INVESTMENT COMMITTEE

POLICY TITLE:	**(41) IMPACT INVESTMENTS**
Date of Adoption:	November 2018
Review Date:	November 2019
Version:	2.0
Authorised:	IC Minor / Board Material Change

1. OBJECTIVES

- To provide a framework to assist the Trust in the identification and evaluation of Impact Investments.
- To provide a framework for managing the Trust's Impact Investment portfolio.
- To provide guidance to applicants on the process and the criteria for Impact Investments.
- To ensure Impact Investments comply with applicable legislation.

The Board has agreed on the fundamental principles of this policy and has delegated responsibility for the implementation and monitoring and minor updating of this policy to the IC Committee.

This policy must be read in conjunction with other Trust policies.

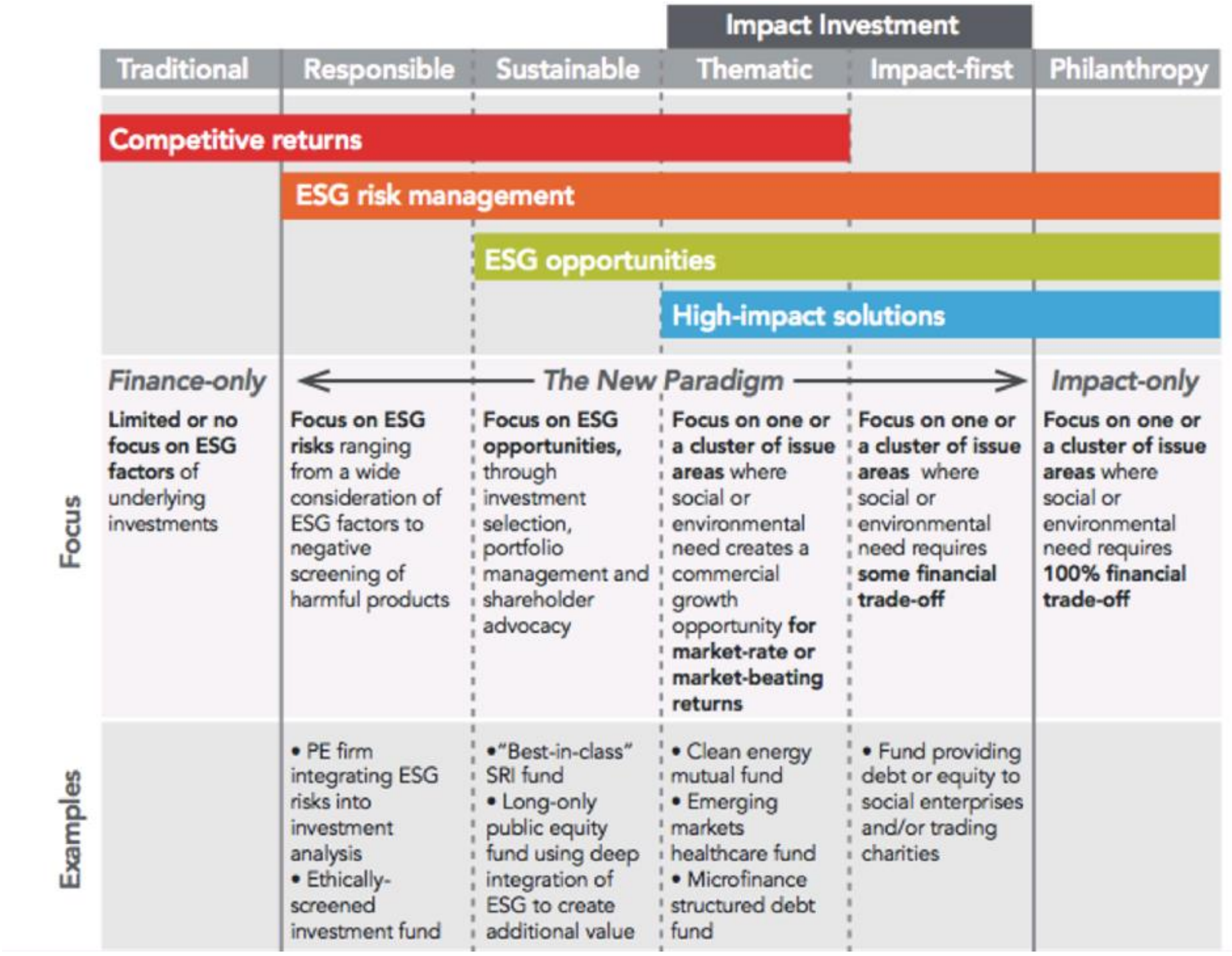
2. BACKGROUND

BayTrust operates a globally diversified investment portfolio with considerable assets that are held on behalf of the community. **The purpose of investing a portion of this portfolio in Impact Investments** is to increase the Trust's impact around its Mission without materially compromising its overall investment returns and in particular to address issues that granting is unable or ineffective in.

Impact Investments are included as part of the Trust's Strategic Asset Allocation (SAA) within the Trust's SIPO. This policy sits alongside the Trust's SIPO document and is referred to within the SIPO. The allocation to growth and defensive Impact Investments as a percentage of the total portfolio is outlined in the SIPO and is reviewed at regular intervals (along with the other asset classes) by the Trust and its Investment Advisors as part of its investment work plan. Further, the financial risk and return characteristics of the Trust's Impact Investments are included (to the extent that this is possible) as part of the Trust's regular SAA and SIPO discussion and review.

Impact Investments are defined as investments that seek both a financial return and a positive social or environmental impact.

The relationship between Traditional, Impact and ESG investing, is outlined in the diagram below:



BayTrust may encounter potential investment opportunities that straddle the line between a ***true*** impact first investment (where the impact is deliberate in its intention to achieve a measurable social/environmental impact) and an ESG investment that produces significant social good, but the primary intention is to produce a financial return. There are also some traditional investments that demonstrate impact. BayTrust will consider each potential investment opportunity that presents on its various merits, utilising a portfolio approach as outlined in this policy.

Definitions:

Impact Investments are investments made into companies, organisations, and funds with the intention to generate a measurable **Social Impact** alongside a **Financial** Return. Impact Investments may include (but are not limited to) direct ownership of property, public or private equity, loans, shares or investments in social enterprises, cash investments with a specific purpose, or guarantees.

Financial returns can include, but are not limited to: interest, dividends capital gains, or other monetary return.

Social Impact is defined as a measurable benefit(s) provided to the BOP community that aligns with BayTrust's Mission, Vision, Values and at least one of its Outcome areas.

3. IMPACT THESIS

Portfolio Mission:

Intentions

Through the Trust's **Impact Investment Portfolio,** BayTrust seeks to invest in organisations, ventures and entities that can demonstrate both a social impact and a financial return. The impact needs to be measurable and align with BayTrust's overall desired Outcome areas (or identified priorities), while the financial return will need to reflect the financial risk of the investment along with the social impact.

To help communicate the Trust's likely impact investing sectors, preference is for investments that can demonstrate impact within the Outcome areas of Healthy Sustainable Housing, Prosperous Communities and Improved Natural Environment, but other investments which impact on BayTrust Outcome areas may be considered.

To align with the Trust's Mission, Impact Investments are required to deliver their social impact principally in the Bay of Plenty ('BOP'), however there is also potential for BayTrust to invest in Impact Investments that provide impact outside the BOP region where the investment:

- Returns an appropriate risk adjusted market return;
- Can be seen to assist in the development of the Impact Investment eco-system within NZ;
- Has the potential for the impact to "trickle down" to BOP communities.

Motivation

BayTrust believes that Impact Investments offer a method to increase the impact to the BOP community in addition to our granting programmes. The Trust seeks to support, through investment, activities that address issues relevant to BOP communities and welcome's innovative approaches to complex social issues.

Mission, Vision and Values

The Trust's Mission, Vision and Values will all be reflected in any Impact Investment consideration.

The **Trust's Mission,** is widely defined in clause 4 of BayTrust's Deed as to 'benefit the community in the BOP'. This has been further refined through:

The Trust's Vision: Bay of Plenty is the greatest place to be

The Trust's Values:

- Kaitiaki (Guardianship) of our assets, our people and our environment
- Together we are strong
- We will make a real difference
- Innovative and balanced solutions produce the best results
- Everything we do, we do well

The Trust will also incorporate Environmental, Social and Governance (ESG) (as defined in the Trust's SIPO) considerations in its impact investment process.

4. PURPOSE

Portfolio Objectives:

BayTrust seeks an Impact Investment portfolio that will achieve increased impact in the BOP, help support and build the impact investing eco-system to attract new investment funds to increase the scale and impact of solutions to community issues whilst meeting its desired Impact Investment financial return and risk characteristics.

Recognition is given to the nature of BayTrust as a Community Trust deriving our initial corpus from community assets, and therefore it is necessary to serve the whole of the BOP population and to keep Outcome areas and targeted populations broad. While Impact Investments could seek impact in any of BayTrust's Outcome areas, they are most likely to be suitable for solutions in Healthy Sustainable Housing, Prosperous Communities and Improved Natural Environment Outcome areas.

Outcome Area	Target Population/Issue	Target Business Model	Target Impact
Healthy Sustainable Housing	✓ Those people / communities residing in sub-standard or inadequate housing.	✓ Supporting social, emergency and affordable housing developments	✓ Reduction in homelessness. Improved community health and wellbeing. Increased stability of families living in steady accommodation.
Prosperous Communities	✓ Deprived communities with high deprivation and low employment. Regions seeking to improve the quality of job offerings to its citizens.	✓ Inclusive Growth economic development opportunities that create sustainable employment opportunities for vulnerable sectors	✓ Improved standard of living, greater community cohesiveness, decreased inequity
Improved Natural Environment	✓ Natural assets – rivers, oceans, land that is at risk from pollution and damage	✓ Environmentally sound and productive agricultural/ horticultural or business models that seek to remedy damage or improve environmental outcomes	✓ Water quality improvement ✓ Increased pasture conversion to wetland ✓ Ha's land utilising reduced nitrogen methods
	✓ Climate change effects	✓ Innovative models that seek to reduce emissions or find alternative operating methods that are not environmentally damaging	✓ Reduced greenhouse gas emissions
	✓ Waste reduction	✓ Waste utilisation businesses	✓ Reduced waste to landfill

5. PORTFOLIO MANAGEMENT APPROACH

BayTrust will utilise a portfolio approach to managing its Impact Investment portfolio and assess potential new investments against the following portfolio targets:

- ***Target Social Impact for Impact Investment portfolio: Significant: >/ = to 4 on BayTrust's Impact Assessment Framework (see Appendix A).***
- ***Target Financial Return for Impact Investment portfolio: mid-point of NZ Treasury Risk Free Rate (currently 2.81%) and the BayTrust's long term net portfolio return target (currently 6.1%) = 4.5% - updated annually;***
- ***Target Financial Risk for Impact Investment portfolio: Risk of permanent loss of investment = Low as determined by BayTrust's Impact Investment Financial Risk Matrix (see Appendix B); and***

The portfolio management reflects the following principles:

Balance: Investments within the portfolio will endeavour to be balanced between those that return a below market return with high Social Impact (Concessionary Impact Investments) and those that have a lower Social Impact but provide a higher commercial return (Non-Concessionary Impact Investments). This will be done through modelling the Trust's current portfolio against the above three targets and also the effect the introduction of a potential new investment will have on the portfolio overall.

Risk tolerance: The Trust is prepared to accept that some Impact Investments will have a higher level of risk than the commercial investments the Trust holds, and there is less opportunity for diversification within the impact investment portfolio (due to size and limited availability of investment opportunities). At the same time, all effort will be made to assess, quantify and mitigate risks on individual investments. Risk will be managed further through diversification within the portfolio where possible, by considering investments across the geographic region, across sectors within the region and investment types.

Further Implications: When considering potential investments, consideration will be given to the suitable vehicle for holding ownership of the asset, implications on management and Trustee time in managing the investment and the complexity of the investment.

Impact Assessment and Management: To understand how Impact Investments are creating Impact, it is essential to attempt measurement of that impact. BayTrust will use the Impact Assessment Framework (see Appendix A) to identify and quantify the potential impact of an investment. This is supported by more granular assessment frameworks for each outcome area that the investment is targeting to determine the scale of the impact. BayTrust will move carefully and respectfully when attempting evaluation of impact, will continue to develop and refine its tools and investigate methodologies such as Social Return on Investment (SROI) as required.

Level of desired Financial Return: The desired gross financial return of the Trust's Impact Investment portfolio has been set at the midpoint between the Treasury risk free rate of ~2.81% (Sep 2018) and the Trust's current long-term net portfolio return objective of ~6.1% (June 2018). This desired return will maintain the portfolio long-term return objective based on the strategic asset allocation targets. This midpoint equates to a rate of ~**4.5%** and this rate will be reset in March each year as part of the Trust's budgeting process (unless a significant market correction/change occurs in the interim). The midpoint has been selected due to:

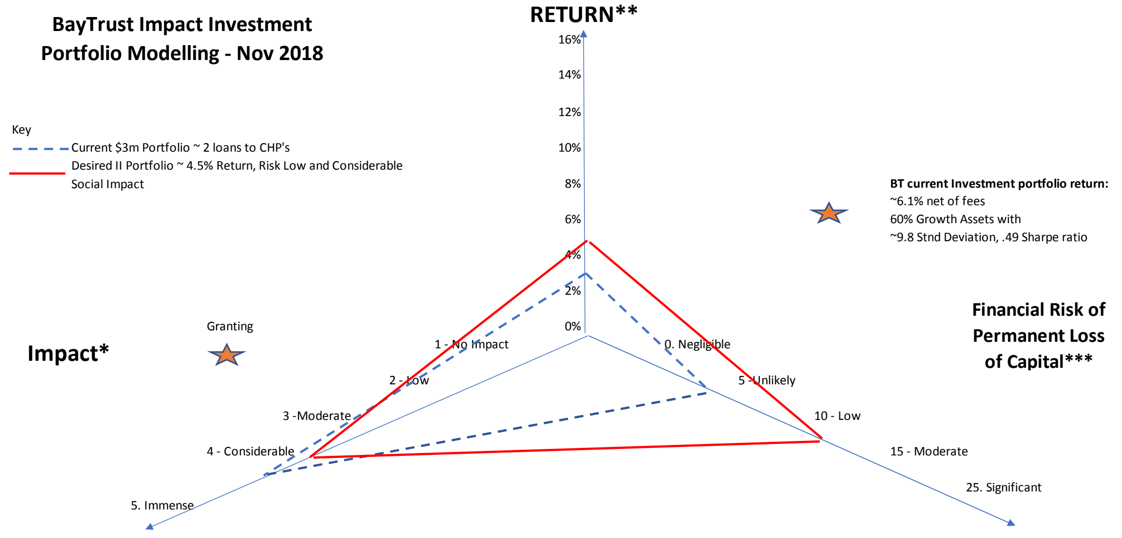
- Recognising the social impact, the portfolio will drive;
- Recognising that the overall risk is likely to be lower than our overall portfolio risk with most potential impact opportunities currently being evaluated in the low risk/defensive space;
- Recognising there will be limited (if any) ongoing fees.

Measurement and Level of desired Financial Risk: The key financial risk that the Trust is concerned about is the **permanent loss of investment capital associated with any one Impact Investment**. The Trust's **Impact Investment Financial Risk Matrix** (Appendix B) is used to quantify this risk, noting that there will always be elements of subjective analysis in coming up with an investment's overall risk rating. For example, we will need to access the ability of the organisation to execute its business model considering historical performance etc as well as any external, market, political or regulatory impacts that may disrupt the financial performance of the investment.

Note that the risk of the project not delivering on the social outcomes is contained in the social impact assessment rating, with reputation risk covered off as part of the due diligence on the impact investment.

The portfolio management approach is further illustrated as per the below:

i. Illustration of Current Portfolio v a Potential Desired Portfolio



* based on BayTrust Impact Assessment Tool

** Return includes target yield and target capital gain and is based on the 'most likely' financial scenario modelling

*** - See Below

Portfolio Modelling - Weighted Average Analysis

	Size $m	Risk	Return	Impact
Current				
TCHT	$1.50	4.0	3.50%	4.36
H4H	$1.50	4.0	3.50%	4.36
Total	**$ 3.00**	**4.0**	**3.5%**	**4.36**
Proposed				
Huakiwi				
Portfolio Impact				
Desired portfolio	**$12.00**	**10**	**4.5%**	**4.0**
Variance - Current	-75%	60%	-22%	9%
Variance - Proposed				

6. POLICY

The Trust will consider proposal requests (as well as actively seek out potential Impact Investments) including direct investment or direct ownership of assets that demonstrate alignment with the Portfolio Mission as stated above.

Due to the complexity involved in Impact Investments, generally only investments over $100,000 will be considered (with investments under $100,000 able to be considered where it is likely that grant funding may be unavailable/insufficient, the investment aligns well with the remainder of this policy and the Social Impact outweighs the investments complexity) and investments over $1m will be subject to due diligence by an independent advisor. Investments below $1m may be evaluated internally, or subject to due diligence by an independent advisor dependent on their complexity. In both cases, an appropriate level of quantitative and qualitative analysis should be conducted relative to the complexity, liquidity and risk associated with the proposed investment.

The Trust will consult with its own legal and accounting advisors on the appropriate agreements/documentation for each deal.

BayTrust may consider Impact Investments from or relating to: Non-profit or charitable groups, social businesses and formal groups/organisations/companies/partnerships or funds that align with the Trust's Impact Investment thesis.

The decision to proceed with any Impact Investment will be made in line with the Impact Investment portfolio management approach. Regard may also be given to a balance in regional spread, industry or sector, and type of Social Impact sought.

Generally, a single impact investment/organisation should not comprise greater than 1% of the Trust's Investment portfolio in order to be equitable to other potential impact investments and also to limit concentration risk.

The Trust will undertake a level of consideration and due diligence relative to the size, complexity and perceived risk of any investment. It is likely that an investment decision could take up to six to twelve months from the time of initial approach to commitment. Potential investees will be made aware of this time frame.

Impact Investment opportunities will be reviewed by staff through a two-stage process:

Stage 1 – Initial Scoping Assessment

Information to be provided by applicant:

1. A high-level summary of the potential investment, what field (industry, geographic region) it is in and what stage the project is at, what is the driver of the project or the need it is addressing.

2. Provide brief information on the organisation's capacity, history, management, financial position and governance structures.

3. What type of investment vehicle (ie limited liability company, JV, Limited Partnership) is being considered?

4. What are the investments proposed financial returns, how will this be calculated and paid to BayTrust as an investor?

5. What are the relevant timeframes, for project commencement, call on funds, payment of financial returns, and exit strategies?

6. What other investors have committed/are interested in this investment, and what stage are you at with discussions?

7. What are the social or environmental impacts envisaged from this investment (use the TOC format), how will they be measured and reported to investors.

Staff to assess:

1. The financial feasibility of the concept and existing financial position of the entity.

2. The social impact of the investment (utilising the impact assessment framework).

3. The financial risk of the investment (utilising the financial risk – impact investing matrix).

4. The impact on the Trust's impact investment portfolio (utilising the portfolio modelling tool).

5. Alignment with the Trust's impact investment Portfolio thesis.

6. Impact of the potential investment on the Impact Investment portfolio with regards to balance in regional spread, industry or sector, and type of Social Impact sought.

7. Suitability for completion of full due diligence stage and recommendation as to who needs to be involved in the DD process.

Recommendation will be made by staff as to suitability to move to next stage which will either be endorsed by the Trust's Investment Committee or the Trust Board, before proceeding to the next stage.

Stage 2 – Full Assessment

Requirements for next stage from Applicant:

Full business plan, Investment memorandum or proposal including (if applicable):

1. Full financial and cashflow projections/predictions including liquidity, investment returns, call for funds and exit options;

2. Feasibility study;

3. Full staff resumes;

4. Environmental impact report;

5. Property valuation;

6. Concept or architectural drawings;

7. Information pertaining to the industry within which the investment will sit;

8. Details of prospective partners, including the role they play within the community;

9. Risk analysis;

10. Any other information as deemed necessary to support the recommendation paper.

Staff to complete a summary of the investment including the below information:

1. Funds required, timeframes, financial returns;
2. Outcomes of full due diligence exercise (internal or external);
3. Analysis of ongoing management requirements including supervisory costs and directorships;
4. Full impact assessment;
5. Effect on the impact investment portfolio;
6. Recommendation to invest/not invest, weighing risk, return, impact and all other factors and where the investment would sit within the overall portfolio;
7. AML/CFT risk and compliance review (as per AML/CFT Compliance Manual).

7. IMPACT LOANS POLICY STATEMENT

Where the Impact Investment is made by way of a Loan, then the following will also apply:

Term: Loan terms will be at the discretion of Trustees and will generally follow standard commercial practice for similar loan types.

Interest Payable: Loans may be offered at the Trust's sole discretion on the following terms:

- Interest payable at such a rate as is agreed between the Trust and the applicant with the default rate being 1% above the Official Cash Rate, and with the rates to be reviewed at a minimum of every two years on the 1st of April;
- Interest may be charged on a straight-line basis, or a table mortgage arrangement may be used, with preference for table mortgage payments.
- Penalty rates in the event of default will be included and be comparable to market penalty rates for similar loans.

Principal Sum: The Trust will consider loans within prudent limits taking account of the organisation's ability to repay and the value of securable assets (where applicable); the organisation's other debt and its overall net asset position.

- The loan may be drawn down in instalments by agreement;
- The loan may be repaid using a table mortgage arrangement.

Security: Security is required as the Trust's first preference with a first charge by way of mortgage being the Trust's preference, but the Trust may also consider other appropriate agreements (ie a second mortgage or guarantees from related persons or entities) if a first charge is not available.

Repayments: Upon such terms as may be agreed with the applicant but normally by equal monthly instalments of principal and interest (where applicable) over the term of the loan. Quarterly or annual payments may also be considered.

The Trust may consider nil repayments during the term of a loan where full repayment at the end of the loan term is planned for and can be assured. Alternatively, the Trust may consider suspending payments for a period at the beginning or during, the life of the loan if such suspension is necessary to ensuring the success of the project and where it does not materially increase the Trust's investment risk.

Loan Costs: The Trust shall use its appointed Solicitors to prepare all security documents but may prepare in-house the appropriate loan agreement or acknowledgement of debt.

Legal Advice: Applicants will be advised to seek independent legal advice with such advice being at their own cost and contractually will be required to provide the Trust with assurance (by way of a BayTrust approved form) that they have not relied on BayTrust advice in relation to any potential investment.

Completion of documentation: Loan funding is to be released only after the loan documentation and securities (if required) have been completed by all parties.

Loan documentation. Loans can be approved by the CEO subject to a full business case being approved by Trustees and the Trust's Solicitors reviewing the loan documentation.

Loans Loss Reserve: The Trust will consider establishing a loans loss reserve (in conjunction with discussions with its Accountants and Auditors), to allow for potential losses on Impact loans, at a time in the future when the loans balance becomes significant enough (or bad debts high material enough) to warrant such reserve.

Compliance with Legislation: All relevant aspects of the Financial Service Providers (Registration and Dispute Resolution) Act 2008 and the Credit Contracts and Consumer Finance Act 2003, the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 and any other applicable legislation must be adhered to including full disclosure to all parties (see BayTrust's AML/CFT Compliance Manual for detailed compliance processes and procedures).

Financial Advice: Neither BayTrust nor any of its Trustees or employees can provide financial advice to the applicants on the Trust's Impact Loans, with the applicants being advised to seek their own independent financial advice. This term is to be documented in both the application form and the final loan agreement.

Administration: The Trust's Finance and Office Manager shall run a suitable diary system to ensure that all loan payments are made on time and may issue reminder notices one month in advance of any principal and/or interest repayments falling due when payments are made on an annual basis.

A **report** on loan balances, pending applications, repayments, and any other relevant matters including any risks associated with non-payment will be provided to Trustees on a quarterly basis.

8. REFERENCES

- Statement of Investment Policy and Objectives (SIPO)
- AML/CFT Compliance Manual
- Appendix A - BayTrust's Impact Investment Framework
- Appendix B - BayTrust's Financial Risk – Impact Investment Matrix

BayTrust Impact Investment Impact Assessment Framework Overview

WHAT?
Impact Value

- Relative importance of impact to the community, how critical is it? Addresses pertinent community or environmental issues?
- Alignment with BT Outcomes and Priorities and Impact Investment Priorities

HOW MUCH?
Impact Magnitude

- Is impact long-lasting or temporary?
- Is the impact small or does it have a significant effect on the lives of those targeted or the environment?
- What is the size of the targeted population? (% of local community, or BoP population)?
- How quickly is the major impact felt?

WHO?
Impact Beneficiaries

- Is impact directed at those in highest need?

CONTRIBUTION
Counterfactual Impacts

- What impact would occur without this intervention?

RISK?
Impact Risk

- Probability that outcomes do not lead to impact or outcomes to impact conversion
- Risk of negative unintended social or environmental consequences as an impact
- Are we enabling investees to generate impact that traditional capital markets would not support
- Risk alternative option is more efficient
- Catalytic or supportive?

BayTrust's Financial Risk – Impact Investment Matrix

Financial Risk of Permanent Loss of Investment Capital = Likelihood*Severity

Severity of Default Risk		1. Improbable	2. Remote	3. Occasional	4. Probable	5.Frequent
	5. Catastrophic	5	10	15	20	25
	4. Significant	4	8	12	16	20
	3. Moderate	3	6	9	12	15
	2. Low	2	4	6	8	10
	1. Negligible	1	2	3	4	5

Likelihood of Default Risk

Significant	Moderate	Low	Unlikely	Negligible

	Description		Capital Loss
Severity	5. Catastrophic		66%+
	4. Significant		33%-66%
	3. Moderate		10-33%
	2. Low		5-10%
	1. Negligible		0-5%

	Numerical:	Historical:
Likelihood	**5.** >1 in 5	Expected to occur in most circumstances
	4. 1 in 5 to 1 in 10	Will probably occur
	3.Occasional 1 in 10 to 1 in 100	Might occur at some time in the future
	2. Remote 1 in 100 to 1 in 1,000	Could occur but doubtful
	1. Improbabl 1 in 1,000 to 1 in 10,000	May occur but only in exceptional circumstances