

Ref: SWD/SL 101/3 II

Social Welfare Department  
29 July 2003

### **Lump Sum Grant Circular No. 8/2003**

#### **Guidelines for Non-governmental Organisations to Invest the Lump Sum Grant Reserves**

##### **Purpose**

The purpose of this circular is to provide guidelines for non-governmental organisations (NGO) operating on Lump Sum Grant (LSG) to invest their LSG Reserves.

##### **Background**

###### *Existing Rules*

2. In respect of LSG Reserves, paragraph 2.33 of LSG Manual Edition 2 stipulates that -

- (a) The level of cumulative Reserves (including interest but excluding PF reserve) at the financial year-end will be capped at 25% of the NGO's operating expenditure (excluding PF expenditure) for that year. Any amount above the cap needs to be refunded to the Government in the following financial year, unless the cap is raised by the Director of Social Welfare (DSW) upon application with justification from the NGO.
- (b) An amount of cash equivalent to the accumulated Reserve must be kept in a separate interest-bearing account with a bank licensed in Hong Kong.

The above prohibits NGOs from investing any surplus funds in their LSG Reserves other than in bank deposits.

### *LSG Reserves*

3. LSG has been implemented for over two years and as shown from the Annual Financial Reports submitted by NGOs, NGOs in general are accumulating rather significant sums in their LSG Reserves. In this regard, the Department has examined the existing rule to see whether we should allow NGOs to consider alternative investments other than bank deposits with a view to achieving a higher return.

4. In consultation with the Lump Sum Grant Steering Committee, the Department has decided to relax the existing rule to enable NGOs to invest sums in their LSG Reserves which are not immediately required according to the guidelines below.

### **Revised Investment Guidelines**

5. NGOs may consider investing surplus funds in their LSG Reserves based on the following investment framework -

<b>Type of Investment</b>	<b>Investment Criteria/Conditions</b>
a. HK dollar bank deposits: (i) Fixed deposit - one year or less  (ii) 24-hour call deposits	(1) Total value of deposits with any one bank shall not exceed \$500,000 or <b>25%</b> of the balance of the LSG Reserve prevailing at the time of investment, whichever is greater.  (2) The bank must be licensed under the Banking Ordinance, Cap. 155.  (3) Sufficient liquidity must be maintained to meet the use of LSG Reserve, including the required refund to the Government (see also para. 6 below).

Type of Investment	Investment Criteria/Conditions
<p>b. HK dollar bonds or certificates of deposits (CD):</p> <ul style="list-style-type: none"> <li>- short to medium term with a maturity period of one to five years</li> </ul>	<p>(1) Total value of bonds/CD shall not exceed <b>50%</b> of the balance of LSG Reserve prevailing at the time of investment.</p> <p>(2) Total value of bonds/CD/bank deposit with any one issuer shall not exceed <b>HK\$50 million</b>, or <b>50%</b> of the balance of LSG Reserve prevailing at the time of investment, whichever is the lower.</p> <p>(3) The credit rating of the issuer must not be lower than the rating of <b>A3</b> given by Moody's Investors Service Inc. or <b>A-</b> given by Standard &amp; Poor's Corporation.</p> <p>(4) Sufficient liquidity must be maintained to meet the use of LSG Reserve, including the required refund to the Government (see also para. 6 below).</p>

### Liquidity Constraints and Market Risks

6. Certificates of deposits and corporate bonds are rather illiquid in the secondary market. The bid/offer spread is usually wide and investors may experience difficulties if there is a need to liquidate the holdings prior to maturity. In addition, there are market risks involved in debt securities. If interest rate has gone up at the time when there is a need to liquidate the holdings, investors may experience a loss on the principal even after taking into consideration the interest element. When making investments, NGOs should pay special attention to such liquidity constraints and market risks and should make allowance for contingencies in projecting the use of the LSG Reserve.

## **Income from Investments**

7. LSG Reserve should be separately invested. Income derived from the investments must be fully and promptly credited to Interest Received in the Annual Financial Report (AFR) and form part of the LSG Reserve.

## **Control of Investments**

8. NGO Boards and Management Committee should, as part of their corporate governance, ensure that there are proper and effective internal procedures to control investments, which should cover the following aspects -

- clearly laid-down responsibilities and authorizations for decision making, transacting, recording and monitoring of investments;
- ensuring investments are made after careful financial planning to meet future uses of the LSG Reserve and to avoid undue loss from sale of investments prior to maturity;
- safe custody of investments with local licensed banks or their custodian subsidiaries;
- periodic reconciliation with the statements from banks and other parties concerned;
- keeping of proper accounting records for the transactions;
- attaching to the AFR submitted to the Finance Branch of SWD a schedule showing a breakdown of the Investment at the financial year-end (see the Annex). The schedule should be certified by the Chief Executive and the Chairman of the Board of the NGO. In case there is a difference between the total amount of LSG Reserve and investments, this should be clearly explained by way of Notes to be attached to the schedule;
- regular audit of the investment operation to ensure compliance of the investment guidelines and framework; and
- regular reviews of the investments and their returns.

## **Enquiries**

9. If you have any enquiries, please contact the responsible Liaison Officer of the Agency.

Social Welfare Department  
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Detailed Analysis of Bonds/Notes as at 31 March \_\_\_\_\_

Agency : \_\_\_\_\_

Investment in HK\$ Bonds/Notes

	Issuer	Nominal Amount HK\$	Cost of Acquisition HK\$ (Note)	Maturity Date	Coupon % p.a.	Effective Yield % p.a.	Credit Rating	Custodian Bank
1.		xx	xx					
2.		xx	xx					
3.		xx	xx					
4.		xx	xx					
	Total	xxx	CC					

Note: The amount will be reduced in accordance with the proportion of the disposal of the investment.