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PITFALLS IN DRAFTING GIFT AGREEMENTS

By Terrance S. Carter, B.A., LL.B., TEP, Trade-mark Agent

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OVERVIEW

- Why is a Gift Agreement Necessary Anyway?
- Why Do Things Go Wrong with Gift Agreements?
- Gift Agreements Involve Donor Restrictions
- Twelve Common Drafting Pitfalls to Avoid

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A. WHY IS A GIFT AGREEMENT NECESSARY ANYWAY?

1. Basic Considerations

- Starting Point: A gift agreement is not a legal requirement in order to make a gift
- To establish a gift at common law simply involves the voluntary transfer of property without consideration
- However a gift agreement provides evidence that there has been (or will be) a gratuitous transfer of property to a charity intended as a gift
- As such, a gift agreement can help to avoid confusion at a later time concerning whether there was a gift and what the terms of the gift were

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2. Some Common Examples of When a Gift Agreement Is Used:

- Imposing a time or use restriction (explained below)
- Establishing naming rights in favor of the donor (explained below)
- Requiring special treatment with a gift in kind (i.e. restrictions on alienation of shares)
- Imposing special investment restrictions
- Recording a “pledge” for either a gift in the future or additional contributions to an existing gift

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3. Understanding The Difference Between a Gift Agreement and a Pledge Agreement

- A gift agreement provides documented evidence of a gift having been made by a donor to a charity and is legally enforceable on the charity when the gift involves restrictions
- A pledge agreement, on the other hand is an agreement that records a commitment by a donor to make a gift at a future time
- The terms "Gift Agreement" and "Pledge Agreement" are often used interchangeably, particularly when a gift agreement for a current gift includes a pledge to make a future contribution

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- A pledge agreement is generally not enforceable at law unless:
  - There is some type of consideration, even a nominal amount of two dollars (It may be possible that (i) naming rights or (ii) the charity agreeing to a project or a restriction may constitute sufficient consideration);
  - The charity can establish that it has acted to it's detriment as a result of the pledge (i.e. detrimental reliance); or
  - The pledge falls within the provisions of "Public Subscription" legislation in Nova Scotia or the Statute of Frauds in P.E.I.

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- The Brantford General Hospital Foundation and Marquis Estate case (2003) is the most recent decision on pledges, but case law is not usually clear in this area
- Important to include testamentary provision in a will to ensure that any outstanding pledge is fulfilled
- Since a pledge may not be enforceable, it should not be considered and counted as a gift until the pledge is actually received, or alternatively it should only be identified as a "pledge" as opposed to an actual gift received

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- It is important to determine whether that portion of a gift agreement that includes a future pledge is intended to be enforceable; i.e. with consideration which can be treated akin to a gift received, or unenforceable, which amounts to generally only a hope of a gift to come
- With a pledge for a future gift, whether enforceable or not, it is important to determine the timeframe in which the gift is to be paid (e.g. 2, 5, or 10 years)
- As well, if there are naming rights associated with a pledge agreement, whether enforceable or not, at what point do the naming rights come into effect; e.g. at 25%, 50%, or more of the gift, etc.
- Once the pledge is fulfilled, then the terms of the pledge agreement will become the basis of an enforceable gift agreement for the charity

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B. WHY DO GIFT AGREEMENTS GO BAD?

- Confusion concerning how and when gift agreement is created:
  - At the initiation of the donor

    - Donor dictates the terms through a testamentary or inter vivos gift
    - Donor negotiates the terms of an inter vivos gift with the charity (possibly even with testamentary gifts)
  - Charity invites contributions to an established fund, which means that the charity needs to articulate and communicate the terms of reference but fails to do so

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- Failure to consider applicable law
- Using unreliable precedents

- Failure to seek legal advice when necessary
- Failure to ensure that a gift agreement is actually prepared instead of relying upon conversations, emails or letter exchanges
- Failure to ensure that the gift agreement has been signed
- Failure to include an arbitration clause to resolve disputes if necessary
- Failure to remember the “contra proferentem rule” (i.e. any ambiguity in the agreement is interpreted against the party that drafted the agreement)
- Capitulating to excessive expectations of donors

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C. GIFT AGREEMENTS INVOLVE DONOR RESTRICTIONS

1. The Difference Between an Unrestricted Charitable Gift and a Restricted Charitable Gift

- It is important to understand the difference between a restricted and an unrestricted charitable gift

a) Unrestricted Charitable Gift

– An unrestricted charitable gift is to be applied towards a charitable purpose of a charity and not subject to any specific restrictions imposed directly or indirectly by the donor

– However, the board of a charity may therefore apply an unrestricted gift to its charitable purposes in whatever manner it deems appropriate

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– This means that the board of a charity may use the gift as it wishes in its discretion, provided that such use does not extend beyond its charitable purposes

– This could involve:

- Disbursing all or a portion of the gift, or
- Investing the gift over the short term or long term and using the income to pursue any one of the authorized charitable purposes within the constating documents of the charity, or
- A board that designates an unrestricted charitable gift for a specific charitable purpose may subsequently apply the funds to a different charitable purpose within the charitable objects of the charity (e.g. “internally restrictive funds”)

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b) Restricted Charitable Gift

- A restricted charitable gift in general means a gift given to a charitable purpose that is subject to restrictions, limitations, conditions, terms of reference, directions, or other restricting factors
- These limitations are imposed by the donor and constrain how the charity may use the gift
- While an unrestricted charitable gift is beneficially owned by the charity, a restricted charitable gift when structured as a restricted charitable purpose trust is held by the charity in trust for the purpose and is not actually owned beneficially by the charity
- For trust law purposes, each restricted charitable purpose trust is a separate trust

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2. Different Types of Restricted Charitable Gifts in General

a) Restricted charitable purpose trusts
- Long term gifts, including endowments
- Restricted use gifts
- Restricted charitable trust property
- Implied special purpose charitable trust funds

b) Conditional gifts
- Conditions precedent
- Conditions subsequent

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c) Precatory trusts and donor advised funds

d) Gifts subject to donor direction under the *Charities Accounting Act* (Ontario)

For more information, see *Drafting Issues for Restricted Gift Agreements Including Endowments*
http://sectorsource.ca/sites/default/files/Restricted_Gifts.pdf

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3. Specifics of Restricted Charitable Purpose Trusts

- A restricted charitable purpose trust is a gift held by a charity in trust for a specific charitable purpose that falls within the parameters of the general charitable purpose of the charity as set out in its constating documents (letters patent or articles of incorporation)
- A charity, cannot hold property as a restricted charitable purpose trust where such purpose is outside the scope of the charity's corporate objects or purposes

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- A charity can only use the gift to accomplish the specific charitable purpose established by the donor
- Common types of restricted charitable purpose trusts include:
  - Endowments
  - Long term funds
  - Scholarship funds
  - Building funds
  - Research funds

For more information, see the following articles on Considerations When Drafting Restricted Charitable Purpose Trusts (2012)http://www.carters.ca/pub/article/charity/2011/ETPJ30-4_Carter.pdf (2010) http://www.carters.ca/pub/article/charity/2010/tsc1001.pdf and Donor-Restricted Charitable Gifts: A Practical Overview Revisited II (2006) http://www.carters.ca/pub/article/charity/2006/tsc0421.pdf

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- There are conflicting approaches concerning the type of evidence necessary to establish that the donor intended to create a special purpose charitable trust
- In Re Christian Brothers of Ireland in Canada (Ont), Blair J. held that a high, formal standard of "in trust" is required, which would necessitate that it be in writing
- In Rowland v. Vancouver College (BC), Levine J. determined that the requirements for a restricted charitable purpose trust are less formal and could involve consideration of all relevant circumstances
- In Re The Land Conservancy of British Columbia (BC), Fitzpatrick J. followed the less formal requirement and considered the "surrounding circumstances" when a will or gift is made
- The dichotomy between the two approaches remains unresolved

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D. TWELVE COMMON DRAFTING PITFALLS TO AVOID

PITFALL #1: Failure to Accurately Describe Restrictions What are the Issues to Consider?

- Lack of clarity concerning whether there is an enforceable restriction or not
  - Unrestricted gift vs. Restricted gifts
  - Precatory gifts; i.e. unenforceable but implying a moral obligation; i.e. "it is my wish" or "desire that"
- Lack of clarity concerning what restriction is to apply e.g. is it a conditional or restrictive charitable purpose trust
  - The recent Norman Estate "Watch Tower Bible Society" decision is a good example of the impact of uncertain provisions
    - See case summary at: http://www.carters.ca/pub/update/charity/14/aug14.pdf

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  - The court had to determine if there was an inter vivos condition subsequent gift or a testamentary gift (which would have required a testamentary instrument to be enforceable)
  - Courts found that there was an inter vivos gift, which was good for the charity given the confusion in the applicable wording
- Do the restrictions on use; i.e. contributions towards a particular type or use of building continue to apply to replacement property?
- Restriction on alienation of gifted property; (i.e. shares in a company) can have an impact upon the fair market value of the gift for receipting purposes

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Tips to Help Avoid the Pitfall

- Determine what the donor actually wants and what the charity can accept from a practical perspective and then choose the appropriate language of restriction that will work best for both the donor and the charity
  - E.g. use a conditional gift with a gift over to another charity to enforce naming rights
- Use correct technical terminology
  - E.g. with restricted charitable purpose trust, use the words "in trust" to ensure it is enforceable
  - E.g. for conditional gifts, use clear conditional language such as "on the condition that" as opposed to less clear wording such as "but" or "if"

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PITFALL #2: Failure to Address What is Meant by "Endowment"
What are the Issues to Consider?

1. General Confusion

- Use of the term "endowment" when drafting needs to be carefully considered as confusion normally results
- "Endowment" is not a well understood legal term
- It generally describes the holding of the capital of a gift on a permanent basis in order to generate income for a charitable purpose
- In Arthritis Society v Vancouver Foundation (BC), the BC Supreme Court held that "the most common definition of the term 'endowment' is the provision of a fund which is intended to generate fixed revenue for the support of a charity"

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- The court also cited with approval the definition of endowment from Black's Law Dictionary that it is "the bestowing money as a permanent fund, the income of which is to be used in the administration of a proposed work"
- However, the word "endowment" has also been used to refer to trusts where the capital was to be retained for "10 years or more" for purposes of avoiding the 80% disbursement quota under the ITA prior to the 2010 amendments to the ITA
- Many donors and charities may not actually want to set up a permanent endowment fund when drafting a gift agreement or a will
- As a result, the actual words used in drafting a restricted gift must carefully reflect what the donor really wants in order to avoid creating an "endowment" when it is not actually intended

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2. Understanding Endowments as a Type of Time Restricted Gifts

- Time restrictions are the length of time that a restricted gift is to be held, creating a type of long-term gift
- The gift may be directed to be held permanently as an endowment or alternatively for a fixed number of years
- The donor may give the charity a right to encroach on the capital during the restricted period or not
- The income (and the capital where encroachment on capital is authorized) are used either for a specific application, like a scholarship, or for the general charitable purposes of the charity
- Once the restricted period has expired, if applicable, the charity can distribute the entire capital of the gift
- An endowment is an extreme form of time restricted gift where the capital of the gift is held in perpetuity and invested to produce income

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- Since charitable purpose trusts are exempt from the rule against indestructible or perpetual trusts, a charity is able at law to accept gifts where the capital is held in trust on a perpetual basis (but not for a non-profit)
- However, the charity is not able to unilaterally vary the trust at common law to collapse the endowment
- The following are examples of unclear wording from actual testamentary and inter vivos agreements purporting to establish an endowment:
  1. "To pay one such share to the [Charity] for the purpose of founding a scholarship in memory of [individual], the approximate net income therefrom to be paid yearly to a student who meets the following criteria."
  2. "This is to confirm the submission of $6175.12 of capital for the [ABC Award] in perpetuity to be awarded in the spring of each year."

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3. "The [Charity] hereby acknowledges receipt of the capital sum and agrees to hold the same in a separate investment account and to invest the capital sum and to pay the income derived therefrom to the [Charity] in one annual instalment on or about [date] in each year."
4. "I direct that the amount payable to the [Charity] shall be used by the Charity to provide a permanent scholarship to be awarded in my name."

Tips to Help Avoid the Pitfall

- Clarify whether the gift is intended to be a long term gift or a perpetual endowment, as frequently the donor does not actually want a perpetual endowment
- Essential to include the right to encroach on capital in an endowment and the ability to vary the purpose with regards to a use restriction
- Avoid using the word "endowment" in fundraising literature without clear explanation of what it means

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PITFALL #3: Failure to Clarify the Disbursement of Funds

What are the Issues to Consider?

- Need to determine whether the donor imposed any restrictions on how the income from a long-term gift, including an endowment, is to be distributed
  - Is it mandatory to disburse all income annually?
    - E.g. "all income each year must be expended on funding the youth scholarships"
  - Or is the charity given a discretion on how much it can disburse from income and how much it can retain?
- Does the agreement impose a restriction to retain a portion of income "to keep pace with inflation"?
- At common law, no encroachment of capital of a perpetual endowment is permitted unless the donor has given the charity authority to do so in the gift agreement

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- What constitutes "capital" that cannot be disbursed?
  - At trust law, capital gains forms part of capital and as such is not income
  - Therefore, unless the gift agreement defines income as including capital gains, expending realized capital gains would constitute breach of trust
  - This means that a "total return strategy" to invest and disburse income (i.e. to look at the best total return, without distinguishing between capital and income) is not permissible without authorization by the donor when the gift is established or by court order
- In Re Killam Estate (Nova Scotia), the court authorized a total return strategy based on the inherent jurisdiction of the court over the administration of charitable trusts

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- In Re Stillman Estate (Ontario), the court restricted the authority of the court to authorize a total return strategy to the cy-près jurisdiction of the court in the situation where there is either an impossibility or an impracticality
- Stillman generally reflects the approach taken by the Ontario Public Guardian and Trustee, so court authorization for a total return strategy in Ontario will be limited to when there is either an impossibility or an impracticality
- Stillman was recently followed in Fenton Estate(Re)(BC)
- What would constitute an impracticality for purposes of a cy-près court application involving a total return strategy?
  - Inability to meet the 3.5% disbursement quota for the charity under the ITA

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  - For larger institutions, query whether it might be possible to argue that it would be impractical to not apply a total return strategy to the collective endowment funds of the charity if it would be an excessively costly administrative burden for the institution to administer those endowment funds different from other investments done on a total return basis
- In Ontario, court authorization may be possible on a consent basis through the Public Guardian and Trustee under s. 13 of the *Charities Accounting Act*, or alternatively by an order in open court

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Tips to Help Avoid Pitfall

- In order to avoid having to obtain court authorization, the charity needs to obtain authority from the donor to adopt a total return investment strategy by:
  - Including specific authorization in the gift agreement, or
  - Incorporating such authority by reference into the gift agreement
- On the latter option, it is best to have a Disbursement Policy which provides for a total return investment strategy that can be specifically incorporated by reference
- However, the Disbursement Policy cannot remediate existing or future gift agreements that fail to incorporate by reference the Disbursement Policy of the charity

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PITFALL #4: Forgetting to Identify If There Might be an "Advantage"

What are the Issues to Consider?

- In the event that there is an "advantage" associated with a gift agreement that is not reflected in the charitable receipt, then:
  - The charity may be subject to a range of penalties of 5%, 10%, or 125% of the value of the gift, and
  - The donor could be subject to reassessment

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- Examples where the "advantage" can be problematic with the gift agreement include:
  - Pecuniary advantages occurring to the donor
  - Sponsorship provisions
  - Commercial naming opportunities
- The rules associated with determining the "advantage" are complicated and broad reaching but reflect the basic mechanics of split-receipting rules:
- Charitable donation receipt must reflect the eligible amount of the gift determined as follows:
  - Eligible amount of the Gift Equals Fair Market Value Less Advantage
- Must have a voluntary transfer of property of ascertainable value

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- Donative intent required
  - Must have a clear donative intent by the donor to benefit the charity
  - Donative intent will generally be presumed if the fair market value of the advantage does not exceed 80% of the value of the gift
  - Deduct Advantage
  - Broad definition of advantage: total value of all property, services, compensation, use or other benefits
    - To which the donor, or a person not dealing at arms length with the donor
    - Has received or obtained or is entitled to receive
    - As partial consideration of or in gratitude of the gift or that is in any other way related to the gift

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- Advantage must be clearly identified and its value "ascertainable"
  - Advantage can be received prior to, at the same time as, or subsequent to the making of the gift
  - Advantage does not require a causal relationship between the making of the gift and the receiving of the advantage, as long as the advantage is in some way related to the gift
  - Advantage can be provided to the donor or to a person or partnership not dealing at arm's length with the donor
  - Not necessary that the advantage be received from the charity that received the gift - advantage could be provided by third parties unbeknownst to the charity

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- CRA's administrative exemption applies where there is a token advantage of the lesser of 10% of the value of the gift and $75 (de minimis threshold)
- Example - A charity receives a gift of land from a donor who has received some type of benefit from a developer who owns property adjacent to the donated property in exchange for making the gift

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Tips to Help Avoid the Pitfall

- Important for gift planners to understand the split-receipting rules that apply in determining if there might be an "advantage"
- Need to understand that the responsibility lies with the charity to determine the "eligible amount" of the gift under the requirements under the ITA, since it is the charity that could face a penalty of 5%, 10% or 125% of the amount of the gift
- It is also important to obtain an appraisal for the fair market value of the advantage, if available, as well as the fair market value of the gift where it involves a gift in kind

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PITFALL #5: Forgetting to Consider the rights of the Donor

What are the Issues to Consider?

- Disgruntled relatives attacking the gift based on allegations of incompetency of the donor or undue influence by the charity
- Donors who are competent but are incapable of providing clear instructions for the gift agreement
- Donors who may be incompetent but are not able to recognize that they may be incompetent
- Donors who are competent but are vulnerable individuals due to age, infirmity, or economic circumstances

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Tips to Help Avoid the Pitfall

- Standard gift agreement used by the charity should contain a provision that states a recommendation and acknowledgement that the donor has been advised to obtain independent legal advice
- Where the competency or the vulnerability of the donor is in question, insist that the donor must obtain independent legal advice before signing the gift agreement and that such advice be confirmed in writing
- In situations where the gift agreement may be challenged by family members, seek an independent opinion of competency before the gift is made
- Where the potential for allegations of undue influence could arise, carefully document the steps that are taken to avoid circumstances that might otherwise suggest undue influence

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PITFALL #6: Giving Excess Control to the Donor What are the Issues to Consider?

- Donor imposing a restriction that is outside the charitable purposes of the charity
- Donor instructing the charity who is to benefit
- Donor instructing the charity which charities are to benefit
- Donor retaining the right of approval over management and/or investment of gifted funds
- Donor retaining the right to vary or approve a variation of restrictions
- Donor's entitlement extending from that of a "Donor Advised Fund" to that of a "Donor Directed Fund"
- Excessive donor's rights could mean that no gift may have been made in the first place

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- Donor direction that a subsequent gift be made to a foreign charity without adequate "direction and control" by the charity (see CRA Guidance on Foreign Activities)
- Donor directing how gifts are to be used in a conflict area could result in compliance issues with regards to anti-terrorism and anti-bribery legislation

Tips to Help Avoid the Pitfall

- "Donor advice" is permissible but must avoid "donor approval" or other forms of overt control by the donor
- Use of restrictions by the donor is permissible but not ongoing management control
- Discretion over the management of the fund must lie solely with the charity and not with the donor
- Considering using a condition subsequent

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PITFALL #7: Unclear and/or Excessive Donor Naming Rights

What are the Issues to Consider?

- Often the gift agreement may contain vague and/or incomplete provisions concerning what the donor naming rights involve, how long those rights will continue and how those rights can be terminated by the charity
- As well, need to determine whether naming rights give rise to an "advantage" being created under the ITA that would prevent the donor from obtaining a tax receipt for the full value of the gift?
  - CRA has generally held that individual naming rights alone do not constitute an advantage

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  - For businesses, if the naming rights amount to sponsorship that promotes the business brand or products, such rights could constitute an advantage
  - However, the business may be able to deduct the value of such an advantage as a business expense
- Donor agreements suggest a type of "donor glorification" verging on a collateral non charitable purpose
  - If the gift agreement is more about the glorification of the donor and his/her reputation than about the gift, there may be a risk that CRA or the courts could find that such extreme naming rights might constitute a collateral non charitable purpose
  - For instance, where a gift agreement includes excessive contractual provisions that allow the donor to seek "damages" from the charity for breach of donor naming rights

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Tips to Help Avoid the Pitfall

- Develop a naming policy that clearly sets out (amongst others) the specifics of the naming rights that the donor will be entitled to, the length of time of those rights, the ability to terminate naming rights, and what portion of the gift must be received before naming rights will commence
- Avoid pressure by "bully donors" who attempt to dictate the terms of the gift agreement primarily for their own glorification
- Avoid contractual provisions that cannot be realistically fulfilled, such as promising to ensure that a building will be " perpetually" named in the name of a donor
- For donors who want recourse in the event that naming rights are terminated, utilization of a "condition subsequent" with a gift over to another charity may be an option to consider

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PITFALL #8: Incomplete Charity Initiated Restricted Funds

What are the Issues to Consider?

- Charity establishing its own restricted fund with a request for contributions from donors without having established adequate terms of reference
  - e.g. Charity requesting contributions to an endowment fund; such as" Millennium Endowment Fund" without having first adopted terms of reference to explain what is meant by "endowment" or the ability to encroach on capital
- Charity encouraging the establishment of "in memorandum gifts" without explaining the purpose and restrictions that will apply to such gifts
- Lack of clarity can create confusion that could require an application to the court for directions

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Tips to Help Avoid the Pitfall

- Need to fully describe the terms of reference for charity initiated funds that donors are asked to contribute to
- Obtain board approval of the applicable terms of reference
- Post the term of reference on the website and/or the publications of the charity
- Take a time dated "screen capture" of the terms of reference for future evidentiary purposes

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PITFALL #9: Failure to Obtain Proper Authorization For the Gift Agreement

What are the Issues to Consider?

- A board member questioning staff, "You agreed to do what with the gift….?"
- When a restriction in a gift cannot be complied with but the charity has accepted the restricted gift, board members can be left exposed to personal liability for breach of trust for failure to comply with the terms set out in the agreement
- Board members have a fiduciary duty to ensure that all restrictive charitable purpose gifts are complied with in accordance with their terms

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- As such, board approval or, delegated approval by the board to senior management is essential to have properly documented because it can impact the board members on a personal basis
- Otherwise, management may simply inform the board about restricted gifts that have already been accepted without first obtaining the necessary approval from the board or seeking delegation of approval authority from the board

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Tips to Help Avoid the Pitfall

- The charity should include in its gift acceptance policy the procedure to be followed for approval of gift agreements
  - The gift acceptance policy may have attached to it a schedule of standard form for gift agreements that can be used as precedents where gift agreements are being negotiated
  - The gift acceptance policy can indicate the level that senior management can have sole authority to accept a gift agreement, beyond which amount approval will need to be obtained from the board of directors

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  - A gift acceptance policy should specify that when management becomes aware of non-compliance with restrictions under a gift agreement that the matter should be brought to the attention of the board of directors or an appropriate board committee
- At the end of the day the board of directors of a charity has a fiduciary duty to account for restricted gifts and therefore all authority concerning acceptance and management of restricted gifts lie with the board

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PITFALL #10: Failure to Include a Variation Clause

What are the Issues to Consider?

- A donor cannot retain the right to vary the terms of a restricted charitable gift after it has been gifted because the gift has become the property of the charity
- However, the donor can retain the ability to provide non-binding input through the inclusion of a donor advised option in the gift agreement
- The charity cannot unilaterally vary the terms of a restricted gift unless the gift agreement provides such authority to the charity or court approval is given

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- Recent case law has underscored problems associated with charities that failed to include a variation clause and the limitations of what the courts can do in response
  - Mulgrave School Foundation decision
    http://www.carters.ca/pub/update/charity/15/jan29.pdf
  - Fenton Estate decision
    http://www.carters.ca/pub/bulletin/charity/2014/chylb333.htm
  - Vancouver Opera Foundation decision
    http://www.carters.ca/pub/update/charity/15/mar26.pdf

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Tips to Help Avoid the Pitfall

- The gift agreement should include a provision that gives the charity the ability to vary the terms of the restricted gift, including both use and time restrictions
- The terms of reference for the charity to be able to utilize a variation power is normally tied to terminology like “impossibility or impracticality” in accordance with the common law cy-près power of court
- However, a variation power granted to a charity does not have to be restricted to only situations where a court could exercise its “cy-près” power, as it is up to the charity to determine the circumstances under which the use or time restriction can be varied

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PITFALL #11: Confusion in Investment Power

What are the Issues to Consider?

- Not clear which investment powers apply
  - Does the gift agreement establish an investment power?
  - If not, need to look at the letters patent, supplemental letters patent, or articles of incorporation of the charity to determine if an investment power has been established

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- Failure of the charity to have a general investment policy
  - The charity should have a general investment policy that reflects the requirements under the *Trustee Act* (Ontario) as oppose to what a financial institutions may propose
  - e.g., the *Trustee Act* provides that:
    - Prudent investment standard applies
    - The ability to invest in mutual and pooled funds
    - The seven mandatory investment criteria
    - The need to diversify investment
  - Each restricted fund may require a different investment approach that builds upon the general investment policy of the charity

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- Failure to provide for delegation of investment decision making
  - At common law a charity cannot delegate investment decision making
  - The *Trustee Act*, when it applies, permits delegation of investment decision making to an agent provided that it complies with provisions of the *Trustee Act*
  - Most investment management agreements with financial institutions that authorize delegation place the responsibility and risk upon the charity and often require an indemnification from the charity, neither of which are acceptable

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Tips to Help Avoid the Pitfall

- The charity needs to adopt its own investment policy in accordance with the terms of the applicable *Trustee Act* in its respective jurisdiction
- When drafting a gift agreement, the investment policy of the charity should be incorporated by reference into the gift agreement by referring to the "investment policy of the charity in place from time to time"
- In rare situations, the donor might be given the option of imposing specific investment restrictions on the gift, provided they are stated as having to be consistent with the "prudent investor standard" set out in the applicable *Trustee Act*, and the investment policy of the charity

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PITFALL #12: Failure to Authorize Administration Fee What are the Issues to Consider?

- Disgruntled family members of a donor who expect that all income from the donor's restricted gift must be used towards the restricted charitable purpose with no part to be used for administrative costs
- This can result in the general funds of a charity having to cover all of the administrative costs of restricted gifts
- Charities that unilaterally state after the fact that they charge an administrative fee on restricted gifts may encounter problems if there is no authority that can be cross referenced in the gift agreement
- In some extreme situations, this could lead to allegations of breach of trust and embarrassment to board members and as well as senior management

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Tips to Help Avoid the Pitfall

- The gift acceptance policy for a charity should provide that an administrative fee will be charged on restricted gifts, with the amount of the administrative fee to be determined from time to time in the discretion of the charity
- Provisions dealing with the administration fee in a gift acceptance policy should be incorporated by reference into the gift agreement
- As well, the website and/or documentation publicizing the fundraising by the charity should clearly indicate that an administrative fee, as determined by the charity, will be charged on all restricted gifts

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