Finance Committee of the Standing Committee

GAB submissions in relation to a Diocesan Investment Strategy

1. The Glebe Administration Board (**GAB**) received the letter from the Finance Committee dated 21 November 2019 at its meeting on 3 December 2019. The GAB appreciates the opportunity to make further submissions in relation to this matter.

2. These submissions expand on the material included in our initial paper to the Standing Committee of 30 June 2019 (**initial paper**) by addressing each of the 5 questions for which the Finance Committee is seeking a response.

3. We acknowledge there are differing views on whether and how to proceed in this matter. Whilst the GAB has a view, we recognise that the decision is ultimately one for the Synod, or the Standing Committee on its behalf, as the appropriate decision-maker in this matter.

Should the two significant pools of central diocesan investments, namely the DE and the LTPF, be amalgamated into a single diocesan investment vehicle?

4. We deal with this question in our initial paper (paragraphs 1-9 of Attachment C) without expressing a concluded view.

5. Our concluded view is that the liquid assets[1] of the Diocesan Endowment (**DE**) and Long Term Pooling Fund (**LTPF**) should be amalgamated into a single long-term, diversified investment vehicle. This was, in essence, the position taken by the Archbishop's Strategic Commission in its 2011 report to the Standing Committee, and was the position initially taken by the Anglican Church Property Trust's (**ACPT**) Investment, Insurance and Finance Committee (**IIFC**) in discussions with the GAB until concerns about the trusteeship of such a vehicle were raised by the ACPT board.

6. As indicated in our initial paper, the arguments for a central diocesan investment vehicle made by the Archbishop's Strategic Commission in 2011 remain as strong now as they were in 2011. The GAB endorses those views. Moreover, each of the reasons given by the Standing Committee in 2012 for not pursuing such a vehicle at that time no longer apply (see Attachment B of our initial paper).

7. In its paper to the Standing Committee of 8 July 2019 (**ACPT paper**), the ACPT offers three main reasons why the Synod should not amalgamate the DE and LTPF.

8. We address each of these in turn.

The risk of amalgamation outweighs the benefit

9. The primary reason given in the ACPT paper for not amalgamating the DE and LTPF is that the benefits of amalgamation do not outweigh the risk in having the two significant central pools of investment of the diocese governed by a single board.

10. In relation to the benefits of amalgamation, the ACPT paper (at paragraph 10) points to the economies which have already been achieved in terms of the discounted fees payable by both the DE and LTPF (as both funds are notionally aggregated by the common external investment

[1] For this purpose, "liquid assets" are non-cash assets, such as holdings in Australian and overseas share funds, which are capable of being realised on short notice.

consultant engaged by both GAB and ACPT, currently Mercer) and the joint meetings of GAB and the IIFC held quarterly with the external investment consultant. The ACPT paper goes on to state (at paragraph 14) –

> The net financial benefit estimated to be achieved from the amalgamation is relatively nominal to justify the effort involved in implementing amalgamation.

11. We agree that some economies have already been achieved under the current arrangements. We also agree that the additional direct cost savings of amalgamation which are capable of ready quantification (mentioned in our initial paper at paragraph 3 of Attachment C) would not of themselves be sufficient to warrant amalgamation.

12. In our view the most compelling reason for amalgamation is the range of benefits that would arise from drawing together on a single board those persons with the best skills and experience in investment management oversight. Although such benefits are not always capable of ready quantification, they are nonetheless real. The most significant of these benefits arises from the focus and value-add that a specialist board would be expected to bring in achieving the missional objectives for which it is responsible. In our initial paper (paragraph 4 of Attachment C) we outline other benefits which would arise from the use of a single specialist board, namely avoiding duplication of effort and opportunity cost in relation to the membership of volunteer boards.

13. This would reflect the Synod's normal pattern for the ordering of the affairs of the Diocese whereby the Synod allocates a distinct set of functions and responsibilities to a distinct diocesan agency governed by a suitably skilled and experienced board. A recent example of this ordering by the Synod is the provision of residential aged care homes and services, and retirement accommodation, by Anglican Community Services, achieved in 2016 though the amalgamation of Anglican Retirement Villages, Diocese of Sydney and the Sydney Anglican Home Mission Society Council. Prior to the amalgamation, both these diocesan bodies provided residential aged care and services, and retirement accommodation (proposed in the case of the Sydney Anglican Home Mission Society Council).

14. We submit the same approach should apply to the management of the liquid long-term investments of the Diocese and liquid long-term investments held centrally on behalf of parishes, a small number of estates and other organisations. We consider the case for taking such an approach in relation to the management of liquid long-term investments is strengthened by the general scarcity of committed Christians with a genuine depth of investment management experience and insight who are willing to serve in this way (an observation made by the Archbishop's Strategic Commission in 2011 which remains at least as true today). We note that this approach has already been taken in relation to short-term cash investments through the Diocesan Cash Investment Fund (**DCIF**).

15. In relation to the risk associated with amalgamation, the ACPT paper (at paragraph 11) refers to the "hard financial and governance lessons learned from the diocesan experience in negotiating the global financial crisis" (**GFC**). The ACPT goes on to state (at paragraph 12) –

> If a conservative approach is taken in relation to investments, there is much to be said for maintaining the present position, so that the major liquid investment funds of the Diocese have two boards considering them rather than having the option of one board only prevail.

16. We agree that hard lessons were learned from the GFC. However, we are not persuaded that this justifies the maintenance of two boards to oversee the management of the long-term investments of the Diocese with very similar investment profiles. Further, we note that since the GFC, there has been significant change and uplift across most diocesan boards in respect of governance and as a consequence, any residual risk associated with having only one board is significantly mitigated to the point of immateriality.

17. In our initial paper (at paragraph 9 of Attachment C) we point out that the most significant risk to diocesan investments relates to the external investment consultant engaged to manage those investments. As the GAB and ACPT currently share the same external investment consultant, any mitigation of this risk by maintaining two boards would appear to be minimal. Indeed, there is an argument that maintaining two boards poses its own risk in relation to the making of timely and necessary decisions in relation to diocesan investments.

18. Overall, we consider that the benefits of amalgamation outweigh any risk.

Amalgamation would prevent future differentiation of investment objectives

19. The ACPT states in its paper (at paragraph 13) that "An amalgamation would prevent the investment objectives and other characteristics of the LTPF and DE being differentiated in the future."

20. We respectfully disagree.

21. As mentioned in our initial paper (paragraph 6 of Attachment C), any divergence in the characteristics of the DE and LTPF in the future could be readily managed through the allocation of assets within an amalgamated fund or through separate direct holdings by either the LTPF or the DE.

22. In this way, the DE's and the LTPF's chosen strategic asset allocations (combining the amalgamated diocesan vehicle and other direct holdings of the DE and the LTPF respectively) would satisfy each respective trustee's separately determined risk appetite and investment objective requirements.

23. This matter is considered further in paragraphs 37 to 42 below.

ACPT assets should not be held by another trustee for investment purposes

24. The ACPT states in its paper (at paragraph 15) that "there would be no logical basis for the ACPT holding assets which, for example, happen to be real estate but if the real estate was sold and invested, for the proceeds then to be held and invested by a different trustee."

25. We respectfully disagree with this statement.

26. We point to the DCIF as an example of the assets of the ACPT already invested by a different trustee. If the long-term investment vehicle contemplated in our initial paper was established in a manner similar to the DCIF, it would not be necessary for either the ACPT or the GAB to relinquish their trusteeship of the interest in the invested funds.

27. We also point to the LTPF. Strictly speaking, whenever an ACPT client fund invests in the LTPF, the pooled investments are held and managed by the ACPT as trustee of multiple parish or other funds (i.e. in different legal capacities) with distinct fiduciary responsibilities.

Should a Diocesan Investment vehicle be formed using an expanded version of the LTPF or a new trust status for this purpose?

28. We do not have a strong view on whether an expanded LTPF or a new trust should be used for the purposes of a diocesan investment vehicle.

29. However, the comments we make in our initial paper (paragraphs 10-16 of Attachment C) suggest that if cost is the only relevant criteria, an expanded LTPF would be the appropriate choice, to efficiently make use of the existing unit-pricing structure.

Who should be the trustee of the Diocesan Investment vehicle and what skills are required of the members of the board of that trustee?

30. We deal with this question in our initial paper (paragraphs 17-33 of Attachment C) without expressing a concluded view. We want to draw particular attention to the consequences outlined in our initial paper of appointing either the GAB or the ACPT as trustee of a diocesan investment vehicle (see paragraphs 30-33).

31. We also want to make a clear distinction at this point between the corporate body that is best placed to be the trustee of a diocesan investment vehicle and the members of that body who are best placed to serve on its board. Our sense is that this distinction is sometimes overlooked when considering the question of corporate trusteeship.

32. In relation to the corporate body, we consider that the ACPT is not an appropriate body to be the trustee. We consider that the ACPT's responsibilities, which are already considerable and onerous, and the skills and experience of its members, should remain focused on its primary role as trustee of real property held for the purposes of parishes. Equally, the trustee of a diocesan investment vehicle and its members should be focused on overseeing the management of the liquid long-term investments of the Diocese and the liquid long-term investments held centrally on behalf of parishes, a small number of estates and other organisations.

33. Otherwise, we do not have a strong view as to whether the GAB or a new body corporate should act as trustee of a long-term diocesan investment vehicle.

34. On one hand, there would be some cost advantages in the GAB acting as trustee. Further, this would result in GAB fulfilling the role of trustee of both the long-term diocesan investment vehicle as well as its existing role as trustee of the short-term diocesan investment vehicle, namely the DCIF.

35. On the other hand, the primary reason to use a new body corporate as trustee of a long-term diocesan investment vehicle would be to avoid the conflict of interest that might be said to exist with the GAB atf DE investing in another GAB trust. However, as a similar situation of potential conflict already exists within the ACPT's current investment structure and with the GAB atf DE investing in the DCIF, this may not be a significant consideration. It is not uncommon in commercial contexts for the same entity to be trustee of multiple funds with cross holdings between the funds – the existing law already regulates the conflicts which can arise in such a situation, and, to the extent it is a concern then, legally, it can be further managed through appropriate provisions in the relevant constituting ordinances.

36. The skills required of the members of the board of the trustee of the diocesan investment vehicle would include oversight of investment management, governance of investment management, financial performance, risk and compliance oversight, investment business development, strategy, commercial investment experience, and dealing with third party service providers (asset consultants and investment accounting firms).

How should the different investment objectives be addressed?

37. Preliminary modelling undertaken by Mercer on the impact to both the LTPF and the DE if the liquid long-term investments were amalgamated shows that both would continue to fulfil their current individual investment policy requirements.

38. Since 2010, the only deviation of the investment objectives between the LTPF and the DE occurred in the period between May 2016 and September 2017, where the absolute difference was 0.50% p.a. This reflects a high degree of commonality between the investment objectives of the two funds in recent years. The long term nature of the two funds, together with future capital market assumptions and consistent spending requirements adopted (based on the advice of the same external investment consultant), suggests this commonality is likely to be maintained for the foreseeable future.

39. If in the future the investment objectives diverge, this could be addressed by changing the funds allocated to the diocesan investment vehicle and other investment options (namely the DCIF and direct illiquid investment holdings).

40. For example, if one investor wanted a more defensive portfolio, units would be redeemed from the diocesan investment vehicle and invested in the DCIF.

41. If another investor wanted more illiquidity, units would be redeemed from the diocesan investment vehicle and invested directly in an illiquid asset such as direct property.

42. The strategic asset allocation of the diocesan investment vehicle would not need to be changed to accommodate different investment objectives, but would be dealt with through each investor's individual mix of short and long-term investment products.

Should a diocesan investment vehicle be open to other diocesan and Anglican investors?

43. We deal with the possibility of opening a diocesan investment vehicle to other diocesan and Anglican investors in our initial paper (paragraphs 34-43 of Attachment C).

44. We consider it would be prudent to establish a diocesan investment vehicle in a manner which leaves open the possibility of adding other diocesan and Anglican investors.

45. However, we do not consider other investors should be contemplated at this time as a key matter in this decision process, and do not consider that the argument for amalgamating the DE and LTPF is dependent on other investors being added.

For and on behalf of the GAB

ROSS SMITH

Chair, Glebe Administration Board

23 January 2019