



HM TREASURY



**CabinetOffice**  
Office of the **Third Sector**



# Charity pooled funds consultation

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**July** 2009





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# 1

## Introduction

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**1.1** The Government announced in the 2009 Budget that it would, together with the Charity Commission, consult on the future regulation of common investment funds (“CIFs”) and common deposit funds (“CDFs”). The policy aim is to move the regulation of these funds away from the Charity Commission and bring it more fully under the Financial Services Authority (FSA), whilst preserving the existing generous UK tax regime.

**1.2** This consultation document sets out a specific proposal to achieve this policy aim, the introduction of a new type of authorised investment fund (AIF), **the charity AIF**, which would be open only to charity investors. The document sets out in overview the proposed regulatory and tax regime for the charity AIF, and asks a number of questions to help the Government assess the possible impacts on funds, managers and investors.

**1.3** The Government will carefully consider the proposal in the light of the consultation responses, and if it decides to take it forward, will publish a more detailed design framework for the proposed charity AIF and seek further views from interested parties.

**1.4** This consultation builds on the changes introduced by the Charities Act 2006, and on the outcome of a previous joint HM Treasury and Charity Commission consultation in 1996. The Government’s aim is to strike the right balance between the need for effective regulation in an increasingly complex economic world and the desire to keep the costs of management and compliance as low as possible.

**1.5** It is important to make clear that this consultation has not been prompted by any concerns over investments in existing CIFs or CDFs. However, as with all investment matters, trustees of charities should take proper advice from a suitably qualified person before they invest, irrespective of whether they are investing with CIFs or other types of investment vehicles.

**1.6** After the Budget 2009 announcement, initial discussions with funds and investment managers raised particular issues around church exempt funds, which are not established by the Charity Commission, but by Act of Parliament or Measure. Whilst the focus of this consultation is on CIFs and CDFs, the Government also wishes to identify what issues would arise if church exempt funds were brought within the proposed new charity AIF framework.



# 2

## Charity pooled funds

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**2.1** Charity pooled investment funds can be divided into four broad categories:

- Common Investment Funds
- Pooling Schemes
- Common Deposit Funds
- Church exempt funds.

### Common Investment Funds

**2.2** Common Investment Funds (CIFs) were established in 1960 to give smaller charities the opportunity to invest collectively in order to benefit from increased investment opportunities and wider diversification. There are currently 45 CIFs being managed by 22 fund managers with charity assets under management in excess of £8.1 billion<sup>1</sup>. [See list at Annex A].

**2.3** CIFs are set up by Schemes made by the Charity Commission under section 22 of the Charities Act 1960 (now repealed) or section 24 of the Charities Act 1993. Before the Charities Act 2006 they were open only to charities in England and Wales, but are now also open to “appropriate bodies” (i.e. bodies established as charitable under the law of Scotland or Northern Ireland and eligible for UK tax relief) where the Scheme permits this. They operate as investment vehicles and are deemed by law to be charities themselves. They are therefore eligible for registration as charities in their own right.

**2.4** CIFs are similar to authorised unit trusts but, unlike authorised unit trusts, they are not authorised or regulated by the FSA. CIFs provide diversification of investment to reduce risk, which is tax efficient, administratively simple and cost efficient. As they are deemed to be charities they enjoy the same tax status as charities.

### Pooling Schemes

**2.5** A Pooling Scheme establishes a particular type of common investment fund whose main characteristic is that the Pooling Scheme and the participating charities must all have exactly the same trustees. A Pooling Scheme allows a body of trustees who administer more than one charity to combine funds from any or all of those charities for investment purposes: this contrasts with the CIFs which are the subject of this Consultation Paper and which are open to different trustees of different charities. Pooling Schemes are outside the scope of the proposals in this Consultation Paper.

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<sup>1</sup> Source: Charity Commission figures.

## Common Deposit Funds

**2.6** Common Deposit Funds (CDFs) are deposit-taking schemes. They are set up by Schemes made by the Charity Commission under section 25 of the Charities Act 1993. They operate as deposit-takers and are deemed by law to be charities themselves. They are therefore eligible for registration as charities in their own right.

**2.7** CDFs provide a deposit-taking scheme which is tax efficient, administratively simple and cost efficient. They enjoy the same tax status as other charities. There are currently 2 CDFs being managed by 2 fund managers with charity assets under management in excess of £1 billion. [See list at Annex A].

**2.8** CDFs are trusts and differ from CIFs in that they do not offer unitised investments; depositing charities own the capital they have placed on deposit together with the interest earned attributable to that capital. Like CIFs, CDFs are not authorised or regulated by the FSA.

**2.9** Generally, CDFs accept deposits from depositing charities and place the money they have accepted on deposit in the money market. The pooling of such money in the form of large sums of money (usually for relatively short duration) on deposit should secure a higher rate of interest for the depositing charities than each charity would otherwise obtain, if undertaken separately.

**2.10** The Charity Commission is responsible for monitoring and regulating the CDFs.

## Church exempt funds

**2.11** In addition to CIFs and CDFs established under the Charities Acts of 1960 and 1993, there are collective investment funds and deposit funds established under statutes or measures concerned with certain church denominations. These are currently exempt from registration with the Charity Commission. The Charities Act 2006 brings in a regime under which exempt charities which do not have a principal regulator will cease to be exempt, and will instead become excepted charities. From October 2009, excepted charities will have to register with the Charity Commission if their annual income exceeds £100,000.

# 3

## The current regulatory framework

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**3.1** The Charity Commission, which currently sets up and regulates CIFs and CDFs, is a statutory corporation and can only do what it is authorised to do by the Charities Acts. The 1993 Act sets out a legal framework within which the Charity Commission will consider new applications for CIFs and CDFs.

**3.2** In exercising its powers to set up CIFs and CDFs, the Commission must so far as is reasonably practicable act in a way which is compatible with its objectives and which it considers most appropriate for the purpose of meeting those objectives. The relevant statutory objectives of the Charity Commission in establishing a CIF are as follows:

- the public confidence objective, i.e. "to increase public trust and confidence in charities".
- the charitable resources objective, i.e. "to promote the effective use of charitable resources".

**3.3** The Charity Commission is not an investment adviser, and cannot offer charities advice about the merits of a particular investment or investment strategy. It does not regulate fund managers or financial advisers other than as charity trustees. It regulates CIFs and CDFs as charities.

### 1998 Regulatory changes for CIFs

**3.4** To provide adequate financial regulation, since 1998 all new CIFs must be administered and managed by:

- a corporate manager authorised by the FSA;
- a corporate trustee authorised by the FSA; and
- an optional board that is independent of the manager and the trustee.

**3.5** Being authorised by the FSA, the Manager and the Trustee are subject to monitoring by the FSA of their business practices. With respect to unauthorised collective investment schemes, FSA requirements and powers are limited compared with the regime that applies to authorised funds.

### The Charity Commission's approach to regulation of CIFs

**3.6** The Commission's approach to the regulation of CIFs is designed to mirror (as far as is appropriate) the requirements of the FSA for authorised collective investment schemes as set out in the Collective Investment Schemes Sourcebook (COLL).

**3.7** Although the provisions of COLL do not, strictly speaking, apply to CIFs, the Commission has decided, as a matter of policy, to have regard to COLL in considering relevant issues and in determining its own regulatory approach towards CIFs.

**3.8** The Commission will evaluate COLL and apply those provisions (with appropriate amendments, if any) that are believed to be advisable for protecting the interest of charities investing in CIFs, but where there is a good reason in the particular circumstances for departing from COLL, the Commission may do so.

**3.9** When the 1998 regulatory framework was introduced for new CIFs, existing CIFs were given the option to convert to the revised framework. The great majority chose to do so, although some opted to remain under the old framework.

## **Regulation of CDFs**

**3.10** CDFs do **not** fall within the definition of a collective investment scheme. Although the operators of CDFs are not required to be regulated under the Financial Services and Markets Act 2000, the Commission has decided, as a matter of policy, that the Managers and the Corporate Trustees (if applicable) should be authorised by the Financial Services Authority (FSA).

## **Regulation of church exempt funds**

**3.11** The Charity Commission currently has no responsibility for regulating church exempt funds, although the 2006 Charities Act will eventually remove their exempt status.

# 4

## The charity AIF proposal

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**4.1** The Government considers that an appropriate way to bring the regulation of CIFs and CDFs more fully within the framework of the FSA is to establish an authorised investment fund (AIF) open only to charity investors, **the charity AIF**.

**4.2** The existing AIF regime is a well understood regulatory and tax framework and charity AIFs would fit within this. AIFs are collective investment schemes authorised and regulated by the FSA.

**4.3** The rules dealing with the constitution and investment powers of AIFs are set out in the 'COLL' sourcebook published by the FSA. This can be found on the FSA website at [www.fsahandbook.info/FSA/html/handbook/COLL](http://www.fsahandbook.info/FSA/html/handbook/COLL).

### Categories of AIF

**4.4** All AIFs (whichever legal form they take) fall into one of three categories defined by the FSA.

- **UCITS funds** are AIFs that are within the terms of the European directive for undertakings for collective investments in transferable securities (UCITS). In accordance with the FSA 'COLL' sourcebook the instrument constituting the scheme must state that the scheme is a UCITS scheme. These schemes can be marketed to retail investors within any European Union member state.
- Non-UCITS retail funds (often referred to as **NURS funds**) are any AIFs which, whilst not being UCITS schemes are not Qualified Investor Schemes. Their investment powers are less restricted than UCITS schemes. They can be marketed to retail investors.
- **Qualified Investor Schemes (QIS)** are AIFs with wider investment and borrowing powers than either UCITS funds or NURS funds and can be marketed only to 'qualified' investors as defined by the FSA within the COLL sourcebook.

**4.5** AIFs may take the form of unit trusts, which have been in existence since 1931 or open-ended investment companies (OEICs), available from 1997. Collective investment schemes may or may not be authorised and regulated by the FSA, under the terms of the Financial Services and Markets Act 2000 (FSMA). AIFs are funds which are authorised and regulated by the FSA.

### Setting up AIFs

**4.6** New charity AIFs would be set up in the same way as other AIFs but would be limited to charity investors. The charity AIF would not be a registered charity, or deemed to be a charity, and would be authorised by the FSA. Service standards exist for the time in which authorisation must be granted or refused.

## Alternative Investment Fund Managers Directive

4.7 At the end of April 2009, the European Commission published proposals for a Directive which would apply to the operators of "Alternative Investment Funds". As set out in the draft Directive, this is broadly defined and could be interpreted to include all three types of charity funds covered by this consultation. The Directive is currently under negotiation within the European Council and Parliament and so the outcome is uncertain. However, respondents may want to consider whether they may be affected in future by this Directive (whether or not they remain in their current format or become authorised investment funds).

### Questions

- 4(i) The proposal is that existing CIFs and CDFs would become charity AIFs. Are there any adverse consequences of this proposal, and how might they best be mitigated?
- 4(ii) Are there any funds for which the OEIC category would be more favourable than the AUT category, and if so, why?
- 4(iii) When church exempt funds cease to be exempt from registration as charities, should they be brought within the charity AIF regime, and if not, how best should they be regulated?
- 4(iv) Charity AIFs would not be charities themselves. Would this have any adverse impacts, and if so, how might they be minimised?

# 5

## Regulatory issues

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**5.1** The regulatory framework for AIFs is set out in the Financial Services and Markets Act 2000 (FSMA) and the Open Ended Investment Company (OEIC) Regulations 2001, further supported by the FSA Handbook.

### Structure of funds

**5.2** Authorised investment funds can be structured as Authorised Unit Trusts (AUTs) or OEICs, depending on whether the fund is set up as a trust or as a body corporate. FSMA and the OEIC Regulations require that funds have legally separate managers and depositaries (known as a 'trustee' for a unit trust). One role of the depositary is to safekeep the fund's assets, and this separation of the fund's assets from the manager is considered a fundamental investor protection measure. Both the manager and depositary of an AIF, as well as the fund itself, will be authorised by the FSA.

**5.3** An OEIC has a Board of Directors. Usually this consists of a single corporate director, also authorised by the FSA. However, there is the option to also have additional directors.

### COLL Rules

**5.4** The FSA Handbook contains a number of different parts. As outlined in chapter 3 the COLL sourcebook is most pertinent for the operation of collective investment schemes, and includes rules on matters including:

- Fund documentation;
- Relations with and rights of investors (eg when changes to the fund are proposed);
- Qualitative and quantitative controls on funds' investment powers;
- Fund valuation, pricing and dealing; and
- Powers and responsibilities of funds' managers and depositaries.

**5.5** Discussions with current operators of charity pooled funds have highlighted some areas of the COLL rules that may need to be amended for a charity AIF. For example, the current requirement that all a fund's income is distributed prevents the kind of 'income smoothing' that some charity pooled funds currently provide.

**5.6** Subject to consideration of a number of charity AIF specific requirements, it is envisaged that the COLL sourcebook could apply in its entirety to charity funds.

### Other FSA rules

**5.7** The other parts of the FSA Handbook cover issues including systems and controls, prudential requirements and conduct of business requirements. Frequently they reflect the requirements of various European Directives. Because these provisions are aimed at the manager or depositary of the fund, rather than the fund itself, many of them may already apply when an FSA authorised firm is involved with a charity pooled fund.

## Questions

- 5(i) How would the current governance structures of charity pooled funds need to change, given the possible AUT or OEIC structures?
- 5(ii) Would it be preferable to specify that charity AIFs must take the format of NURS (rather than UCITS schemes or QISs)?
- 5(iii) Which requirements of COLL would be unduly burdensome for charity AIFs? Please explain why and provide details of compliance costs, where possible.
- 5(iv) Which requirements of the FSA Handbook outside COLL would be unduly burdensome for charity AIFs? Please explain why and provide details of compliance costs, where possible.
- 5(v) What, if any, transitional arrangements should be made for charity pooled funds converting to charity AIFs? Please explain why and provide details of compliance costs, where possible.

# 6

## Tax issues

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**6.1** The basis of the proposed charity AIF tax framework is to move the point of taxation from the AIF to the investor (i.e. the charity), with the result that the investor faces broadly the same tax treatment as they would had they owned the underlying assets directly.

**6.2** The Government is keen to minimize the costs and administrative burdens of changing to the new framework, and to ensure that the charity AIF does not provide opportunities for tax avoidance.

### Current tax status of CIFs and CDFs

**6.3** CIFs and CDFs enjoy the same tax status as charities. They are exempt from tax on all income and gains that are applied for charitable purposes only. If income was not applied for charitable purposes then it would be taxable.

**6.4** CIFs and CDFs normally pay gross distributions without deduction of tax. CIFs pay distributions in the form of dividends and CDFs pay interest to investors. The charity investors are not taxed on these distributions, provided they are applied wholly for charitable purposes.

**6.5** CIFs and CDFs are normally exempt from Stamp Duty Land Tax and Stamp Duty Reserve Tax, but as they are not authorised funds, are required to charge VAT on their management fees.

### Proposed tax regime for charity AIFs

**6.6** The charity AIF could be either an authorised unit trust (AUT) or an open-ended investment company (OEIC). A charity AIF must ensure that only charities hold its units and will be subject to tax consequences (including possible loss of its charity AIF status) if this is not the case.

**6.7** AIFs are subject to corporation tax, but only on income, not on chargeable gains. It is proposed that charity AIFs will similarly be subject to corporation tax, but not on chargeable gains.

**6.8** AIFs are chargeable to corporation tax at 20 per cent on taxable income. However, most dividends are already exempt from tax. If the AIF has general management expenses these can be set off against any taxable income such as interest or rental income.

**6.9** It is proposed that charity AIFs would also be chargeable to corporation tax at 20 per cent on income. It is possible that CIFs and CDFs which mainly invested in equities would not pay any tax on income in practice for the same reasons as other AIFs. However, in order to maintain the current taxation position for CIFs and CDFs, it is proposed to introduce a similar exemption from tax on income that they currently enjoy.

**6.10** That exemption might be achieved by allowing the charity AIFs to deduct distributions of otherwise taxable income made to charity investors in its corporation tax computation. But the income would remain taxable in the AIF if it was distributed to non-charity investors (although in practice the fund scheme rules should not allow non-charities to participate in charity AIFs). The recipient charity would be obliged to use the income for its charitable purposes (or lose its own tax exemption on that income).

**6.11** It is proposed that the charity AIF could either pay a dividend or interest distribution depending on the main form of underlying assets in the funds.

**6.12** AIFs are required by FSA rules to distribute the total amount shown in the accounts as available for distribution to their investors. Investors normally receive a dividend or an interest distribution from an AIF, which would remain so under the charity AIF proposal. The charity investor would be treated as receiving a dividend or a gross payment of yearly interest (i.e. no tax would be withheld).

**6.13** Charity AIFs would retain the current exemptions from SDRT and SDLT enjoyed by CIFs and CDFs, provided this could be achieved without any adverse impact on the wider AIF tax regime.

**6.14** As authorised funds, AIFs are exempt from VAT on their management, including management services delegated to third parties. It is proposed that charity AIFs will also benefit from this treatment, which is more favourable than the current position for CIFs and CDFs.

## Questions

- 6(i) Would the proposal to tax charity AIF income at 20 per cent if the income is not applied for charitable causes have any adverse consequences in practice, and if so, why?
- 6(ii) Are there any circumstances where the requirement that the charity AIF does not withhold tax from distributions work to the detriment of the charity investors?
- 6(iii) Are there any other adverse tax consequences arising from the charity AIF proposal?

# 7

## Summary of questions for consultation

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### Chapter 4

- 4(i) The proposal is that existing CIFs and CDFs would become charity AIFs. Are there any adverse consequences of this proposal, and how might they best be mitigated?
- 4(ii) Are there any funds for which the OEIC category would be more favourable than the AUT category, and if so, why?
- 4(iii) When church exempt funds cease to be exempt from registration as charities, should they be brought within the charity AIF regime, and if not, how best should they be regulated?
- 4(iv) Charity AIFs would not be charities themselves. Would this have any adverse impacts, and if so, how might they be minimised?

### Chapter 5

- 5(i) How would the current governance structures of charity pooled funds need to change, given the possible AUT or OEIC structures?
- 5(ii) Would it be preferable to specify that charity AIFs must take the format of NURS (rather than UCITS schemes or QISs)?
- 5(iii) Which requirements of COLL would be unduly burdensome for charity AIFs? Please explain why and provide details of compliance costs, where possible.
- 5(iv) Which requirements of the FSA Handbook outside COLL would be unduly burdensome for charity AIFs? Please explain why and provide details of compliance costs, where possible.
- 5(v) What, if any, transitional arrangements should be made for charity pooled funds converting to charity AIFs? Please explain why and provide details of compliance costs, where possible.

### Chapter 6

- 6(i) Would the proposal to tax charity AIF income at 20 per cent if the income is not applied for charitable causes have any adverse consequences in practice, and if so, why?
- 6(ii) Are there any circumstances where the requirement that the charity AIF does not withhold tax from distributions work to the detriment of the charity investors?
- 6(iii) Are there any other adverse tax consequences arising from the charity AIF proposal?



# 8

## Next steps

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### How to respond

**8.1** The Government welcomes comments on the questions in this consultation paper. Any comments should be sent to:

Jeremy Sherwood  
Personal Tax Team  
HM Treasury  
1 Horse Guards Road  
London  
SW1A 2HQ

Alternatively, please e-mail: [charity-funds-consultation@hm-treasury.x.gsi.gov.uk](mailto:charity-funds-consultation@hm-treasury.x.gsi.gov.uk)

**8.2** Comments should be received **by 31 October 2009**.

**8.3** HM Treasury, the FSA, the Office of the Third Sector and the Charity Commission will continue to discuss the issues outlined in this paper with charity pooled funds, investment fund managers, charity investors and other interested parties.

**8.4** The Government will carefully consider the responses, and if it decides to take the charity AIF proposal forward, will publish a more detailed framework and invite comments from interested parties.

### Confidentiality Disclosure

**8.5** Information provided in response to this discussion document, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

**8.6** If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury, the FSA, the Office of the Third Sector, or The Charity Commission.

**8.7** HM Treasury, the FSA, the Office of the Third Sector and the Charity Commission will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

## Code of practice for written consultation

**8.8** This consultation process is being conducted in line with the Code of Practice for written consultation (<http://www.berr.gov.uk/files/file47158.pdf>) which sets down the following criteria:

- Formal consultation should take place at a stage when there is scope to influence the policy outcome.
- Consultations should normally last for at least 12 weeks with consideration given to longer timescales where feasible and sensible.
- Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence and the expected costs and benefits of the proposals.
- Consultation exercises should be designed to be accessible to, and clearly targeted at, those people the exercise is intended to reach.
- Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.
- Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.
- Officials running consultations should seek guidance in how to run an effective consultation exercise and share what they have learned from the experience.

**8.9** If you feel that this consultation does not fulfil these criteria, please contact:

Luke McInerney

Growth, Competition and Markets Team

HM Treasury

1 Horse Guards Road

London

SW1A 2HQ

Email: [luke.mcinerney@hm-treasury.gov.uk](mailto:luke.mcinerney@hm-treasury.gov.uk)

# A

## List of charity pooled funds

<b>Names of Common Investment Funds</b>	<b>Registration Numbers</b>	<b>Fund Manager</b>
COIF Charities Investment Fund	218,873	CCLA
Charinco CIF	270,540	BlackRock
Charishare CIF	295,634	BlackRock
COIF Charities Fixed Interest Fund	803,610	CCLA
The Bond Fund for Charities	1,014,756	JP Morgan
The UK Equity Fund for Charities	1,014,758	JP Morgan
Targeted Return Fund	1,015,446	Barings
The Alpha Common Investment Fund for Endowments	1,025,527	Sarasin Chiswell
Common Fund for Income	1,038,265	HSBC
Common Fund for Growth	1,038,267	HSBC
The Charity Fixed Interest Fund	1,038,561	Schroders
The Charity Equity Fund	1,038,563	Schroders
Chariguard Fixed Interest Fund	1,039,352	RCM
Chariguard UK Equity Fund	1,039,354	RCM
Chariguard Overseas Equity Fund	1,045,682	RCM
Charishare Tobacco Restricted Fund	1,062,581	BlackRock
The Income Trust for Charities	1,065,732	Cazanove
The Growth Trust for Charities	1,065,734	Cazenove
Diversified Charity Fund	1,066,827	Lazard
ChariTrack Common Investment Fund	1,077,125	BGI
The Charities Property Fund	1,080,290	Rensburg Sheppards
Affirmative Fixed Interest Fund for Charities	1,087,227	Epworth
Affirmative Equity Fund for Charities	1,087,228	Epworth
Global Growth and Income Fund for Charities	1,089,229	Newton
COIF Charities Property Fund	1,093,084	CCLA
Armed Forces Common Investment Fund	1,093,529	BlackRock
Absolute Return Trust for Charities	1,094,498	Cazenove
Equity Income Trust for Charities	1,094,572	Cazenove
CAF UK Equitrack Fund	1,108,291	Legal&General
The Alpha Common Investment Fund for Income and Reserves	1,110,710	Sarasin Chiswell
Charity Select Global (ex UK) Equity Fund	1,114,640	Aberdeen
Charity Select UK Bond Fund	1,114,641	Aberdeen
Charity Select UK Equity Fund	1,114,643	Aberdeen
Accommodation Investment Fund for Charities	1,115,363	Cordea Savills
Charifaith Common Investment Fund	1,116,156	BlackRock
The Multi-Strategy Property Trust for Charities	1,116,505	Cazenove
Charity Value and Income	1,119,289	OLIM
The Charity Multi-Asset Fund	1,119,649	Schroders
COIF Charities Global Equity Income Fund	1,121,433	CCLA

National Association of Almshouses CIF	223,887	M&G
Charibond Common Investment Fund	271,815	M&G
CAF UK Equity Growth Fund	803,287	CAF
CAF Bond Income Fund	803,288	CAF
Combined Charitable Income Fund	1,059,272	UST
Combined Charitable Capital Fund	1,059,275	UST
<b>Common Deposit Funds</b>		
COIF Charities Deposit Fund	1,046,249	CCLA
The Affirmative Deposit Fund for Charities	1,115,887	Epworth

# B

## Impact Assessment

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## Summary: Intervention & Options

<b>Department /Agency:</b> CC, HMT, HMRC, FSA	<b>Title:</b> Impact Assessment of change of regulation of Common Investment Funds and Common Deposit Funds	
<b>Stage:</b> Consultation	<b>Version:</b> 1	<b>Date:</b> 30 July 2009
<b>Related Publications:</b> Consultation document		

### Available to view or download at:

[http://www.hm-treasury.gov.uk/consult\\_index.htm](http://www.hm-treasury.gov.uk/consult_index.htm)

**Contact for enquiries:** Jeremy Sherwood

**Telephone:** 020 7270 6190

### What is the problem under consideration? Why is government intervention necessary?

Common Investment Funds(CIFs) and Common Deposit Funds (CDFs) are currently created by the Charity Commission (CC) and deemed to be charities. The funds in question administer billions of pounds worth of investments on behalf of charities. Currently they are exempt from regulation as financial products and the only regulator is the CC which regulates them as charities. In the increasingly complex economic world it is right to revisit the regulatory framework to ensure it continues to meet the needs of charity investors.

### What are the policy objectives and the intended effects?

The objective is to consider the case for moving the regulation of CIFs and CDFs away from the Charity Commission and bring them more fully within the regulation of the Financial Services Authority whilst preserving their current tax status as far as possible.

### What policy options have been considered? Please justify any preferred option.

Preserving the existing situation is a possible option, given that the FSA already regulates the great majority of CIF fund managers and trustees (although in respect of their operation of unregulated collective investment schemes, the regulation is limited). However, the CC considers it does not have the necessary expertise to approve and regulate increasingly complex financial products, and the current dual regulation by the FSA and the CC imposes an extra administrative burden.

The current preferred option is to design a new form of authorised investment fund that would be regulated by the FSA and open only to charity investors. This would remove from the CC its role in setting up and regulating CIFs, and preserve as far as possible the current tax reliefs enjoyed by CIFs.

### When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

The policy will be reviewed after five years.

### **Ministerial Sign-off** For Consultation Impact Assessments:

*I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.*

Signed by the responsible Minister:



.....Date: 21<sup>st</sup> July 2009

## Summary: Analysis & Evidence

<b>Policy Option:</b>	<b>Description:</b>
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<b>COSTS</b>	<b>ANNUAL COSTS</b>		<p>Description and scale of <b>key monetised costs</b> by 'main affected groups'</p> <p>A new charity AIF would need to pay an authorisation application fee currently of £1,500 to be considered as a NURS fund. A charity AIF would have to pay an annual ("periodic") fee of currently up to £570. The transition costs are estimated on the basis of 45 CIFs paying an initial application fee, and the annual costs on the basis of 45 charity AIFs paying the annual fee, with around 5 new charity AIFs paying the £1,500 application fee per year.</p> <p>Managers and depositaries may incur additional costs (that could ultimately be borne by the charity funds themselves) compared to the current situation if charity pooled funds become charity AIFs. It is not possible to quantify these costs at the present time until the design of the regulatory regime becomes clearer. This paper asks questions to help determine the detail of that regime.</p> <p>The FSA is required, when consulting on changes to its rules, to include in the consultation an estimate of the costs together with an analysis of the benefits that will arise from the making of the proposed rules. To the extent that managers and depositaries of charity AIFs already also deal with authorised funds, and so have the systems and procedures in place to comply with COLL, any additional compliance costs will be mitigated.</p>
	<b>One-off (Transition)</b>	<b>Yrs</b>	
	£ <b>67,500</b>		
	<b>Average Annual Cost</b> (excluding one-off)		
£ <b>33,150</b>		<p><b>Total Cost (PV)</b> £ <b>100,650</b></p>	
Other <b>key non-monetised costs</b> by 'main affected groups'			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		<p>Description and scale of <b>key monetised benefits</b> by 'main affected groups'</p> <p>Benefit to the CIFs/CDFs of not completing Charity Commission annual return £11,250.</p> <p>Benefit to the Charity Commission of not regulating CIFs/CDFs £173,454</p>
	<b>One-off</b>	<b>Yrs</b>	
	£ <b>Nil</b>		
	<b>Average Annual Benefit</b> (excluding one-off)		
£ <b>184,704</b>		<p><b>Total Benefit (PV)</b> £ <b>184,704</b></p>	
Other <b>key non-monetised benefits</b> by 'main affected groups'			

Key Assumptions/Sensitivities/Risks

Price Base Year	Time Period Years	Net Benefit Range (NPV) £		NET BENEFIT (NPV Best estimate) £	
What is the geographic coverage of the policy/option?				UK	
On what date will the policy be implemented?				not known	
Which organisation(s) will enforce the policy?				FSA/HMRC	
What is the total annual cost of enforcement for these organisations?				Not known	
Does enforcement comply with Hampton principles?				Yes	
Will implementation go beyond minimum EU requirements?				Yes	
What is the value of the proposed offsetting measure per year?				£ nil	
What is the value of changes in greenhouse gas emissions?				£ nil	
Will the proposal have a significant impact on competition?				No	
Annual cost (£-£) per organisation (excluding one-off)		Micro	Small	Medium	Large
Are any of these organisations exempt?		NK	NK	N/A	N/A
<b>Impact on Admin Burdens Baseline</b> (2005 Prices)				(Increase - Decrease)	
Increase of £		Decrease of £ 11,250		<b>Net Impact</b> £	

Key:

Annual costs and benefits: Constant Prices

(Net) Present Value

## Evidence Base (for summary sheets)

CIFs are collective investment schemes. They operate as investment vehicles and are deemed by law to be charities themselves. They are similar to authorised unit trusts but, unlike authorised unit trusts, they are not authorised by the Financial Services Authority (FSA). The majority of CIFs are, however, administered and managed by a corporate manager and corporate trustee who are authorised by the FSA and subject to FSA monitoring (but in respect of unregulated collective investment schemes themselves the FSA requirements are limited).

The Charity Commission's approach to the content of schemes for CIFs has regard to the approach of the FSA to authorised collective investment schemes as set out in the Collective Investment Schemes Sourcebook (COLL). In this way the regulatory regime for CIFs is comparable for those collective investment schemes regulated by the FSA.

The Commission's power to create CIFs was introduced in 1960, when the investment context was very different. There was not the range of collective investment products or underlying investments available that there is today. The power introduced by the Charities Act 1960 was seen as a way of enabling smaller charities to pool their funds so they had access to more efficient investment strategies and the world financial markets. It was envisaged that for a charity to invest in a CIF would discharge the trustees from further consideration of their investment duties.

The investment context today is a very different matter. There has been a huge increase in the number of collective investment schemes pursuing a large range of complex investment strategies. It is no longer so simple for charities to discharge their investment responsibilities simply by investing in a CIF. They have to consider carefully the risks and investment strategies involved and weigh these with the needs of their charities.

For some years the CC has considered that it is appropriate for an investment vehicle to be regulated as such rather than as a charity. Increasingly, the CC is being asked to establish as CIFs investment vehicles with complex investment strategies of which the CC has limited experience.

Accordingly, it may be more appropriate to develop a new product which is subject to regulation as an investment product while preserving the existing tax benefits for charities investing in such a product. The policy aim is to make provision for existing CIFs and CDFs to become products of this nature.

The transitional and annual costs are based on around 45 CIFs applying for registering as charity AIFs, at a potential registration cost of £1,500 each, and annual fee of £570. Based on historical trends for CIFs, up to 5 new charity AIFs could be expected to be set up annually, each with an initial application fee of £1,500.

The benefit to the CIFs/CDFs of not completing the Charity Commission's annual return is estimated at £11,250. This is calculated on the basis that there are 45 CIFs/CDFs that are required to prepare a return and the cost to each of preparing the return is £250. The annual return is likely to be completed by the CIF corporate manager and will form a small part of the overall regulatory work undertaken; the majority of regulatory work carried out is to meet FSA requirements. Fund manager fees (normally charged to the fund) are based on the size of investment, which will encapsulate the salary cost of the fund manager. Based on a salary of £60,000 per annum the employers' cost of seven hours work, the time estimated by the Charity Commission to complete the annual return, is £250 per fund.

The benefit to the Commission of not regulating the CIFs/CDFs is £173,454. This is calculated as follows:

		Direct cost	Overheads (70%)	Total
PB4	Full time	£32,000	£22,400	£54,400
PB5	Full time	£40,000	£28,000	£68,000
PB6a legal	33.3%	£18,315	£12,821	£31,136
Board discussion	3 hours	See below		£5,546
2 Commissioners	69 hours combined at £50 per hour	£3,450	N/A	£3,450
Chief executive	15 hours	£1,307	£915	£2,222
Director of legal services	99.5 hours	£5,118	£3,583	£8,701
<b>TOTAL</b>				<b>£173,454</b>

*3 hours board discussion*

		Direct cost	Overheads (70%)	Total
Chair	1 day	£635		£635
8 members	1 day each at £350 per day	£2,800	N/A	£2,800
Chief executive	Half day	£312	£218	£530
Directors	2 days combined	£740	£518	£1,258
PB6a	Half day	£116	£81	£197
PB4	Half day	£74	£52	£126
<b>TOTAL</b>				<b>£5,546</b>

### **Administrative Burden impact**

Currently the managers and corporate trustees of most CIFs and CDFs are regulated by the FSA but CIFs and CDFs are not. The move to such funds becoming authorised funds regulated by the FSA is likely to provide additional flexibility for alterations to the fund structure without the need for additional schemes. As the manager, corporate trustee and the product will be regulated by the FSA there is also likely to be less duplication and the administrative burden of administering a CIF or CDF is likely to be reduced.

### **Specific impact tests**

#### *Competition Assessment*

The competition assessment impact from this policy option is not likely to be significant. The model Scheme for CIFs requires a fund manager who is authorised by the FSA and a corporate Trustee who is authorised by the FSA. Accordingly, they are likely to be familiar with the requirements for an authorised investment fund. There are a small number of CIFs who were not established with the model scheme which are not subject to these requirements. However, the Charity Commission is not creating any further CIFs other than by the model scheme.

#### *Small Firms Impact Test*

This policy option should not have an adverse impact on small firms given the existing requirement in the model schemes for CIFs and CDFs that a fund manager and a corporate trustee be authorised by the FSA.

#### *Legal Aid*

There is no impact on legal aid from this policy option.

#### *Sustainable Development*

There is no impact on sustainable development from this policy option.

#### *Carbon Assessment*

As this policy will eliminate dual regulation of CIFs and CDFs the carbon footprint arising from such regulation should similarly diminish.

*Other environment*

The other environment impact from this policy option is neutral.

*Health Impact Assessment*

The health impact assessment from this policy is neutral.

*Race Equality*

The race equality impact from this policy option is neutral.

*Disability Equality*

The disability equality impact from this policy option is neutral.

*Gender Equality*

The gender equality impact from this policy option is neutral.

*Human Rights*

The human rights impact from this policy option is neutral.

*Rural Proofing*

The rural proofing impact from this policy option is neutral.

## Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	Yes	No
Sustainable Development	Yes	No
Carbon Assessment	Yes	No
Other Environment	Yes	No
Health Impact Assessment	Yes	No
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	Yes	No
Rural Proofing	Yes	No

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### **HM Treasury contacts**

This document can be found in full on our website at:  
[hm-treasury.gov.uk](http://hm-treasury.gov.uk)

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