"Revised Investment Powers for Charities Under the Trustee Act: Delegation and Investment Policies"

> Not-For-Profit Board Management for Turbulent Times "Where do we go from here?"

Tuesday June 18th , 2002

Terrance S. Carter

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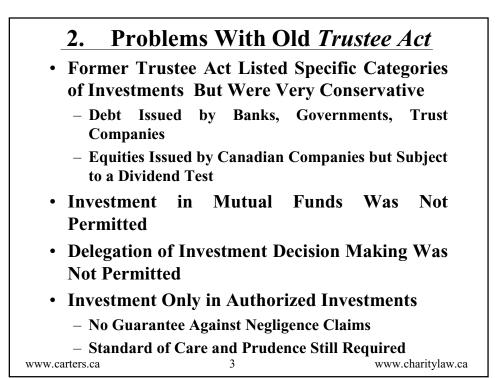


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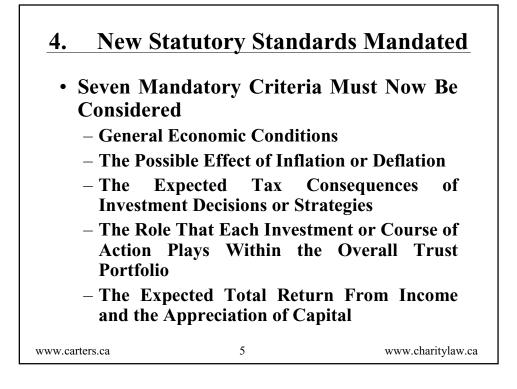
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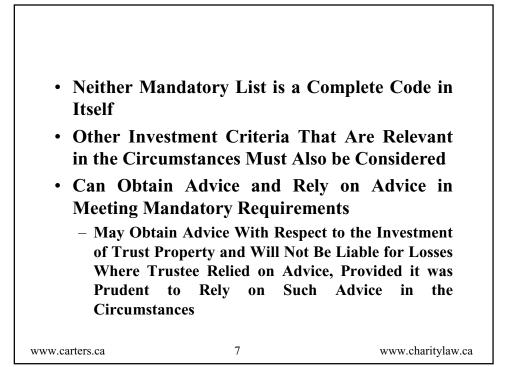
Application of *Trustee Act* to Charities 1. Charitable Corporations and Charitable Trusts Are Deemed to Be Trustees For Purposes of the Trustee Act • Property That is Subject to Special Purpose **Trust Is Trust Property Under the Trustee Act** • Special Purpose Trust in a Testamentary Gift or a Gift Agreement May Establish Different Terms of Investment Powers From the Trustee Act Trustee Act Will Not Apply If There Is Specific Investment Power Set Out in a Statute **Creating the Charity** 2 www.charitylaw.ca www.carters.ca



New Prudent Investor Rule 3. • Effective July 1, 1999 – Prudent Investor Rule **Replaced "Legal List" Authorized Investments** - "A Trustee May Invest Trust Property in Any Form of Property in Which a Prudent Investor Might Invest" • No Restrictions on Type of Investments • Standard of Care Required - The Care, Skill, Diligence and Judgment That a Prudent Investor Would Exercise in Making Investments Investing in Mutual Funds Now Permitted - But No Definition of Mutual Funds Investing in Pooled Funds Now Permitted - But No Definition of Pooled Funds 4 www.charitylaw.ca www.carters.ca



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5. Previous "Catch 22" Situation in Delegation

- Amendments to the *Trustee Act* Enacted on July 1, 1999 Did Not Provide the Authority to Delegate Investment Decision Making to Qualified Investment Managers
- This Created a "Catch 22" Situation for Many Charities
- Charities Had to Satisfy the "Prudent Investor" Rule in Investment Decision Making but Were Not Able to Delegate the Necessary Day-to-day Decision Making to Qualified Investment Professionals

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- This Situation Was Contrary to What One Would Expect of a "Prudent Investor" Who Did Not Have the Sophistication Necessary To Make Daily Investment Decisions
- If a Charity Continued to Delegate Investment Decision Making, the Charity and Its Board of Directors Ran the Risk of Being Found in a Breach of Trust for Having Undertaken an Unauthorized Delegation of Investment Decision Making

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- At the Same Time, If the Board of Directors Did Not Use the Services of a Qualified Investment Manager, It Ran the Risk of Being Found in Breach of the New Statutory Requirement to Exercise the Standard of Care Expected of a Prudent Investor
- Charities and Their Board of Directors Were Left in an Untenable Situation.

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6. Delegation Now Permitted

- Bill 57, Given Royal Assent on June 29th, 2001, Was the Result of an Initiative Taken by the Ontario Bar Association to Amend the *Trustee Act* to Authorize Current Practice of Delegation
- Bill 57 Now Permits a Board of Directors of a Charity As Trustees to Delegate Investment Decision Making to the Same Extent That a Prudent Investor Could

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Bill 57 Permits Trustees of a Charity (i.e. Its Board of Directors) to Delegate Investment Decision Making to a Qualified Investment Manager
The Mandatory Statutory Requirements of Bill 57 for Delegation Must Be Carefully Reviewed and Complied With
This Is in Addition to the Existing Right to Delegate Through Mutual Funds

7. The Requirements in Order to Delegate Investment Decision Making

INVESTMENT PLAN

- Cannot Delegate Without an Investment Plan in Place
- Investment Plan Is Otherwise Optional but is Recommended in Any Event
- The Investment Plan Must Set Out a Strategy for the Investment of the Trust Property, Comprising Reasonable Assessments of Risk and Return, That a Prudent Investor Would Adopt Under Comparable Circumstances

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The Investment Plan Must Be in Writing and Must Take Into Account the Seven (7) Mandatory Investment Criteria And The Mandatory Requirement to Diversify
Need to Be Careful That Description of Board Duties in Investment Plan Does Not Increase Liability for Directors
May Need to Have Different Investment Plans for Different Funds
Legal Counsel Should Review Investment Plan

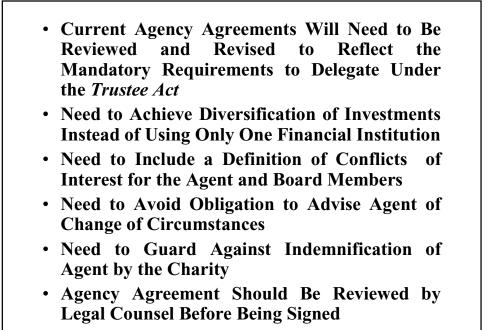
BEST INTEREST OF THE BENEFICIARIES

- The Trustee Must Be Satisfied That the Investment Plan Is Intended to Ensure That the Functions Will Be Exercised in the Best Interest of the Beneficiaries of the Trust
- i.e. The Investment Plan Must Be in the Best Interest of the Applicable Charitable Purposes of the Charity As Opposed to the Donor or Any Other Party

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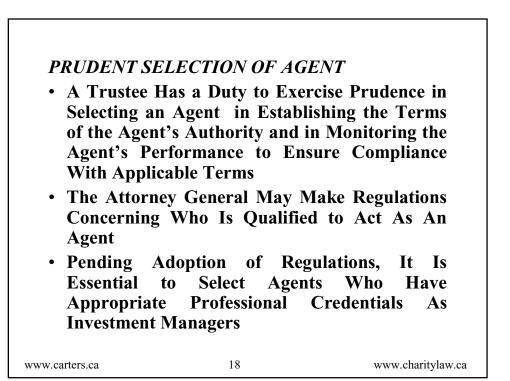
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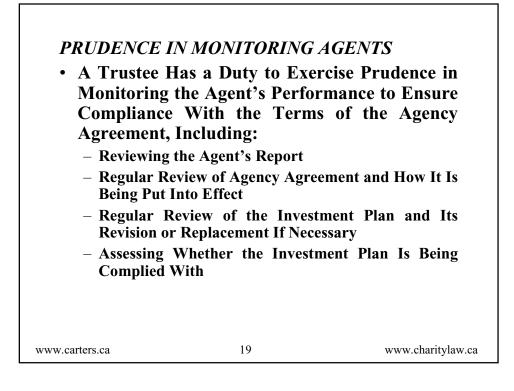
AGENCY AGREEMENT • The Trustee Must Have a Written Agreement Between the Trustee and the Agent (i.e. An **Agency Agreement**) • The Agency Agreement Must Include - A Requirement That the Agent Comply With the Investment Plan in Place From Time to Time; And - A Requirement That the Agent Report to the **Trustee at Regularly Stated Intervals** • In the Event That the Charity Develops a **Delegation Plan Separate From the Investment** Plan, Then the Agency Agreement Would Also Need to Require the Agent to Comply With the **Terms of the Delegation Plan** 16 www.charitylaw.ca www.carters.ca

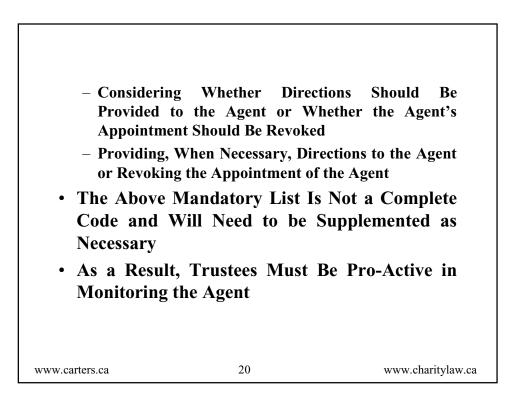


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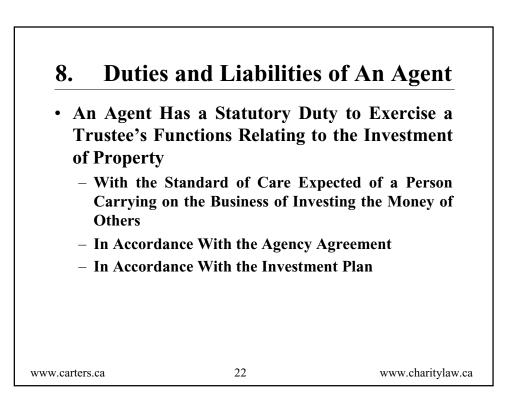
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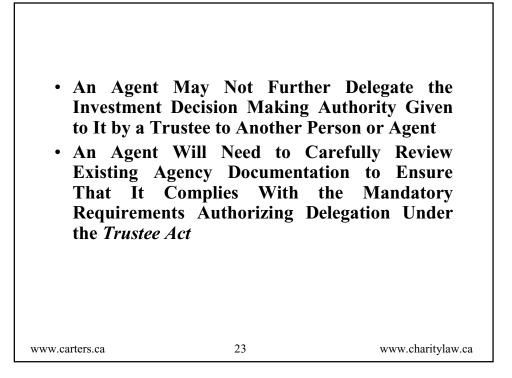


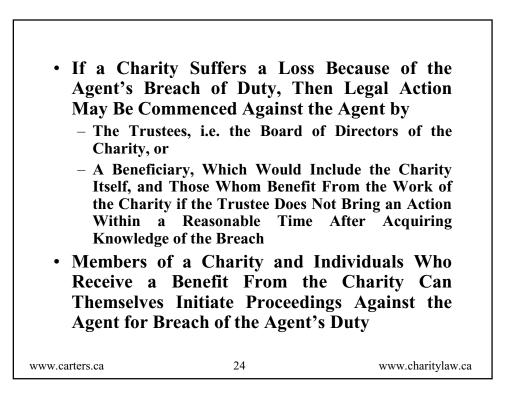












9. Liability of Trustees

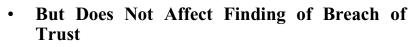
- Relief From Technical Breaches of Trust Under the *Trustee Act* Is Not Available for Losses Resulting From Investment of Trust Property
- The *Trustee Act* Provides That a Trustee Will Not Be Liable for Losses From the Investment of Trust Property If the Conduct That Lead to the Loss Conformed to an Investment Plan That a Prudent Investor Would Adopt Under Comparable Circumstances

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• Failure Comply With **Mandatory** to **Requirements for Delegation Will Preclude** Liability Protection Under the Trustee Act and Will Expose Trustees to Liability for Breach of Trust for Unauthorized Delegation of **Investment Decision Making** • Anti-netting Rule Does Not Apply to the **Calculation of Damages for Investment Losses** • Insurers for the Charity Should Be Consulted to Determine If Directors' and Officers' Insurance Covers Trustees' Liability From **Investment Losses**

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- **Damages Include Not Only Losses but Income** • **That Might Have Been Earned**
- Other Areas of Exposure to Liability for • **Trustees Relating to Investments**
 - The Income Tax Act in relation to permitted investments
 - The Charitable Gifts Act Prevents a Charity, Other Than a Religious Organization, From Owning More Than 10% of Any Business
 - The Charities Accounting Act Prevents a Charity, Other Than a Religious Organization, From Holding Land Not Required for Its Charitable Purposes, Such As Investment Property, for More Than Three Years 27

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- Special Purpose Funds, Like Endowment Funds, Must Be Invested Separately From the General **Funds of a Charity**
- Co-mingling of **Special Purpose** Funds for Investment Purposes Must Comply With the Stringent Accounting Requirements Pursuant to the New Regulations Under the Charities Accounting Act (See Charity Law Bulletin No. 4 at www.charitylaw.ca)
- A Charity Incorporated Under the Ontario Corporations Act Is Required to Prepare Annual Audited Financial Statements, Which Should Detail the Investments of the Charity

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10. Reducing the Risk of Exposure to Liability For Investments

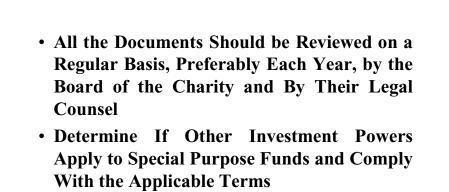
- Determine What Investment Powers Apply to the Charity and in Which Jurisdiction
- Consider Taking the Appropriate Corporate Steps to Have the Charity Come Under the Investment Power Regime of the *Trustee Act*, if Necessary
- Consider Amending Corporate Powers in Letters Patent to Include Powers to Sub-Delegate Investment Making Decision Making

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• Take Proactive Steps to Comply With Statutory **Requirements of the Trustee Act** • Establish and Implement an Investment Plan • Establish Specific Investment Plans for Separate Funds • Where Investment Decision Making Is Delegated, Then Establish and Implement a Delegation Plan and an Agency Agreement • Investment Plan Should Focus on Meeting Statutory **Requirements of Trustees Which Would Override** Contrary Provisions of an Investment Plan **Prepared by an Investment Manager** • Cross Reference Investment Plan to Disbursement **Policy of the Charity** www.carters.ca 30 www.charitylaw.ca



• Obtain Assistance From an Investment or Finance Committee of the Charity but **Require the Committee to Be Accountable Back to the Trustees**

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