

Agenda item:	5
Report title:	Report of the Investment Sub-Committee 2015/16
Report by:	Vicky Elkin , Governance Manager, Office of the Chair and Chief Executive, velkin@gmc-uk.org , 020 7189 5269
Action:	To consider

Executive summary

This is the first annual report to Council outlining the Investment Sub-Committee's work since January 2015. Following this first report, which has been timed to allow for the most up-to-date information related to placing GMC funds under management, the Sub-Committee will report to Council in February of each year, from 2017.

The Sub-Committee is also required to undertake an annual review of the Investment Policy. Following this report, the Sub-Committee agreed that it would conduct the Investment Policy review in Quarter 1 of each year from 2017, and that it would be reported to Council separately from its annual report on its activities. It was also agreed that a summary of investment performance would be reported to Council at each of its meetings as part of the normal reporting of financial performance within the Chief Operating Officer's report.

Recommendations

Council is asked to:

- a** Consider the report on the work of the Investment Sub-Committee in 2015/16.
- b** Agree the proposed changes to the Investment Policy, at [Annex A](#).

Report of the Investment Sub-Committee's activities in 2015/16

- 1** Council agreed to establish the Investment Sub-Committee at its meeting on 25 September 2014. Following this, the Sub-Committee met once in shadow form on 22 January 2015 to agree its proposed ways of working, and then a further four times in March, June, September and November 2015. Additionally it met once in April 2015 to have a briefing on ethical issues in investments.
- 2** The Sub-Committee also considered one issue on email circulation between meetings, to agree amendments to the Investment Policy and its Statement of Purpose before consideration by Council at its meeting on 30 September 2015.
- 3** In 2016, the Sub-Committee has met once so far, on 23 March 2016.

Membership

- 4** The Investment Sub-Committee's membership includes four Council members, two external co-opted members (appointed in March 2015), the Chief Operating Officer, the Director of Resources and Quality Assurance and the Assistant Director of Finance and Procurement. Ajay Kakkar stood down in December 2015, and at its meeting on 25 February 2016 Council agreed to appoint Enid Rowlands as a member of the Sub-Committee. Jason Britton, one of the external co-opted members, stood down in December 2015, and a recruitment exercise is underway to seek to fill the vacancy by end Quarter 2 2016.
- 5** The Sub-Committee's Statement of Purpose had originally included provision for the appointment of an external investment adviser. Following the appointment of the external co-opted members, the Sub-Committee agreed that it was not necessary to appoint an external investment adviser to attend Sub-Committee meetings on a routine basis, but that they would be engaged on a case-by-case basis as the need arises for periodic review. Council agreed this change to the Sub-Committee's Statement of Purpose at its meeting on 30 September 2015.

Appointment of fund managers and framework for monitoring performance

- 6** Following a rigorous tendering and interview process, the Sub-Committee agreed to appoint CCLA, who are specialists in ethical investment management for the charity, church and local authority sectors, as fund managers from December 2015, and that this appointment would be on an ongoing basis, subject to periodic performance review.
- 7** Following the recent period of market volatility, the Sub-Committee decided to invest £10 million through CCLA's pooled COIF Ethical Investment Fund, to ensure strong diversification, and to minimise the risk of unpredictable losses in specific securities.

- 8** The Sub-Committee agreed an initial short-term asset allocation to reflect market conditions, moving to a more strategic medium-term position over time. CCLA will provide monthly reporting on market conditions, to allow the Sub-Committee to consider changes to the initial asset allocation.
- 9** CCLA will provide monthly reporting on the progress of the GMC's investments, which will be considered by the Sub-Committee by telephone conference.
- 10** The Sub-Committee also agreed an internal monitoring framework for assessing fund manager performance, including critical performance benchmarks to create a system of trigger points for action. It agreed that, in addition to periodic reviews which would be undertaken in Quarter 4 of each year, a review could be triggered by any member of the Sub-Committee with concern about the fund manager's performance.

Development of the Investment Policy

- 11** The Investment Policy has a three-tiered approach to cash management; £10 million of funds under management; £20 million held in instant access accounts as working capital; and the balance of funds held in medium term deposits. The Policy requires the GMC's medium term deposits to be held in UK banks, within a defined credit rating framework, with a maximum holding in any one bank of £40 million.
- 12** The Sub-Committee considered the Investment Policy, at [Annex A](#), at its meetings in March and June 2015, and on email circulation in July 2015, and agreed to recommend to Council:
 - a** To change the measure the measure for a target rate of return on investments from the Retail Prices Index (RPI) to the Consumer Prices Index (CPI).
 - b** To remove references to specific targets for strategic asset allocation.
 - c** To strengthen ethical considerations by adding stewardship, using voting rights either directly or through fund managers, to encourage ethical behaviour by firms in which the GMC has an interest.
- 13** Council agreed these proposed changes to the Investment Policy at its meeting on 30 September 2015.
- 14** Following advice from CCLA at its meeting on 23 March 2016, in the light of prevailing market conditions the Sub-Committee recommend that the Investment Policy should be amended to allow for more flexibility in its target rate of return on funds under management. The current target of CPI + 2% was set by Council to limit our risk exposure at a time when a significantly higher level of investment was anticipated (around £40 million). Council subsequently decided to limit our risk exposure by

reducing our investment to £10 million, and holding the balance of our funds in cash and term deposits. The COIF Ethical Fund, through which we propose to invest, has a target return of RPI +5% and so CCLA have indicated that they would need to hold a proportion of our investment in cash in order to achieve our target of CPI +2%. This would effectively reduce our funds under management below £10 million and increase our overall holdings in cash. The Sub-Committee considers that a revised target rate of return based on a range of CPI +2% to +5% would provide us with a greater degree of flexibility to meet our original investment intentions, in the light of prevailing market conditions.

- 15 The Sub-Committee has therefore proposed a change to paragraph 11 of the Investment Policy, at [Annex A](#).

Development of an Investment Risk Register

- 16 The Sub-Committee agreed to proposals for the development of an Investment Risk Register as part of its consideration of risks inherent in investing funds through fund managers and holding cash for investment purposes. The Sub-Committee considers the Investment Risk Register at each of its meetings.
- 17 Consideration was given as to whether making provision within the Investment Policy for funds to be held in UK banks only was necessary and prudent, and the Sub-Committee agreed that given the current low interest rate environment, a detailed review of European banks and counterparty limits would not be undertaken at this time. It also agreed that external advisers would be engaged should a review be undertaken in the future.

Future annual reports to Council

- 18 From 2017 the Investment Sub-Committee's annual report will also include the outcome of the period review/health-check of investment, and the annual report on quantitative and qualitative data for fund manager performance, which will be undertaken in Quarter 4 of each year.

Annual review of the Investment Sub-Committee's Statement of Purpose

- 19 The Investment Sub-Committee reviews its Statement of Purpose, at [Annex B](#), at least once a year and may make suggestions for any necessary amendments to Council.
- 20 The Statement of Purpose was last reviewed by the Sub-Committee at its meeting in June and on email circulation in July 2015, and an updated version which clarified the following points was agreed by Council at its meeting on 30 September 2015:

- a** The Sub-Committee’s role in relation to fund managers.
 - b** To remove references to the Sub-Committee setting the asset allocation.
 - c** To remove the requirement to appoint an independent investment adviser, in light of the expertise gained in the appointment of the external co-opted members.
 - d** To remove the requirement for a quarterly report to Council on the Sub-Committee’s activities.
- 21** At its meeting on 23 March 2016, the Sub-Committee considered its Statement of Purpose, and believes that it remains relevant to its role.

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Investment Policy

Introduction

- 1 As a matter of prudent financial management we must hold sufficient free reserves to meet the financial risks we face, and to ensure that our regulatory independence is underpinned by a strong and stable financial base.
- 2 The need for reserves coupled with the pattern of registration and retention fees received during the year means that we hold significant cash sums. They arise as a consequence of our being in business.
- 3 This policy sets out the approach we will take with all of the funds that we hold.
- 4 Our funds can be separated into three categories: those which are required as working capital for the normal day to day operation of the business; those which we invest under management; and the remaining cash balance which fluctuates during the year.

Working capital

- 5 We will hold £20 million as working capital for normal cash-flow purposes. This amount will be reviewed annually by Council.
- 6 Funds will be held as cash in instant access interest-bearing accounts in UK banks which are subject to regulation by the Financial Conduct Authority.
- 7 As a minimum, the bank must hold at least two out of three of the following short term credit ratings:

■	Moody's	P-2
■	Fitch	F1
■	Standard and Poor's	A-2

- 8** Funds will be managed by the Director of Resources and Quality Assurance who will seek to secure the most advantageous interest rates available, within the constraints of the policy. Funds may be moved between banks during the year to achieve this, but the primary requirements for working capital funds are security and liquidity.

Funds under management

- 9** We will invest £10 million under management. This amount will be reviewed annually by Council.

Attitude to risk

- 10** We have a low risk appetite. We wish to protect against volatility, capital loss and the erosion of asset value by inflation.

Objective

- 11** We seek to generate the best financial return that is consistent with our attitude to risk and therefore aim to achieve a target rate of return on funds under management of inflation (CPI) plus 2% to 5%, over a rolling five year period.
- 12** Asset allocations will be determined by the fund managers in order to achieve the target return and ethical considerations set out in this policy. Fund managers may invest through a mutual fund, segregated portfolio, or a combination of both.
- 13** The asset allocations will be reviewed periodically by the Investment Sub-Committee to ensure that they remain consistent with our low risk appetite. Where more than one fund manager is used, the Investment Sub-Committee will also monitor the aggregate asset allocation to ensure it provides sufficient diversification.

Ethical considerations

- 14** We have adopted a comprehensive ethical investment approach. We seek to avoid those investments that we believe conflict with our charitable aims, and we may invest in companies whose activities are consistent with, or supportive of, our charitable aims. We may also use our position as an investor to influence the corporate behaviour of those companies we invest in.
- 15** We will invest only through fund managers who demonstrate the strongest environmental, social and governance credentials. We seek to specifically exclude investments in companies whose principal purpose is involvement with tobacco, alcohol, gambling, pornography, high-interest rate lending, cluster munitions and landmines.

Remaining cash balances

- 16** The balance of funds held by the GMC during the year, not held as working capital or invested under management, will be held in medium term deposits.
- 17** Medium term deposits will be held in UK banks which are subject to regulation by the Financial Conduct Authority. As a minimum, the bank must hold at least two out of three of the following short term credit ratings:
- | | |
|---------------------|-----|
| Moody's | P-2 |
| Fitch | F1 |
| Standard and Poor's | A-2 |
- 18** The maturity date for medium term deposits should be no longer than 18 months, and no single deposit should exceed £5 million. Term deposits should be spread, on a rolling maturity basis, subject to a maximum exposure of £40 million per bank (including any funds held as working capital in instant access interest-bearing accounts).
- 19** Funds will be managed by the Director of Resources and Quality Assurance who will seek to secure the most advantageous interest rates available, within the constraints of the policy.

Management, reporting and monitoring

- 20** Council is responsible for determining and reviewing the overall investment policy, objectives, risk appetite and target returns.
- 21** Council has delegated to the Investment Sub-Committee responsibility for implementing the investment policy, appointing and managing fund managers, monitoring performance and reporting to Council. Full responsibilities are set out in the Investment Sub-Committee's statement of purpose.
- 22** Professional fund managers are responsible for managing investments in line with the policy, and are accountable to the Investment Sub-Committee for performance. The Investment Sub-Committee may determine benchmarks against which to measure performance.
- 23** Each fund manager is required to provide quarterly valuation and performance data.

Approval and review

- 24** The Investment Policy will be reviewed by Council annually, on the advice of the Investment Sub-Committee. This will reflect the Council's overall financial position, its budgetary requirements, and any changes to the reserves policy.

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Statement of purpose of the Investment Sub-Committee

Purpose

- 1 The purpose of the Investment Sub-Committee is to provide a forum for implementing and reviewing Council's Investment Policy.
- 2 Council is ultimately responsible for determining and reviewing the overall Investment Policy, objectives, risk appetite and target returns. Operational decision-making and implementation of the policy is delegated to the Investment Sub-Committee.

Duties and activities

- 3 The Investment Sub-Committee:
 - a Ensures the management of the assets is consistent with the Investment Policy set by Council.
 - b Monitors the Investment Policy to ensure it remains appropriate, and to recommend changes to Council as appropriate.
 - c Implements changes to the Investment Policy as appropriate.
 - d Establishes and monitors the investment management structure to ensure that it is appropriate to meet the agreed Investment Policy. This includes decisions about the appointment of fund managers, the number of fund managers used, the proportion of assets managed by each manager, and their mandates.
 - e Agrees the terms of appointment of the investment fund managers, including their fee scales.
 - f Implements changes to the investment management structure as appropriate.

- g** Monitors the actual asset allocations chosen by the fund manager, to ensure that the allocation is consistent with the agreed Investment Policy. Where more than one fund manager is appointed, the Investment Sub-Committee will also monitor the aggregate asset allocation to ensure it provides sufficient diversification.
- h** Monitors the performance of each fund manager against agreed objectives by means of regular review of the investment results and other information.
- i** Monitors the corporate governance activities, policies and exercising of voting rights of the investment fund managers.
- j** Meets with the investment fund managers on a regular basis to discuss their performance, actions and future strategy.
- k** Monitors the continued stability of the investment fund managers against agreed objectives. Implementing changes to the investment mandates as necessary.
- l** Monitors and reacts to legislative, financial and economic changes affecting, or potentially affecting, investment policy. The Investment Sub-Committee may engage external professional advisers to undertake a periodic review/health-check of the investment arrangements.
- m** Review the investment policy so that it remains consistent with, and supportive to, Council's overall business plan, budget and reserves policy.

Working arrangements

- 4** The Investment Sub-Committee meets quarterly. Additional meetings may be scheduled if necessary.
- 5** Draft minutes should be cleared by the chair and circulated to members for comment within two weeks of the meeting. The Investment Sub-Committee approves the minutes at its next meeting.
- 6** Membership of the Investment Sub-Committee comprises:
 - a** Four members of Council, one of whom will be appointed as Chair of the Investment Sub-Committee.
 - b** Two external, co-opted members, with extensive investment experience.
 - c** The Chief Operating Officer, the Director of Resources and Quality Assurance and the Assistant Director, Finance and Procurement. Other staff may attend as necessary.

- 7** Fund managers who are appointed to manage investment funds on behalf of the GMC will be expected to attend Investment Sub-Committee meetings.
- 8** A summary of investment performance will be reported to Council as part of the normal reporting of financial performance within the Chief Operating Officer's report. In addition, the Investment Sub-Committee will report annually to Council on its activities.