Finance and Investment Report 2018

Summary

2018 was a difficult year in relation to the Society's finances. At an Informal Meeting with the membership in April 2018, Jon Levett, then CEO and the Honorary Treasurer presented details of the Society's financial situation and the need for a realistic financial strategy. This was in the context of an operational deficit in 2017 of £417k and a budgeted deficit for 2018 of £314.5k. Unfortunately, the development of a financial strategy was delayed due to the departure of Jon Levett in September 2018 and the retirement of Nick Childs, Finance Manager, in January 2019.

Significant longstanding difficulties in the finance department led to a major delay in the completion of the 2018 accounts and audit, so that unaudited figures were presented at the AGM in July 2019. The figures outlined below are based on the audited accounts and reveal an even more worrying financial situation than had been forecast, with an overall excess of spending over income of £537k.

In advance of these figures, the Board had begun to take urgent steps to remedy the situation. The appointment of a new CEO, Caroline Langley, in December 2018 and a new Head of Finance, Sam Duffy in January 2019 has enabled us to begin to take a better hold of the situation. Although reluctantly approving a deficit budget for 2019 of £429k the Board also set a target to achieve a balanced budget by the end of 2021. This has required the Board to approve £100k of savings in the current year already, with further projected savings in progress for 2019 and 2020. "Savings" in this context mean both reducing costs where possible but also developing new and established areas of income generation.

Overall position

Overall the Society made a loss in 2018 of £804,121 compared with a loss of £151,274 in 2017. This loss is made up of both an operating deficit (spending more money than comes in as income) and a loss on investments for the year. The total assets of the Society now stand at £9.0 million. Our assets comprise tangible fixed assets - the freehold of Byron House, the Mews leasehold, library and archives and fittings – and investments.

Total income for the year was £2,060,727 (2017:£2,457,931) and total expenditure was £2,597,826 (2017:£2,874,991). The operating deficit, i.e. the loss excluding investment gains/losses, was £537,099 (2017: £417,060). This is significantly worse than the budget approved for 2018. As was explained at the IM in June 2019 and the AGM in July 2019, this is an unsustainable situation for the future of the Society.

The overall **loss** on investments over 2018 was £267,022 (this included a small increase in the valuation of farm land) compared to a **gain** in investment in 2017 of £265,786.

Operational deficit

The operational deficit in 2018 includes a number of one-off costs, most significantly a sum of £147.7k in relation to the Revised Standard Edition (RSE). This was money that had been spent over preceding years, held as work in progress in the balance sheet, pending income from the RSE. This amount, together with spending on RSE in 2018, has now been expensed to the profit and loss. There were also one-off staff costs (redundancy, CEO recruitment etc.) totalling £95k and a loss on the IJP centenary conference in New York of £25k. This means the underlying deficit for 2018 – the excess of ongoing spending over ongoing income – was £270k. This is an unsustainable position.

Significant areas to note in relation to income include:

- PEP donation of £305k.
- Outstanding PEP royalties received in the year of £82k.
- Net income from the English Speaking Weekend Conference of £21k.

However we also saw decreases in income from IJP and membership subscriptions, both major sources of Society income.

Online education showed a significant increase in income from the previous year (£171k compared to £53k) but still made a loss overall of £53k. Outreach had a reduction in income from £163k last year to £129k, but also saw a significant reduction in costs (due in part to there being no Film Festival or Summer School) producing a small surplus of £3k compared to a deficit of £70k in 2017.

Investments

Total investments sold in 2018 were £73k, compared with £591k in 2017. Total investment income was £156k before fund management charges. These sums were used to make grants to areas of our charitable activity to fund general activities. The overall position is that the value of listed investments fell from £4,403,417 in 2017 to £4,034,296 in 2018.

As was discussed at the AGM in July 2019, we have been spending more money than we have coming in over a number of years and this has been funded by the sale of investments. As a consequence our capital funds are steadily reducing and our investment income, from a shrinking pot, is also reducing. If we continue spending and using capital in this way we will have used up all our capital in about 10 years.

Reserves

Free reserves are those funds within our overall reserves that could be utilised relatively quickly, rather than those which could not easily be converted to liquid funds such as our buildings. These are funds that are readily available to be used for any unforeseen expenditure that might arise, a sort of safety net in relation to the Society's financial risks. Free reserves decreased to £719k at the end of 2018, from £1,034k last year. Whilst this is within the target range set by the Board of £600-£800k this area needs to be monitored carefully.

General funds are those which do not have restrictions directing how they can be used, and are important as they can be used for general purposes such as increasing our working capital and cashflow position. Restricted funds can only be spent on activities that are in line with the specific purposes of the fund when it was established, for example as specified in a bequest. Our general funds reduced to £4,631k in 2018, from £5,080k the previous year. Restricted funds reduced to £3,880k from £4,264k.

The Innovation and Development Fund was established by the Board in 2014 for new projects and was used primarily for building work. At the end of 2018 this fund stood at £264K. We are planning to ask the Board to re-designate this fund to the general fund as there are unlikely to be new projects in the immediate future.

Investment Strategy

The majority of the Society's investments are managed by Sarasin & Partners. In March 2018 the funds were transferred into the new Sarasin Climate Active Endowments Fund.

The Climate Active Endowments Fund operates an ethical policy, as follows:

- No investment in companies with 5% or more of their turnover involved in the mining of thermal coal or tar sands;
- Following engagement, no investment in companies that needlessly emit significant quantities of carbon into the atmosphere, or which do not take seriously the transition to a low carbon economy;
- Qualitative judgements to be considered on a regular basis by the Climate Active Advisory Panel;
- Zero tolerance on tobacco production and manufacturing of tobacco related products; and
- No investment in companies that generate a significant turnover from the manufacture of arms, alcohol, gambling or pornography.

In order to prevent further erosion of our capital investments, the Board has approved an investment policy in 2019 as follows:

- spending from all investment funds (restricted and general) should not exceed 4% of the overall value of the funds, on an annual basis, including investment income, and

- any capital withdrawals of over 1% of total fund value per annum (excluding income as this is paid automatically) should only be made with the express approval of a majority of the Board, on the basis of a clear investment proposal with properly evidenced business plans.

Financial sustainability

It is clear that the future financial sustainability of the Society is at risk due to increased spending and decreased income in recent years. This has led to the use of capital to support ongoing spending without this being replenished. Investment in income generating activities, such as Online Education, has not proved as successful as we had hoped. The Board therefore has difficult decisions to make in order to bring the financial situation back into balance, and will need the support and cooperation of both staff and Membership in this process.

Thanks

I am grateful to Sam Duffy (Head of Finance) Patricia Vepuri (Assistant Accountant) and various temporary colleagues for all their hard work in managing the Society's finances during the year. Jana Pavlickova (Finance Administrator) also worked very hard for the Society before she took redundancy in August. We are in the process of recruiting a new full time accountant to provide additional expertise in the finance team. I am also grateful to Neil Loden, investment advisor, for his quiet persistence, patience and determination in helping us face financial reality. Finally, I am grateful to Caroline Langley and the Board for their support and energy in tackling these difficult financial decisions.

Elizabeth Coates Thümmel

Honorary Treasurer

17 October 2019