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# Guidance of the Public Guardian and Trustee: Charities and Social Investments April 9, 2018

The following Guidance is posted in accordance with permission from the Ontario Public Guardian and Trustee (“PGT”) and is current as of August 30, 2018. However, since the PGT may update this Guidance in the future without notice, charities should contact the PGT to obtain the most up to date version.

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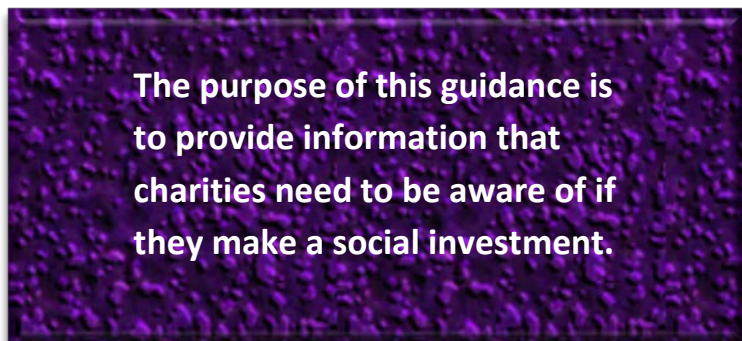
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## Charities and Social Investments

The Charities and Social Investments Guidance is intended to provide general information and is not intended to be a substitute for legal advice. For legal advice, charities should consult their legal advisor.



A social investment seeks to achieve both the charity's purposes and a financial return.

Charities can make social investments under sections 10.2 to 10.4 of the *Charities Accounting Act*.

The provisions are designed to facilitate social investing by giving charities flexibility to invest funds in ways that allow them to further their charitable purposes. For example, joint projects, revenue participation, non-collateralized loans or other financial structures could be available to charities.

Ordinarily when a charity makes an investment, it must comply with the prudent investor rules under the *Trustee Act*. When a charity makes a social investment, the prudent investor rules are replaced with new statutory duties under the *Charities Account Act* which are discussed below.

Sections 27 to 29 of the *Trustee Act* contain the prudent investor rules. Most of these provisions do not apply to social investments, with the exception of subsections 27 (3) and (4).

- Subsection 27 (3) authorizes charities to invest in mutual funds, pooled funds or segregated funds under variable insurance contracts. For instance,

a charity may pool their funds with other charities when making a social investment.

- Subsection 27 (4) authorizes charities that hold funds with a trust corporation as co-trustees to invest in a common trust fund that is maintained by the trust corporation.

When a charity is considering making a social investment it should decide whether the investment would be appropriate based on its charitable purposes and assets, the rules and duties that apply to social investing, the specific provisions of the charity's governing documents<sup>1</sup> and a director's or trustee's general fiduciary obligations.

If the charity is registered with the Canada Revenue Agency (CRA), it should also consider how CRA will view the investment. (see Canada Revenue Agency, page 8)

Social investing is available to charities regardless of how or when they were created. Charities established outside of Ontario or that have been federally incorporated may also be able to use the provisions if they are subject to Ontario jurisdiction.

## **What is a Social Investment?**

A social investment means using a charity's funds to directly further its purposes and achieve a financial return. Social investments fall on a continuum ranging between charitable expenditures at one end and purely conventional investments at the other.

A 'financial return' is defined as achieving an outcome that is better for the charity in financial terms than expending all of the property that was invested. A

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<sup>1</sup> Generally speaking, the governing document for a charitable trust is its deed of trust; for an unincorporated charitable organization, its constitution; and for an incorporated charity, its articles of incorporation, letters patent or the Act that established it.

'financial return' is not required to be at market rates and depending on the terms of the investment, may not require a re-payment of the investment capital.

For example, a charity aimed at helping the poor is considering making a loan to another charity to help build apartments for the poor. Only a small part of the loan would be re-paid and no revenue would be generated. As the outcome would be better for the charity in financial terms than having spent all of the funds, the charity would be considered to have received a financial return.

## Potential Restrictions on Social Investments

A charity's ability to make social investments may be restricted or excluded by the terms of its governing documents. If the governing documents expressly prohibit social investing, the charity may not undertake a social investment.

In some cases, a charity's governing document may stipulate how the charity is to invest its funds. For example, many charities incorporated in Ontario have a special provision that requires the organization to invest its funds pursuant to the *Trustee Act*. Restrictions or directions on how a charity is to invest its funds only apply to its conventional investments. These general restrictions do not apply to social investments because, under section 10.2(5) of the *Charities Accounting Act*, a social investment is not regarded as an investment for any other purpose.

Typically, foundations in Ontario have the following standard charitable purpose clause:

To receive and maintain a fund or funds and to apply all or part of the principal and income therefrom, from time to time, to charitable organizations that are also registered charities under the *Income Tax Act* (Canada).

Foundations operating with this clause only are not limited to funding a particular purpose or named charity. If a foundation that is a registered charity is not required to apply its funds to a particular charitable purpose or benefit a named charity, it can undertake social investments that directly further any charitable

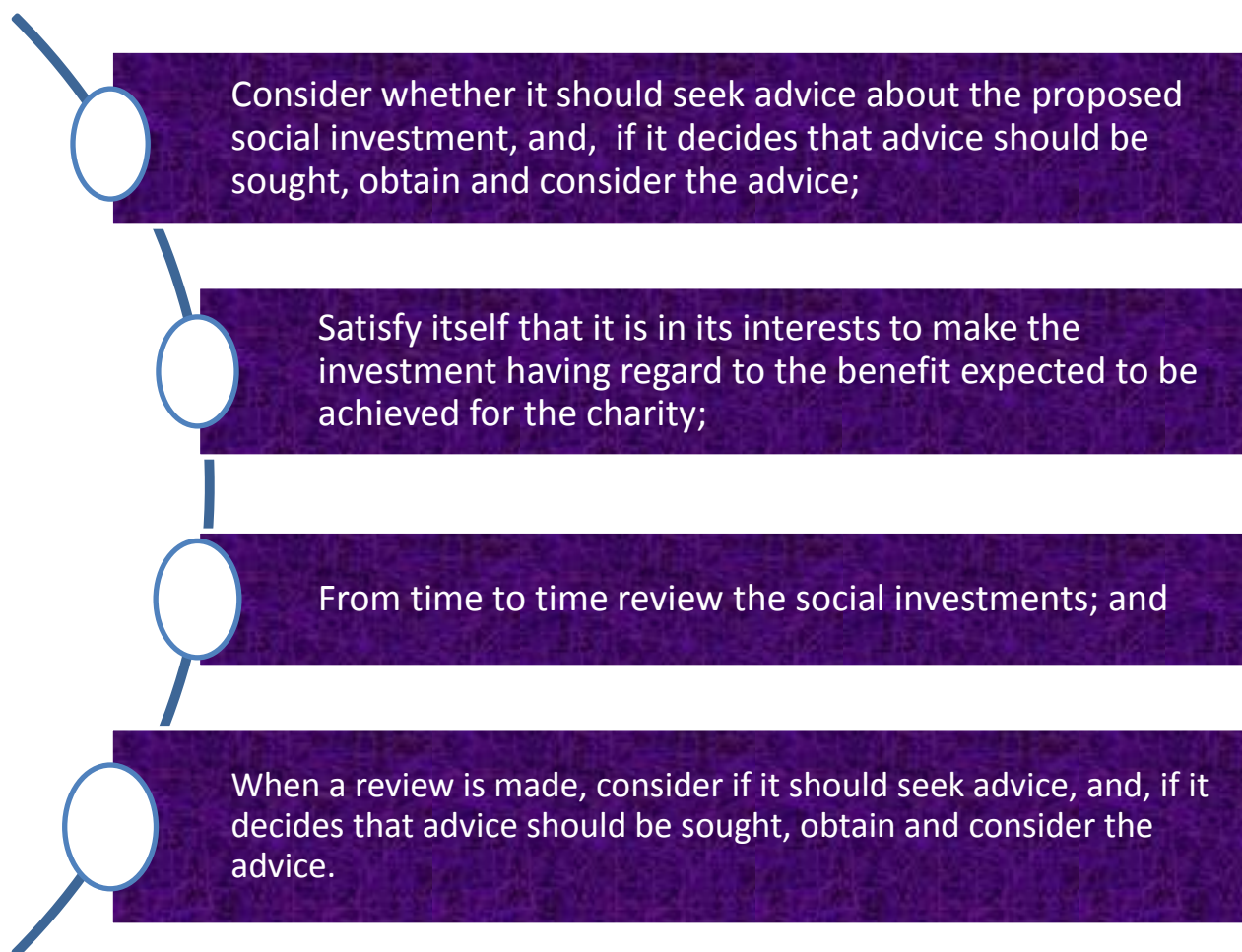
purpose as long as the recipients of the investment are registered charities under the *Income Tax Act* (Canada).

If a charitable organization which includes a foundation, is a registered charity established to benefit a particular purpose or a named charity, then the particular purpose or named charity must benefit from the social investment and the recipients of the investment must be registered charities under the *Income Tax Act* (Canada).

## **Statutory Duties**

### **(i) Specific Duties**

Before making a social investment, a charity must comply with the following statutory duties:



These statutory duties cannot be restricted or excluded by a charity's governing documents.

## **(ii) Seeking Advice**

Directors and trustees have a duty to consider if advice should be sought each time they consider a possible social investment.

When considering whether to seek advice, it is suggested that the charity review the following factors among others: the amount of risk involved; the impact on the charity if the social investment fails; the experience of the board members; the complexity of the proposed investment; the impact on the charity's reputation; and the effect on the charity's charitable registration, if applicable.

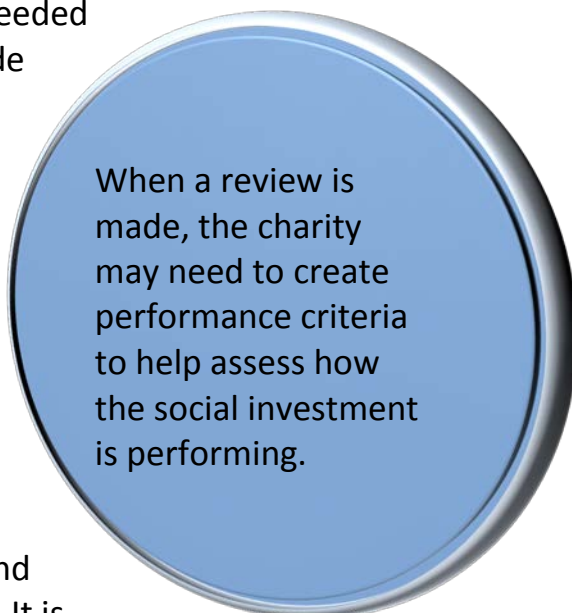
If the charity concludes that advice should be obtained, then the charity must obtain and consider the advice.

The charity should consider what kind of advice is needed and what professionals may be competent to provide such advice. It may be appropriate to consider whether advice should be sought from a lawyer, accountant, or other professional.

While the legislation does not require the advice to be in writing, it would be good practice to document any advice received.

Charities are required to review the social investments from time to time. How often a social investment should be reviewed is within the discretion of the directors or trustees and will depend upon the unique features of each social investment. It is suggested that the higher the degree of risk that attaches to a social investment, the more often the social investment should be reviewed.

A review of the social investment also requires that the charity consider if advice should be obtained. If a charity decides to obtain advice at this stage, then it must obtain and consider the advice.



When a review is made, the charity may need to create performance criteria to help assess how the social investment is performing.

### **(iii) Whether the Social Investment is in the Interests of the Charity**

Fundamentally, charities should make sure they understand and are comfortable with all aspects of the transaction. They may need to dig deeper, test assumptions

and ask questions about anything they don't understand. Some factors that might be considered are:

### **Information**

- Does the charity have adequate information to enable the directors or trustees to make an informed decision? Is there relevant information that needs to be obtained?
- Are any assumptions that have been made reasonable and based on reliable information?
- If the charity decides to obtain advice, does the advisor have the relevant expertise?

### **Financial**

- Would the social investment affect the charity's ability to carry out its current operations and fit within the charity's overall charitable activities and investment portfolio?
- Would the social investment fit within the short and long terms plans of the charity?
- Are the risks associated with the investment commensurate with the positive impact the charity hopes to achieve? Such risks could include: The number of factors beyond the charity's control; The amount of its funds that are at risk relative to the total assets of the charity; The impact on the charity should the investment fail or underperform;
- Will the costs of making the social investment impact the charity? These could include legal and financial costs; the possible loss of revenue compared to investing in a traditional investment; and possible income tax consequences;

### **Safeguards**

- Are the risks associated with the investment substantial enough that the charity should consider putting safeguards in place to protect the investment?
- Can the investment be terminated on reasonable terms in the event the investment is no longer used to further the charity's purposes?
- Should the charity request up-dates on the investment throughout the investment period? If so, how often?
- Consider the period of time that the charity's funds would be locked-up and whether the funds may be withdrawn at a particular time; could this create cash flow problems? If so, what safeguards could alleviate the potential problem?

### **Reputation**



- Would the investment fit within the expectations of donors to the charity and users of the charity's services?

Social investing will not necessarily be in off-the-shelf investments and assessing risk, liquidity and social return may be difficult. Therefore, depending on the complexity of the social investment and amount involved, it may be appropriate for charities to have a written plan.

## **General Fiduciary Obligations**

The social investment provisions do not relieve directors and trustees of their general fiduciary obligations to the charity.

Directors and trustees must handle the charity's property with the care, skill and diligence that a prudent person would use. They must act in the best interests of the charity and treat the charity's property the way a careful person would treat their own property. They must always protect the charity's property from undue risk of loss and ensure that no excessive administrative expenses are incurred.

At their core, fiduciary obligations require that directors and trustees act honestly, in good faith and avoid situations where their personal interests conflict with their duties to the charity or to other parties. Charities must be careful that a member of their board does not have a personal interest in the business in which the charity is investing.

As directors or trustee are responsible for carrying out the charitable purposes, they should also oversee the decision to make the social investment and the monitoring of the investment.

For more information about fiduciary obligations, please see the Public Guardian and Trustees guidance, [Duties, Responsibilities and Powers of Directors and Trustees of Charities](#), which can be found at

<https://www.attorneygeneral.jus.gov.on.ca/english/family/pgt/charbullet/bullet3.php>

## Permanent Endowment Funds

Charities sometimes hold funds on which donors have placed restrictions on the distribution of the principal or capital. In most of these cases, only the income earned by the fund may be expended on the charitable purposes. These funds are sometimes known as permanent endowment funds or perpetual charitable trusts, as the principal or capital of the fund is required to be held permanently by the charity.

Permanent endowment funds that restrict the expenditure of capital can be invested in social investments if: (i) The charity expects that the capital will be returned to the charity; or (ii) The document that created the endowment allows for such an investment.

## Canada Revenue Agency

The Canada Revenue Agency does not recognize ‘social investments’ as a separate category of investment. Therefore, registered charity’s making social investments must comply with both the provisions of the *Charities Accounting Act* and any CRA requirements that apply to the investment. Such requirements will differ based on whether CRA views the investment as a conventional investment, Program Related Investment (PRI) or program expenditure.

Many social investments may be viewed by CRA as a PRI, however, this is not necessarily the case for every social investment. It is recommended that registered charities that want to set up a social investment review CRA’s requirements to ensure that the proposed investment qualifies either as a PRI, program expenditure or conventional investment.

For more information about PRIs, please contact CRA directly:

**By telephone:**  
1-800-267-2384

**By TTY service for people with a hearing or speech impairment:**

1-800-665-0354

**By mail:**

Charities Directorate  
Canada Revenue Agency  
Ottawa ON K1A 0L5

<https://www.canada.ca/en/services/taxes/charities.html>

**Further Information**

For the most recent version of this Guidance, or for more information on charitable matters in Ontario, please visit the OPGT's webpage at:

<https://www.attorneygeneral.jus.gov.on.ca/english/family/pgt/charities/>

You can also contact the Charitable Property Program of the Office of the Public Guardian and Trustee directly at:

**Charitable Property Program**

595 Bay Street, Suite 800, Toronto, ON, M5G 2M6

Tel.: (416) 326-1963 (please leave a message)

Toll-free: 1-800-366-0335 and then press 1, 3, 7

Fax: (416) 326-1969

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