsibility requires them to use their own brains, reach their own conclusions and formulate their own policy.

c) It will be important for Trustees to have some mechanism (such as a Subcommittee) to consider and review the ethical aspects of their investment policy. This will make sure that they are kept on the agenda.

d) In formulating an ethical investment policy, Trustees will need to consider carefully the various points in these guidelines. In particular they will need to weigh the possible costs and practicalities against the size of the funds which they operate, the resources available to them, the time required for the implementation of the policy and the possibility of co-operating with other Trusts and agencies. However, the approach of the Trustees should not be that an ethical policy needs to be all or nothing: a policy based on only some of the ethical considerations in this document is almost certainly better than no ethical policy at all, provided it is carried out responsibly. It may be that a policy needs to start in one corner of the field, and slowly develop to cover a greater part of it.

e) The Trustees will need to ensure that their Fund Managers are familiar with their ethical investment policy, in sympathy with it, competent to operate it, and able to advise on its financial implications.

Questions:

1. How do the Trustees determine their ethical policy? Should there be a Subcommittee for this purpose**?**

2. How often is the policy reviewed?

3. Where do the Trustees turn to for advice on the ethical issues?

4. Is there a local forum in which education and debate on the ethics of investment are promoted? Are there ways in which the Trustees can co-operate with others to make public opinion more favourable to the promotion of ethical investment?

5. What legal and financial advice is sought on these matters, and from whom?

6. Are the Fund Managers familiar with, and sympathetic to, the Trustees' ethical policy? Can they advise on its financial implications?

2. Stakeholders in the Policy

a) The primary stakeholders in any ethical investment policy are the beneficiaries or objects of the charity. It is their interests which the charity exists to advance, and these have generally been taken to mean seeking the best financial return from the charity's investments, consistent with commercial prudence.

b) Other groups of people may also be affected by the work of the Trust, for example, staff those who make donations, professionals who give advice and make investments, the companies in which investments are made, the people affected by those companies' operations, and the public more generally.

c) It is for the Trustees to decide what weight to give to the interests of the secondary stakeholders and how they relate to the overriding duty to the beneficiaries, and the requirements of commercial prudence.

d) The Trustees will need to consider how the views of both primary and secondary stakeholders are to be sought, and their judgments encouraged and developed.

Questions:

1. Who are the beneficiaries or what are the objects of the charity?

2. Who are the secondary stakeholders affected by the charity's investments and operations?

3. How are the views of beneficiaries and secondary stakeholders sought?

4. What is the charity doing to educate beneficiaries and secondary stakeholders about the ethical dimensions of its work?

3. Scope of the Policy

a) Trustees will need to decide how far their investment policy is in line with the nature and purpose of their charity. The Charity Commissioners advise that Trustees should decline to invest in a particular company if it carries out activities which are directly contrary to the charity's purposes, and therefore against its interests or those of its beneficiaries. For instance, a charity for the relief of cancer sufferers would be justified in avoiding investment in tobacco companies, or temperance charities in breweries.

Further, if Trustees are satisfied that a particular range of investments would impede the furtherance of the objects of a charity, and be of financial detriment, then they may exclude that range. For example, investments may be excluded if they would result in a loss of financial support from subscribers, where the charity depended on public donations; or if the beneficiaries were unwilling to accept help from a particular investment source.

Trustees may also wish positively to seek out opportunities to invest in companies whose products, services or methods of operation are in line with the purpose of their charity. For example, medical charities may wish to invest in pharmaceutical companies or manufacturers of medical equipment, and environmental charities may prefer companies which have an excellent environmental record, or whose products and services are directly related to environmental improvement. Such positive investments should nevertheless fulfil the normal criterion of seeking to obtain the best financial return consistent with commercial prudence.

b) There may be a further range of investments which Trustees wish to exclude, or encourage, where there is a less clear-cut relationship with the object of the charity. For example, Church investment bodies may exclude investments in armaments, gambling, tobacco, brewing and distilling, or companies whose directors award themselves very large pay increases, not because there is an unambiguous conflict with the objects of the charity, but because the Trustees wish to respect the convictions of those who do believe such investments to be ethically unacceptable. Trustees are at liberty to make such judgements. provided there remains a sufficiently wide range of alternative investments to obtain the best financial return for the beneficiaries.

c) These questions may be complicated by the increasing practice of charities working in partnership with other agencies. For example, in bidding for awards under City Challenge or the Single Regeneration Budget. charities may find themselves being asked to work with companies in which they would normally not invest in order to provide sponsorship for worthwhile local projects which are to the advantage of their beneficiaries. Although such partnerships do not directly affect the charity's investment policy, Trustees will need to give careful consideration to the wisdom of such partnerships in the light of their ethical investment policy.

d) The Charity Commissioners insist on the distinction between ethical and political concerns; thus, while a charity may legitimately avoid making investments in a company which supplies arms to a repressive regime, any campaigning against that regime or the company may be judged political, and could therefore be inconsistent with the charitable objects of the Trust.

e) Trustees need to decide whether their ethical investment policy applies to all their investments, including shares, cash, land and property. or whether it only applies to certain types of investment. Particularly difficult problems can arise where, for example, a Church hall or school has been declared redundant, or where charitably owned land which is farmed or used as a local amenitv becomes available for mineral extraction. To the Trustees, such properties represent investment opportunities. In the eyes of the local community, however, they are still regarded as functional properties, and there may be expectations that they should be available to the local community for less than the full market value. Serious difficulties can arise for the good name and standing of the Church or charity in the local community if the property is sold in what is seen as a remote and impersonal transaction. Where such cases arise, the Trustees need to ensure that they are well supported by appropriate professional advice. The Trustees will need to consider whether there is a serious danger of alienating local supporters of the Church or charity, and if so, how-great that danger is. In some cases the Trustees and the local community may need to accept the moral responsibility exercised by the local Planning Authority, and once planning permission has been given, the sale or change of use must be allowed to proceed. In other instances it may be possible for the Trustees to help the local community either to acquire the property at full market value or to use the property in a way which is partly or wholly in furtherance of the charity's objects. In the case of Church or school buildings, particular attention needs to be paid to the precise Trusts on which the property is held.

Questions:

1. Are there investments which are directly contrary to the objects of the charity?

2. Are there investments which the Trustees would like to promote as positively furthering the objects of the charity? Are they justifiable on financial grounds?

3. Are there investments which the Trustees would prefer to avoid on ethical grounds, even though their relationship with the objects of the charity is ambiguous or controversial? If so, is there a sufficient range of alternatives to provide a proper financial return?

4. Is the charity co-operating in partnerships with companies or agencies it would normally avoid for ethical reasons? If so, what bearing should the ethical investment policy have on the decision to enter such partnerships?

5. Are the Trustees observing the Charity Commissioners' distinction between ethical concerns and political activity? Does this distinction create difficulties for the charity?

6. Are there instances where the sale of redundant functional properties is creating strong local opposition? What advice should the Trustees seek? Are there ways in which the Trustees are able to combine their investment duties with the needs of the local community? Do the Trusts on which the property is held give the Trustees any discretion in disposing of the property for less than the full market value? Are there ways in which the property can be used in furtherance of the charity's own objects?

4. Positive and Negative Ethical Investment Policies

a) Ethical investment policies are often expressed negatively, in terms of avoiding investment in, or divesting from, companies whose activities the Trustees disapprove of. It is equally or more important to consider positive ethical investment policies, where Trustees seek out investments which promote the object of the charity, or are compatible with it, or which enhance the reputation of the charity. It is for the Trustees to determine the balance they wish to strike between the positive and negative factors.

b) Sometimes charities may positively choose to invest in a local company This enables the Trustees to show commitment to the local area, to promote local employment, and to monitor the company's performance more easily than is possible with more remote corporations. Where Trustees are considering a range of possible investments, this local consideration can be an important tie breaker.

c) Trustees may also wish to consider creative investment possibilities. The Charity Commissioners rightly warn Trustees against speculation, and counsel prudence and caution. But this should not discourage charity Trustees from exploring ways of combining more than one objective. For example, housing charities can fulfil their obligations to provide accommodation for the homeless, and at the same time provide training opportunities for local unemployed people. In a similar way, the New York City Pension Fund has developed an imaginative scheme to provide low-cost housing for their own beneficiaries by entering into a partnership with the State Authorities. This enables the Pension Fund to achieve a proper market return, and at the same time make a large amount of capital available to meet a serious social need which affected their own beneficiaries even though it was not directly within the objects of the fund. Such ventures need not necessarily be "speculative" as defined by the Charity Commissioners.

There may also be a category of investment which does not achieve the maximum return on a purely financial assessment, but which has a beneficial consequence in terms of the charity's own objects which validates the investment nevertheless. In such cases Trustees need to ensure that the kind of ‘spin-off' benefit is indeed in line with the objects of the charity. Any diminution of the investment return must be justified by the direct contribution it makes to the fulfillment of the charity's objects.

As partnerships between charities, Local Authorities, Central Government, the Private and Voluntary Sectors, and European Regional Funds increase, such creative opportunities are well worth exploring (with due consideration to the point made in 3c) above). Charities in a local area could well consider employing (preferably on a voluntary basis) an Adviser suitably qualified to explore with them the potential of such partnerships, and the use of a proportion of their funds (without risk to their charitable purpose) as “Ethical Venture Capital".

d) Ethical interests and financial interests are often seen as being inherently in conflict. This is not necessarily the case. The two spheres of interest may be represented by two circles in which there is an area of overlap, but also areas which are distinct. Some ethical strategies (e.g. reducing waste) may have financial benefits, while others (e.g. cleaning up rivers) may have costs. Trustees may pursue ethical policies which are to the financial detriment of their charity only where the ethical considerations concerned are clearly and directly related to the charity's purposes. In other cases, it is in everyone's interest to maximise the area of overlap between financial and ethical interests. Businesses are obviously more likely to listen to ethical arguments where these can be seen to be also in their long-term financial interests. Companies may be encouraged to regard attracting ethical investors as enhancing their own reputation. Equally, charities are more likely to be encouraged to pursue ethically responsible policies if they can feel confident of obtaining good financial returns. Both sides are more likely to take hard ethical questions seriously, even where there may be a financial cost, if it can be shown that ethics and profitability are not always on opposite sides.

Questions:

1. Which investments should the Trustees seek to avoid, or to dispose of?

2. Are there investments which the Trustees wish positively to promote as being in line with the charity's objects?

3. What opportunities are there for local investment?

4. Are there investment opportunities which provide a desirable "spin-off” in some other area of social need or environmental improvement?

5. Are there investments which combine the furtherance of the charity's own objects with a return which may be less than the full market rate?

6. What creative possibilities are there of exploring mutually advantageous partnerships with Local and National Government, Voluntary Organisations, European Regional Funds, and/or the Private Sector?

7. What sources of advice are available locally on these matters? Can your charity appoint an Adviser, preferably voluntary, either by itself or in co-operation with other charities?

5. Monitoring the Policy

a) In formulating an ethical policy, Trustees need to take into account the need for effective monitoring of the companies in which investments are made. Standards of improvement and decline need to be formulated and communicated to the managements concerned.

b) Trustees will need to have some means of obtaining information about the actual performance of companies, and discussing performance with the managements concerned. They will need to take a view on how far they can rely on the managements themselves to provide reliable information. Other sources of information include Government databases such as the National Rivers Authority and the Health & Safety Executive; trade bodies such as the Advertising Standards Authority; Press reports and trade journals; campaigning bodies; independent research organisations such as EIRIS and PIRC; and other Trustees who may have had dealings with the same issues.

c) Trustees will need to consider carefully whether they have the time and resources to monitor ethical performance adequately.

Questions:

1. What are the criteria by which Trustees will monitor the ethical performance of each of the companies in which they invest?

2. How much Staff and Committee time is available for monitoring company performance?

3. What sources of information about a company's performance are available to the Trustees? What could be "bought in" or copied from other investors or interest groups?

4. Is any training or development of Staff or Committee members needed? How can that best be organised?

6. Implementing the Policy

a) Having monitored performance Trustees will need a strategy for influencing company behaviour. It will be important first to establish facts with the company and its critics, and then to establish exactly what it is hoped to achieve. Further action may involve following up with senior management any criticisms of a company’s activities through confidential correspondence or direct discussions. In some cases it may involve proposing or supporting resolutions at shareholders' meetings or other forms of publicity. This can be time-consuming, so Trustees may wish to consider joining with other shareholders or interest groups wherever appropriate.

b) Trustees will also need to consider the circumstances in which they would wish to divest entirely from a company, and the consequences of doing so.

c) Trustees may find it helpful to have a policy which combines “Voice" and “Exit" **-** a clearly stated strategy of increasing or reducing shareholding in response to the direction the company is taking on ethical issues.

Questions:

1. What time and resources are available to Trustees to seek to influence company managements by correspondence or discussion?

2. How can Trustees gain experience and training in influencing companies through shareholders' meetings?

3. With which other Trusts or agencies are the Trustees prepared to co-operate in implementing the ethical policy?

4. What are the criteria by which the Trustees will increase or reduce their shareholdings in companies on ethical grounds, and by how much?

5. Divestment is a serious step; what are likely to be the consequences in terms of influence, particularly if the relationship with the company is well established or significant?

7. Communicating the Policy

a) Trustees will need to consider how their ethical policy is to be communicated, and to whom. The interests of the various stakeholders (especially Fund Managers, Companies, Beneficiaries, and the Public at large) need to be considered from this perspective.

b) Individual decisions will also need to be communicated, and the possible media implications of this should be thought out in advance.

c) The Annual Statement or Report of the Trustees should reflect the ways in which the policy is being implemented and modified in the light of experience.

Questions:

1. In principle, who should know about the ethical policy which the Trust follows?

2. To whom should individual decisions be communicated and how?

3. What sources of advice are available to the Trustees to enable them to handle any media publicity which may arise from decisions in individual cases?

4. What documents should be available to any enquirer on request?

8. The Legal Framework for Ethical In vestment

a) The duties of Charitv Trustees are set out in the document “Investment of Charitable Funds Basic Principles" published by the Charity Commissioners for England and Wales (Publication CC 14). This includes a section on ethical investments, the contents of which have been incorporated in the guidelines above.

The basic principles governing ethical investment are that the Trustees have a primary duty to promote the interests of the charity's beneficiaries, and this is in general best served by the Trustees seeking to obtain the best financial return from the charity's investments, consistent with commercial prudence. Trustees may not exclude, to the financial detriment of the charity, a particular range or class of investments in order to give effect to some moral or political belief held by the Trustees but not directly related to the interests of the charity and its beneficiaries. Within these parameters, however, there is scope for a range of ethical policies and strategies as described above.

b) The law on ethical investment was tested in the case of the Bishop of Oxford and others v. the Church Commissioners, and the judgment of Vice-Chancellor Nicholls set out a number of principles. These are:

i. The Trustees have a right to take ethical considerations into account, even where this is to the financial detriment of the charity, where statutory provision has been made.

ii. Another circumstance where Trustees would be entitled, or even required, to take into account non-financial criteria would be where the Trust Deed so provides. Trustees therefore need to be familiar with the precise wording of their Trust Deed.

iii. Trustees must consider those cases where there may be a straightforward conflict between an investment and the aims of the charity. The judgment states:

'There will be some cases, I suspect comparatively rare, where the objects of the charity are such that investments of a particular type would conflict with the aims of the charity. Much cited examples are those of cancer research charities and tobacco shares, Trustees of temperance charities and brewery and distillery shares, and Trustees of charities of the Society of Friends and shares in companies engaged in the production of armaments. If, as would be likely in those examples, Trustees were satisfied that investing in a company engaged in a particular type of business would conflict with the very objects their charity is seeking to achieve, they should not so invest. Carried to its logical conclusion, the Trustees should take this course even if it would be likely to result in significant financial detriment to the charity. The logical conclusion, whilst sound as a matter of legal analysis, is unlikely to arise in practice. It is not easy to think of an instance where in practice the exclusion for this reason of one or more companies or sectors from the whole range of investments open to Trustees would be likely to leave them without an adequately wide range of investments from which to choose a properly diversified portfolio.’

iv. Another justification for ethical investment might be the possible alienation of recipients or supporters of the charity. To quote the judgment again:

‘There will also be some cases, again I suspect comparatively rare, when Trustees' holdings of particular investments might hamper a charity's work either by making potential recipients of aid unwilling to be helped because of the source of the charity's money, or by alienating some of those who support the charity financially. In these cases the Trustees will need to balance the difficulties they would encounter, or likely financial loss they would sustain, if they were to hold the investments against the risk of financial detriment if those investments were excluded from their portfolio. The greater the risk of financial detriment, the more certain the Trustees should be of countervailing disadvantages to the charity before they incur that risk.'

In practice the rarity of the conflicts to which Vice-Chancellor Nicholls refers will depend on the objects of charities, the activities of companies and the changing degree of the public awareness of these issues.

v. Another situation which may influence Trustees is the possibility of the charity being brought into disrepute, for example through adverse Press publicity. ViceChancellor Nicholls states:

'Of their very nature, and by definition, investments are held by Trustees to aid the work of the charity in a particular way, by generating money. This is not to say that Trustees who own land may not act as responsible landlords or those who own shares may not act as responsible shareholders. They may. The law is not so cynical as to require Trustees to behave in a fashion which would bring them or their charity in to disrepute (although their consciences must not be too tender: see Buttle V. Saunders [1950] 2 All ER 193).'

vi. Where there is disagreement as to whether a particular commercial activity is or is not compatible with the charity's object, the judgment of Vice-Chancellor Nicholls states:

'Trustees must not use assets held by them for investment purposes as a means of making moral statements at the expense of the charity of which they are Trustees. Trustees may, if they wish, accommodate the views of those who consider that on moral grounds a particular investment would be in conflict with the objects of the charity, so long as the Trustees are satisfied that course would not involve a risk of significant financial detriment.

In other words, they may avoid that particular investment provided there remains a sufficiently wide range of alternatives to achieve the best result for their beneficiaries.

c) Trust Deeds:

Where a new Trust is being set up it may be possible to include ethical criteria in the investment powers which will be approved by the Charity Commissioners.

Where an existing Trust Deed is concerned, its terms may empower the Trustees to amend its terms and provisions. If this is the case, it will be important first to ascertain whether the consent of any other person is required, or whether the Trustees can simply make the amendment without reference to anyone else.

It is normal for amendment provisions in charitable trusts to require the consent of the Charity Commissioners, although there are examples of charitable Trust Deeds in existence which enable the Trustees to effect an amendment without the Charity Commissioners' consent. Clearly where the consent of someone other than the Trustees is required, that consent must be obtained if the amendment is to be valid.

It is one thing to have a power, and another to he able to exercise it properly in the circumstances. Thus, even if there is a power of amendment which does not require the consent of anyone else, the Trustees must consider before doing so whether it is a proper exercise of that power, and, if it is, what the consequences of that exercise might be.

Charity Trustees must exercise their powers in the interests of the charity to which they are administering. That means that before including a provision to enable them to do something, they must be satisfied that it would be in the interests of the charity (and not simply in keeping with their own personal beliefs) for the proposed amendment to be made. Any provisions which were to be introduced would have to be capable of justification on one of the grounds referred to in this section of these guidelines.

Where there is no express power in the Deed enabling the Trustees to amend its terms, it may still be possible for an amendment to be made by obtaining a scheme from the Charity Commissioners. The Charity Commissioners will need to be persuaded that it is in the interests of the charity for the amendment to be made.

Before considering any amendment to the Trust Deed, the Trustees should consider whether or not the Charity Commissioners would be likely to consider it appropriate for a change to be made (even if the Trustees can amend their Trust without the Charity Commissioners' consent or the need to consult them for a scheme) as this will provide a useful yardstick against which to consider whether or not it is proper for the amendment to be made.

Trustees who are contemplating amending their Deed must take appropriate professional advice to avoid the possibility of making an invalid amendment, or of making an amendment which could conceivably prejudice the charitable status of the Trust.

d) Trustees need to be able to show that their ethical investment policy falls within the above criteria. Any policy outside this framework would require a change in the law.

Questions:

1. What is the present legal purpose of the Trust?

2. What are its present investment powers? Are there limits on the types of investments that can be made? (e.g. The Trustee Investment Act 1961 has been liberalised by the Charities' (Trustee Investment Act 1961) Order 1995, which came into force on 25 April 1995; charities which feel their powers are still too narrow, despite the Order, can apply to the Charity Commissioners for a Scheme).

3. Is there any reference to ethical investment in the Trust Deed? If not, could the deed be amended? Who would need to approve any amendment, and what process would be required?

4. What sources of legal advice currently available to the Trust have the experience and skills required to advise on and assist in the implementation of an ethical policy? Are there other sources of such advice that could strengthen what is currently available?

MAY 1996

The Christian Ethical Investment Group, as a voluntary pressure group, was formed in 1988 to promote a stronger Ethical Investment policy in the Church of England. In April 1996 it accepted among its objectives the promotion of an awareness and study of ethical investment issues within all Christian denominations. It seeks to encourage the development of clearly stated theologically based ethical investment policies. It does not, however, seek to promote a specific line on any particular ethical issue and it believes the issues set out in this booklet are important for all charities and not just for church-based ones.

Membership of CEIG is open to all. Please visit our website at www.ceig.org **for further information, email us on** info@ceig.org **, or write to us at the following address:**
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