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CHARITY INVESTMENTS UNDER CHARITIES ACT 1992

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Introduction

Myths are hard to dispel. Despite wars, Antonio's trouble with Shylock, the South Sea bubble and loss of post-election euphoria, the quest for safe investments offering high returns is pursued with enthusiasm.

The person who risks his own and succeeds may be admired or envied or sent to the Upper House, and may be quickly forgotten if he fails. Unauthorised speculation on your own behalf with other people's property is seldom applauded (let alone up-lorded); but if it does well the rectified misappropriation may never come out; and if it misfires you can always fall off a boat. Trustees, who are authorised, indeed are enjoined by law, to speculate with other people's property, may also do well or badly. If their investments prosper, someone will be pleased; if the trustees stay within the law, but the value of the trust property falls or disappears, those who are not pleased have no redress.

All investment is speculation. The question for the Court of Chancery, which passed to Parliament a couple of centuries ago, is not what investments are safe, so that trustees should be allowed to buy them with trust money, but how to reduce the hazards to a level which is acceptable when entrusting a fund to fiduciary management.

Every few decades, Parliament accepts that what it enacted last time has ceased to be appropriate. The Trustee Investments Act 1961 will not last much longer, or at least not in its present detail, although it must already be one of the most amended non-taxing statutes. As in the late 1950s, judges are prepared to use the Trustee Act 1925 section 57, the Variation of Trusts Act 1958 or the charity jurisdiction to expand the terms of trust instruments so as to enable trustees to invest in ways outside their statutory powers. For charitable trusts, the Charity Commissioners occasionally give authority under the Charities Act 1960 section 23. Investment clauses in new trust instruments usually give much wider scope than that of the 1961 Act. The House of Lords favoured wider powers of investment when debating the Bill which became the Charities Act 1992. The Government speaks of reviewing the investment powers of trustees. Everything points to forthcoming legislation increasing the range and manner in which trustees relying on statutory powers may invest, but nobody knows when.

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Special Investment Powers for Charities

Apart from provisions relating to jurisdiction to authorise particular transactions, and apart from enabling common investment schemes to be made for two or more charities under section 22 of the Charities Act 1960, legislation on investment has until now treated charitable trusts and other trusts alike. That community of treatment will end when the Charities Act 1992 comes into force. Common deposit funds will join common investment funds (1960 Act section 22A, added by section 16 of the Act of 1992); but the more dramatic innovation is in two sections which have their genesis in the committee stage of the Bill in the House of Lords.

In fact, against the advice of the Government, their Lordships in committee added three clauses on investment. One clause was intended to give charity trustees power (which other trustees have not got unless it is conferred by the trust instrument) to delegate the investment of trust funds unless expressly prohibited from doing so by the trust instrument. The idea was to allow the employment of professional managers. The capacity of many trustees to take investment decisions may be limited, or even pathetic, but that could apply also to their capacity to choose a professional manager. A professional manager may be knowledgeable, but his knowledge is historical and investment misfortunes can often be avoided only by use of insider information or a serviceable crystal ball. In the event, the House of Lords removed that clause before completing their deliberations on the Bill and sending it to the House of Commons. That is just as well. The matter deserves further consideration in the context of trustee investments generally. In any case, only fairly large charities have any use for professional managers and may already have express powers to do so or command the experience and skill within the ranks of their trustees or employees.

The two clauses which survived became, with changes, sections 38 and 39 of the Charities Act 1992. Section 38 provides for charity trustees to have different powers from those of other trustees to invest in wider-range investments within the meaning of the Trustee Investments Act 1961, and section 39 provides for the investment of charity property in ways not authorised by the 1961 Act. Both sections make the Home Secretary and the Treasury joint repositories of wisdom.

Varying Equal Division of Investments: Section 38

Wider-range investments, as the Trustee Investments Act 1961 uses the expression, are mostly shares and debentures, quoted on the Stock Exchange, issued by large United Kingdom public companies with uninterrupted recent dividend payments, and units in authorised unit trusts. Trustees relying on statutory powers can invest up to half the trust fund in wider-range investments. If they wish to acquire or retain a wider-range investment, the trustees must make an equal division of the trust fund, once for all (one part available for use for either wider-range or narrower-range investments and the other restricted to the narrower range) and must divide equally between the two parts any subsequent augmentation of the trust fund (unless the additional property accrues to the trustees as owners of property comprised in one part of the fund, for example a bonus issue of shares to shareholders, in which case it is allocated to that part). They must obtain and consider proper advice before investing in the wider range and from time to time as appropriate. Section 38 of the Charities Act 1992, when it operates, will empower the Secretary of State, with the consent of the Treasury and with the approval of both Houses of Parliament, to make Orders varying the requirement of equal parts when the trust fund is divided by a charity in England or Wales or by a recognised body in Scotland. If an Order is made, a charity or recognised body which had already divided its fund under the 1961 Act will be allowed to make one re-division in pursuance of the Order. The progenitors of section 38 of the 1992 Act had in mind that more than half of a fund would be allowed into wider-range investments, but the terms of the section are such that an Order could provide for a limit less than half. It is to be expected that either more than half will be authorised or the power to make Orders will not be exercised. Under s.13 Trustee Investments Act 1961 the Treasury has power to vary the requirement of equal parts for all trusts, so as to provide for a wider-range part from one-half to three-quarters of the fund, but s.13 has not been used in its thirty-one years of existence.

Charitable trusts vary in their investment requirements, as do other trusts. There are no considerations which apply to all charities and to no other trusts. The sole reason for legislating on charity investments separately is that the occasion arose when Parliament was considering a Charities Bill. That it would introduce a distinction between charitable and other trusts is in itself no reason for abstaining from making an Order relating to charities: that reason is precluded by the will of Parliament in conferring the power. However, if an Order made for charities is suitable for all trusts, and a similar Order would be wholly or partly *intra vires* s.13 Trustee Investments Act 1961 it is to be hoped that the Treasury would do for other trustees as much as they could of what they approve the Home Secretary doing for charity trustees, notwithstanding that a general review of the law governing trustee investments may be in train.

The text of the Charities Act 1992 section 38 is:

(1) The Secretary of State may by order made with the consent of the Treasury -

(a) direct that, in the case of a trust fund consisting of property held by or in trust for a charity, any division of the fund in pursuance of section 2(1) of the Trustee Investments Act 1961 (trust funds to be divided so that wider-range and narrower-range investments are equal in value) shall be made so that the value of the wider-range part at the time of the division bears to the then value of the narrower-range part such proportion as is specified in the order;

(b) provide that, in its application in relation to such a trust fund, that Act shall have effect subject to such modifications so specified as the Secretary of State considers appropriate in consequence of, or in connection with, any such direction.

(2) Where, before the coming into force of an order under this section, a trust fund consisting of property held by or in trust for a charity has already been divided in pursuance of section 2(1) of that Act, the fund may, notwithstanding anything in that provision, be again divided (once only) in pursuance of that provision during the continuance in force of the order.

(3) No order shall be made under this section unless a draft of the order has been laid before and approved by a resolution of each House of Parliament.

(4) Expressions used in this section which are also used in the Trustee Investments Act 1961 have the same meaning as in that Act.

(5) In the application of this section to Scotland, "charity" means a recognised body within the meaning of s.1(7) of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1990.

Investment Pursuant to Statutory Regulations: Section 39

The First Schedule to the Trustee Investments Act, 1961 currently lists the types of narrower-range (fixed capital value and mostly fixed interest) and wider-range investments which trustees are allowed to make if not prohibited by their trust instrument and to which they are restricted if that instrument does not give them wider powers. Section 39 of the Charities Act 1992, when it comes into force, will empower the Secretary of State, with the consent of the Treasury and with the approval of both Houses of Parliament, to make regulations authorising the investment of charity property or the property of a recognised body in other investments not expressly excluded by the terms of the trust. If regulations are made, they will confer powers additional to, not alternative to or in derogation of, any other powers of investment a charity has. Accordingly, it will be necessary for regulations to specify not only what investments may be made but also how much (or what proportion) of the trust funds may be invested in these new goodies and what procedure the trustees must follow (e.g., obtaining and considering advice) before investing.

Since Parliament continues to list types of investment which trustees are authorised to make, rather than laying down standards of conduct in investing (such as prudence in managing the affairs of other people), the question arises for the Home Secretary, the Treasury and the two Houses of Parliament of what additional types of investment charity trustees should be permitted to indulge in. Once again, the fact that the investments might also be suitable for trusts other than charities cannot be a reason for refraining from allowing them to charity trustees, although there is no power to enable other trustees to follow suit. Two obvious candidates for inclusion (ignoring recessions and other possibly temporary phenomena) are the purchase of land for letting at a rent and the buying of shares or debentures not issued in the United Kingdom or securities of those kinds issued by companies not registered in the United Kingdom. Buying non-income-producing property, such as pictures or antique jewellery, with an eye to manic increases in market value, could probably not be authorised because doing that is probably not comprehended within the statute's use of the verb "invest".

The text of section 39 of the Charities Act 1992 is:

(1) The Secretary of State may by regulations made with the consent of the Treasury make, with respect to property held by or in trust for a charity, provision authorising a trustee to invest such property in any manner specified in the regulations, being a manner of investment not for the time being included in any part of Schedule 1 to the Trustee Investments Act 1961.

(2) Regulations under this section may make such provision -

(a) regulating the investment of property in any manner authorised by virtue of subsection (1), and

(b) with respect to the variation and retention of investments so made,

as the Secretary of State considers appropriate.

(3) Such regulations may, in particular, make provision -

(a) imposing restrictions with respect to the proportion of the property held by or in trust for a charity which may be invested in any manner authorised by virtue of subsection (1), being either restrictions applying to investment in any such manner generally or restrictions applying to investment in any particular such manner;

(b) imposing the like requirements with respect to the obtaining and consideration of advice as are imposed by any of the provisions of section 6 of the Trustee Investments Act 1961 (duty of trustees in choosing investments).

(4) Any power of investment conferred by any regulations under this section -

(a) shall be in addition to, and not in derogation from, any power conferred otherwise than by such regulations; and

(b) shall not be limited by the trusts of a charity (in so far as they are not contained in any Act or instrument made under an enactment) unless it is excluded by those trusts in express terms;

but any such power shall only be exercisable by a trustee in so far as a contrary intention is not expressed in any Act or in any instrument made under an enactment and relating to the powers of the trustee.

(5) No regulations shall be made under this section unless a draft of the regulations has been laid before and approved by a resolution of each House of Parliament.

(6) In this section "property" -

(a) in England and Wales, means real or personal property of any description, including money and things in action, but does not include an interest in expectancy; and

(b) in Scotland, means property of any description (whether heritable or moveable, corporeal or incorporeal) which is presently enjoyable, but does not include a future interest, whether vested or contingent:

and any reference to property held by or in trust for a charity is a reference to property so held, whether it is for the time being in a state of investment or not.

(7) In the application of this section to Scotland, "charity" means a recognised body within the meaning of section 1(7) of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1990.