Trust Investment and Financial Management

Investment and financial management

Where a perpetual charitable trust is established by a gift to the University, the trust capital is invested by the University, and the net annual income of the trust is applied by the University for the purpose specified by the donor.

Investment pools

Recognising the University's role as the trustee of multiple perpetual charitable trusts, section 40 of the *University of Melbourne Act 2009* (Victoria) provides that the Council of the University may establish one or more investment pools for the collective investment of any trust funds held by or in the custody of the University.

With respect to trusts, there are two investments pools established by the University:

- the long-term investment pool; and
- the short-term investment pool.

For all trusts of which the University is the trustee:

- trust capital and trust income are invested in either or both of these investment pools; and
- at all times the accounting records and systems of the University record the
- capital and income relating to each separate trust, notwithstanding the pooling of trust capital and trust income as permitted by the *University of Melbourne Act 2009* (Victoria).

With respect to perpetual charitable trusts of which the University is the trustee, the key objectives of the University's investment policy are to preserve the real value of trust capital while achieving an appropriate level of annual income to finance the purpose specified by the donor.

Investment of trust capital

Trust capital is invested in the long-term investment pool, by way of the purchase of investment units in that pool.

Once each year the market value of all units in the long-term investment pool is calculated, with a corresponding adjustment to the value of each trust's investment in that pool.

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Thus, for each trust, the University invests trust capital to maximise capital growth, with the benefit of the economies of scale arising from the size and breadth of the University's long-term investment pool.

Protection against capital depreciation and years of reduced income

Section 41(2) of the *University of Melbourne Act 2009* (Victoria) permits the Council of the University from time to time to add some portion of income from an investment pool to the capital of the pool 'as a provision against capital depreciation or reduction in income'.

Thus the University is empowered to retain a portion of income as part of capital:

- in anticipation of years when income from an investment pool is reduced; and
- to guard against capital depreciation.

The University is empowered to adopt these protective investment mechanisms by the *University of Melbourne Act 2009* (Victoria).

Investment of trust income

Income from trust capital invested in the long-term investment pool which is available for distribution is paid into the short-term investment pool, where interest is derived for the benefit of the particular trust while that income remains in the short-term investment pool.

Net annual income

For most of the perpetual charitable trusts of which the University is the trustee, the trust terms permit only the expenditure of trust income for the purpose specified by the donor, meaning that the trust capital must be preserved.

At the University, the expression 'net annual income' is used to describe the trust income available each year for expenditure for the purpose specified by the donor.

How is Net Annual Income calculated?

The income of a trust of which the University is the trustee comes from two sources, and that income is held in the University's short-term investment pool:

- interest derived from trust income held in the short-term investment pool; and
- income derived from trust capital invested in the long-term investment pool.

Income from the long-term investment pool is capped at a figure set by the Council of the University from time to time; the current cap set by Council is 5.5% of the capital value of the fund. If in any year the income return from the long-term investment pool:

- is greater than 5.5%, then the portion of that income:
    - representing the 'first' 5.5% income return on capital is paid into the short-term investment pool for the benefit of the particular trust; and

  - over and above 5.5% (ie the 'excess' income) is returned to capital for the benefit of the particular trust as 'a provision against capital depreciation or reduction in income', as permitted by section 39 of the *Melbourne University Act 1958* (Victoria);
- is less than 5.5%, all of that income is paid into the short-term investment pool for the benefit of the particular trust.

As permitted by section 42 of the University, an administration fee is currently levied by the University on both the long-term investment pool distribution and the short-term interest income. For each trust of which the University is a trustee, the University deducts from the income of that trust a commission for the administration of the trust, being 2.5% of the income derived from:

- interest derived from trust income held in the short-term investment pool; and
- income derived from trust capital invested in the long-term investment pool.

In summary,

NET ANNUAL INCOME =

(1) Interest income from trusts held in the short term investment pool **PLUS**

(2) Income from the trust capital investment pool (currently set at a maximum of 5.5% of pool investment) **LESS**

(3) Commission for administration of trust funds (2.5% of 1 & 2 above)

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