

## Investments and reserves

January 2023

### Our approach to investments and reserves

The work of the SRA is funded primarily from the annual collection of practising fees. This income is received at the start of the financial year in November and we manage that working capital effectively throughout the year to deliver an appropriate return and manage risks.

In addition, we maintain reserves to provide a contingency for potential reductions in income, unexpected liabilities, or to allow for planned increases in expenditure without making significant increases in practising fees.

In line with good corporate governance we seek to maintain the capital value of reserves within an acceptable level of risk. This is to ensure that the real value of these reserves is not eroded over time. We hold a proportion of our reserves in cash deposits with the larger proportion invested in a balanced portfolio and managed by an external investment manager.

We proactively look to ensure that we take account of environmental, social and governance (ESG) considerations in respect of our approach to investments. We work with our investment managers to ensure that we invest in responsible and sustainable investments wherever possible and look to exclude investments in fossil fuels, alcohol, pornography, armaments, tobacco, gambling and high interest rate lending.

The detailed approach to our investments and reserves is set out in our SRA investment and reserves policies. These are approved by the Board and reviewed on an annual basis to ensure that the approach towards both remains appropriate.

### SRA investment policy

#### Introduction

- Solicitors Regulation Authority Limited (SRA) is a private company limited by guarantee. The SRA is the regulator of solicitors in England and Wales.
- We have an annual income of c.£70m with an equivalent level of annual expenditure.
- This policy statement concerns working capital, medium term reserves held in cash and long-term reserves available for investment. These are summarised in this table:

What	Accessibility	Held as	Managed by
Working capital	In year as required in line with cashflow forecast	Cash – term deposits available in line with cashflow forecast	Externally managed service overseen by Executive Director of Resources and Director of Finance and Business Planning
Medium-term reserves (cash buffer)	As needed – available for unplanned immediate calls on reserves	Cash deposits including money market accounts – accessible within two months (or shorter subject to	Finance Department - overseen by Executive Director of Resources and Director of Finance and Business Planning



Long-term reserves (investments)	At least 7 year time horizon	interest penalties). Investments - no requirement for liquid holdings	Investment Management
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- Our reserves policy [last updated June 2022] is to hold £15.7m to £22.5m as reserves to ensure continued financial security and to provide for contingencies.
- We have approximately £14.5m of uncommitted reserves (at 30 April 2022). A proportion of reserves (between 5% and 15%) should be held in cash deposits with the remainder available for investment.
- Working capital is at its highest in November each year following the collection of practising fee income, reducing gradually throughout the financial year.
- Our financial objective is to at least maintain the real value of the reserves through a combination of investments which generate a return in excess of inflation and cash holdings where risk is kept to a minimum.
- Our Board is responsible for investment decisions. Investment management is delegated to an authorised professional investment manager, currently Cazenove Capital.

## Investment objective

- We seek to at least maintain the capital value of reserves within an acceptable level of risk.
- Our investment objective for the long-term reserves is to generate a return in excess of inflation over the long term. The long-term target for returns is inflation (as measured by the Consumer Prices Index) plus 3% net of any management fees.
- Our investment objective for the medium-term cash reserves and working capital is to minimise risk and obtain the best available returns within those risk constraints.
- Working capital should be readily available to meet known cash flow requirements as they fall due throughout the year.

## Risk

- We are reliant on practising fee income for its activities. Investment assets are held as reserves and not to supplement running costs.
- The key risk to our long-term reserves is inflation, and the assets should be invested to mitigate this risk over the long term. The Board understands that this is likely to mean that investment will be concentrated in real assets and that the capital value will fluctuate.
- The Board is able to tolerate volatility of the capital value of our financial investment portfolio, as we are able to meet its short-term operational activities and financial commitments through working capital.
- Our assets can be invested widely and should be diversified by asset class, and by security. Asset classes could include cash, bonds, equities, property, hedge funds, structured products, private equity, commodities and any other asset that is deemed suitable for us.
- The Board is charged with agreeing a suitable risk profile for the invested reserves with the investment manager.
- Short and medium-term cash deposits should be managed across at least two counterparties, with no less than 20% per institution.

## Liquidity requirements

- The long term invested reserves are not expected to be required at short notice and as such there is no specific requirement for short term capital liquidity within the investment portfolio.



- As part of a balanced portfolio however, it is expected that some asset classes will be relatively liquid.
- A proportion of our reserves (5% to 15%) are to be held in cash deposits mitigating the risk of any call on the invested reserves in the event of a short-term unforeseen cash requirement.
- We will draw down the working capital cash deposits in line with the planned expenditure schedule. Maturities of cash deposits should therefore match this timetable.

### **Time horizon**

- We expect to exist in perpetuity and investments should be managed to meet the investment objective and ensure this sustainability.
- We have divided our reserves into those that can be held for a long-term time horizon (at least seven years) and those that should be liquid in the shorter term.
- Working capital should be realisable in line with the planned expenditure schedule.

### **Ethical investment policy**

- Our assets should be invested in line with its role as a public service regulator. Individual investments may be excluded if perceived to conflict with our role. These would include, but are not limited to, direct investment in listed law firms and organisations with which we have a significant third-party relationship. A list of organisations (or types of organisations) will be provided annually.
- In addition, we will seek to invest in a broad ethical/sustainable portfolio within our current risk appetite.

### **Management, reporting and monitoring**

- We have appointed an investment management firm to manage the long-term assets on a discretionary basis in line with this policy. The investment manager is required to produce a valuation and performance report quarterly. We have nominated a list of authorised signatories, two of which are required to sign instructions to the investment manager.
- The Board has responsibility for agreeing strategy and monitoring the investment assets. The Board will receive a quarterly update on the portfolio, including an analysis of return, risk and asset allocation. Performance will be monitored against agreed market benchmarks, and against the investment objective of inflation plus 3% over the long term. The investment manager is required to present to the Board on at least an annual basis and by request on an exceptional basis.
- Working capital will be an externally managed service within the parameters established by this policy and overseen by the Executive Director of Resources. This may be the same investment management firm that is managing the long-term assets. Working capital funds may be held with counterparties with a credit rating no less than A3 (Moody's), A- (S&P) or A- (Fitch) with the exception of call monies (including overnight) which should be in line with the investment manager's policy.
- Medium-term cash reserves will be managed by the finance department, overseen by the Executive Director of Resources.
- The return on these cash reserves and working capital will be monitored against the Bank of England's SONIA interest rate benchmark.
- The Board will review the performance of the Investment manager on an annual basis and will consider retendering for an investment manager after three years. The Board may decide to delay retendering for up to two years. The maximum term without retendering for an investment manager is therefore five years.

### **Approval and review**

- This Investment Policy Statement was prepared by the Director of Finance on behalf of the Board of the SRA to provide a framework for the management of its investment assets. It will be reviewed on an annual basis to ensure continuing appropriateness.

**Approved by the SRA Board 7 June 2022**

Date of next review: June 2023

## **SRA reserves policy**

A reserves policy explains to existing and potential stakeholders why an organisation is holding a particular amount of reserves. A good reserves policy gives confidence to stakeholders that the organisation's finances are being properly managed and will also provide an indicator of future funding needs and its overall resilience.

### **Purpose**

The SRA regulates solicitors in England and Wales. Solicitors Regulation Authority Limited operates as a company limited by guarantee. The SRA does not trade and operates as a not-for-profit entity. As such this policy was developed with regard to the Charity Commission guidance on reserves.

Deciding the level of reserves that a company needs to hold is an important part of financial management and forward financial planning. All companies should develop a policy on reserves which establishes a level of reserves that is right for the company and clearly explains to its stakeholders why holding these reserves is necessary.

### **Background**

We are funded primarily from practising fee income collected from solicitors and law firms, with additional income from regulatory activities such as authorising firms to offer legal services. The level of practising fees is agreed annually by the Board, approved by the Legal Services Board and collected predominantly during October and November each year as part of an annual renewals exercise.

### **What are reserves**

Reserves are that part of a company's unrestricted funds that is freely available to spend on any of the company's objectives. The items that should be excluded from reserves are:

- Restricted funds which are not therefore freely available to spend on any purpose.
- Tangible fixed assets used to carry out the company's activities, such as land and buildings.
- Designated funds set aside to meet essential future spending, such as funding a project that could not be met from future income
- Commitments that have not been provided for as a liability in the accounts.

### **Restricted funds**

These are funds that can only be used for a particular purpose. The Solicitors Regulation Authority Limited is an eligible body in respect of the provision of education services, specifically in relation to the Solicitors Qualifying Examination. Any profit that might arise from the supplies of education and training is used solely for the continuation or improvement of such supplies.

Any such funds generated in this way are restricted funds and are not included within the level of reserves required by this policy.

## **General reserves policy**

In identifying an appropriate level of reserves for us to hold, the Board considered:

- Required reserves for potential reductions in income
- Required reserves for additional liabilities or commitments
- Risks of unexpected expenditure in relation to legal costs
- Planned increases in expenditure

This approach provides a target level of general reserves between £15.7m and £22.5m. This represents between three and five months' expenditure in 2021/22.

Consideration is given to levels of reserves when setting the annual practising fee requirement. The level of reserves is assessed against the policy with consideration given to whether any adjustment is necessary and over what time period to remain within the agreed policy.

## **Monitoring and review**

The policy is reviewed annually by the SRA Board.

The value of reserves is reviewed as part of regular budget monitoring and cash flow forecasting and reported to the board on a quarterly basis.

Our annual report includes details on the level of reserves held and any action to be taken to adjust those levels where they fall outside of the policy, given plans for future activities.

**Approved by the SRA Board 7 June 2022**

Date of next review: June 2023