BOOK REVIEW

Investing Charity Funds
Michael Harbottle, Barrister.
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As far as we are aware, this is the first book to be devoted to the legal basis of charity investment in England and Wales. We welcome its publication, which is timely, given the increasing focus on investment by charities following the termination of the investment function of the Official Custodian for Charities and the collapse of Barings. It covers the area quite comprehensively and indeed discusses matters not dealt with in the standard texts on charity and trust law, including insights into the Charity Commissioners' policy and practice. The importance of investment to charities is indicated by the Henderson Top 2000 Charities 1996, which shows that the largest charities derive a total of 14% of income from interest, dividends and rents - although in a quarter of individual cases the figure rises to 86% or more.

The author was for eleven years an employee of the Charity Commissioners for England and Wales, the last six as senior lawyer responsible for investment issues. He is now principal of Harbottle Associates, a charity consultancy.

The book starts by discussing the common law principles relating to investment and then covers the Trustee Investments Act 1961, and other statutory powers. It then deals with express investment powers, and the conferring of wider investment powers. The chapter on management deals with advice and delegation, followed by a discussion of the power to delegate to discretionary managers and the use of nominees. There are then two chapters on common investment funds and pooling schemes. A chapter on ethical investment is followed by one dealing with underwriting, swaps, futures and options. After discussing investment in land and the consequences of improper investment, the author ends with an overview, which considers possible amendments to the Trustee Investments Act 1961, and liability insurance. The Appendices include model investment clauses and a model clause permitting delegation to a fund manager and use of nominees.

Particularly interesting sections include the discussion of whether the Trustee Investments Act 1961 applies to corporate charities. After discussing various cases, Harbottle concludes that there is genuine uncertainty as to whether this is the case, although he assumes it to be so for the purpose of the book. He cites the remark of Slade J in *Liverpool and District Hospital for Diseases of the Heart v A-G* [1981] Ch 193 that "a [charitable] company is in a position analogous to that of a Trustee in relation to its corporate assets" as authority for the directors of a charitable company being subject to the normal principles of trust law when deciding how to invest the company's property, even though such a company does not hold its assets on trust for charitable purposes.

We are also glad that Harbottle has not shrunk from criticising the Charity Commissioners' policy in a number of areas. He questions their views on the use of derivatives and foreign currencies and points out that their policy of limiting the proportion of a portfolio that may properly be invested in overseas securities to 20% is restrictive compared to the widely adopted City allocation of around 30%.

Unfortunately, the book has several glaring omissions. In the discussion of ethical investment, there is no reference to the widely-known case involving the Bishop of Oxford, *Harries v Church Commissioners for England* [1993] 2 All ER 300 (which is also relevant to the development of the common-law prudent investor rule). Despite the sentence in the Preface that "the law is stated as at 1 August 1995", the chapter on the conferring of wider investment powers makes no reference to *Decisions of the Charity Commissioners* Volume 3 (January 1995) with its full exposition of the Commissioners' policy on "Schemes Conferring Wider Powers of Investment".

Nor is there any reference to *Nestle v National Westminster Bank* [1993] 1 WLR 1260, which is an important case, both in the development of the prudent investor rule and in any discussion of trustees' liability for improper investment. The Court of Appeal was faced with a claim that the defendant bank had failed to meet the prudent investor standard in its management of a trust fund over a period of some 60 years. Notwithstanding that the bank had (i) failed to seek advice on, and indeed had misunderstood, the terms of the investment clause, and (ii) had apparently omitted to conduct regular reviews, at least between 1927 and 1959, the claim failed.

There is no discussion of the important question of reserves, including the Charity Commissioners' policy (which is currently under review) and the peculiarities of the rule against excessive accumulation (which does not apply where a company is the settlor of a charitable trust or to a corporate charity).

Harbottle refers to the expanding range of investments and to the increasingly sophisticated financial tools available, without discussing the roles of total return and asset allocation as responses to what he calls the investment dilemma, namely the desire to produce income while preserving and enhancing the real value of a charity's capital. His discussion of the principles of investment, while referring to the benefits of diversification, tends to treat individual investments in isolation, rather than looking at them in the context of the overall portfolio, which is one of the key tenets of modern portfolio theory. This approach is validated by the words of Hoffman J in the *Nestle* case (at first instance - unreported): "Modern trustees acting within their investment powers are entitled to be judged by the standards of current portfolio theory which emphasises the risk level of the entire portfolio rather than the risk attaching to each investment taken in isolation".

While Harbottle has endeavoured to grapple with a wide variety of investment concepts, and is to be lauded for covering swaps, futures and options, his understanding of them is limited. For example, the explanation of a swap in paragraph 11.21 is not a swap at all, but what is known as a "swaption", or option on a swap. And the definition in paragraph 11.28 of traded options is misleading - a "traded" option is one traded in standardised terms on a recognised exchange as distinct from an "over the counter" option created by a financial intermediary in a customised transaction. It would have helped readers (and possibly the author) if a glossary of investment terms had been included.

There are other less serious errors and omissions, perhaps inevitable in the first edition of a work of this nature, but suggesting that the manuscript has not been read by expert legal or investment practitioners.

With regard to future developments in the law, the author fails to mention the formation of the Trust Law Committee in 1994, whose work on the extension of trustees' powers of investment and delegation has resulted in the government's announcement in December 1995 that a consultation paper on reform of the Trustee Investments Act 1961 will be issued by 1 May 1996. It is thus likely that far-reaching changes will be in place by 1997, which will, unfortunately, render several chapters of the book out of date.

The book is stated to be aimed at charity trustees and their advisers and, by trying to cover both, it has tended to fall between two stools. While containing a full list of cases, statutes, etc., there is a lack of citation of references in the text which the professional would find useful as authority for the many points made for which such sources exist (including Charity Commissioners' leaflets, Reports and Decisions). On the other hand, the discursive and somewhat repetitive style makes the book less useful as a quick reference source for the charity trustee or finance director who wants "the bottom line". Indeed there are occasions when an incorrect inference could be drawn unless the relevant text is read thoroughly and completely.

There is a valuable and worthwhile book trying to escape from this one and we hope that perhaps a new edition may be produced when the law has been reformed, which would be tighter, more rigorous and user-friendly. However, despite its shortcomings, the present work will be a useful reference for charity legal advisers and the finance directors of larger charities. As well as dealing with investment, the book also provides useful guidance to charity trustees when carrying out their other functions. For example, readers will find helpful material on general principles of liability for breach of trust, remedies for breach of trust and defences to such actions. If readers are concerned primarily with investment matters, they may find that a much simpler and broad brush reference source, written from the investment practitioner's point of view, meets their needs. Such is *Managing Charitable Investments* by John Harrison (ICSA Publishing, 1994; £15.95), which sketches the legal framework, while concentrating on practical issues of setting investment policy, the role of reserves, asset allocation, risk management and implementation.

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