Legal Developments

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Ethical Investing

In (1993), 11 *Philanthrop.* No. 4, I reported on *Harris and Others* v. *The Church Commissioners*, an English case dealing with "ethical investing" by charitable trustees. Those interested in that subject should read the Manitoba Law Reform Commission's Report No. 79 of 1993, *Ethical Investments By Trustees.*

Ethical investing generally means refusing to place trust funds in investments considered morally questionable by the trustees, or investing in ventures which advance the trustees' vision of the "good society". Trust law has long insisted that all trustees, be they of private trusts or of large funds such as trusteed pension plans, must invest prudently, an admonition that includes having regard to the primacy of the rate of return. The only departures from this principle come when the trust instrument itself allows investing to be guided by other considerations, and in the case of South Africa, through Ontario's *South African Trust Investments Act*, R.S.O. 1990, c. S-16 (still unrepealed).

The *Report* does an excellent job of laying out both the meaning of "ethical investing" (chapter 2) and the current law on the subject (chapters 3 and 4). When it moves to analysis, it does not suggest that anything other than the trust instrument should permit ethical investing at the expense of prudence. It considers only whether trustees are allowed, or should be allowed, to make ethical choices among investments that qualify as prudent. It argues, correctly, that the current law on this matter is actually unsettled and discusses the arguments against allowing trustees to do so. These include the additional administrative costs that will be incurred, the difficulty of knowing what beneficiaries want (especially in trusts with many beneficiaries), and the possibility of abuse. It demonstrates that these difficulties are often overstated and concludes that there should be an amendment to the provincial *Trustee Act* explicitly to permit trustees to employ non-financial criteria in making investment policy provided, of course, that the trust instrument does not preclude this and that the rule of prudence is observed. The suggested amendment states that in employing non-financial criteria a trustee must exercise "the judgment and care that a person of prudence, discretion and intelligence would exercise in administering the property of others".

This is a modest recommendation, its modesty emphasized by the fact that the Report also states that a trustee who employs non-financial criteria must keep as "the primary objective of the trust" (p. 42), or alternatively as "a predominant goal" (p. 48), the securing of a "reasonable financial return" (both pages). While some might argue that Pandora's box has been opened and that abuse and litigation will escape, this is unlikely. Trustees already have general discretion to choose among investments that are prudent, and this amendment would only clarify one aspect of that discretion.

Cultural Property

In July of last year the Federal Court Trial Division handed down judgment (unreported, Court No. T-1181-92) in a messy affair involving one Samuel Sarick, the Art Gallery of Ontario (AGO), and the Canadian Cultural Property Export Review Board (the Board).

In 1991 Sarick donated over 200 pieces of Inuit sculpture to the AGO. He wished to take advantage of the substantial income tax benefits that accrue to donors when they donate property designated as "Canadian cultural property" to a designated institution.[1] In Sarick's case there was no question that the paintings were cultural property and no question that the AGO was a designated institution. Rather, a dispute occurred about their value and, therefore, about the amount of the tax deduction the donor could claim.

Under the legislation, the Board is the body charged with determining value and in this case the AGO submitted two appraisals with its application for valuation, each for a little over $1.5 million. The Board indicated that it had some concerns with the appraisals submitted to the AGO and independently obtained a third one which was less than either of the other two but was also for more than $1.5 million. It also obtained an opinion (though not an actual appraisal) from the National Gallery of Canada to the effect that the appraisals were on the high side of what was reasonable, but nonetheless within the category. It then obtained a fourth appraisal, and on the basis of this alone, decided that the value of the gift was 60 per cent of the AGO's appraisals, or about $950,000.

The case that went to the Federal Court ultimately dealt only with one narrow point—whether the Court should order the Board, when it conducted a redetermination of fair market value, to give an oral hearing to the applicant AGO. Counsel for the Board conceded that there should be a redetermination because the original process had not been carried out in accordance with the Board's governing statute or with procedural fairness. Specifically, the Board had not disclosed to the AGO the information it had received in the form of the fourth appraisal and other information, and had not given the AGO the opportunity to make representations regarding the appraisal or anything else. In addition, it had

not provided written reasons to the applicant in support of its determination of fair market value.

Thorstein J. allowed the application for an order directing an oral hearing on the redetermination. He did not say that such a hearing was required in every case but felt that in the particular circumstances natural justice required one. Those circumstances included the failure to proceed fairly as noted above but they went beyond that. The Court alluded also to the fact that the fourth, low, appraisal, had been done without the appraiser actually viewing the collection, that the appraisal itself consisted of a handwritten note of some one and one-quarter pages, and that there was a previous relationship between the appraiser and the Chair of the Board. Indeed, it should be noted that the Court also ordered that the Chair not be involved in the redetermination. The Court was concerned that the fourth appraisal, about the credibility of which it thought "a suspicion" existed, had been accepted without challenge while the others had been effectively rejected without inquiry. The Court obviously had concerns about the motives and actions of the Chair, although nowhere does the case discuss what those motives might have been. All of these factors meant that "an open process with the opportunity for cross-examination is...desirable". The original decision was one in which the AGO "quite properly did not have confidence".

While the decision in the case was confined to a narrow point on the law of procedural fairness, it is likely to have wider ramifications. The legislative scheme which provides for the designation of cultural property and for its valuation for tax purposes is designed to encourage private collectors to donate cultural property to Canadian institutions rather than to sell them on the open market, which will often involve foreign sales. If collectors come to feel that they could have no confidence in the process, they might well be discouraged from donating.

This decision will probably prevent members of the Board from acting inappropriately in a future case, whatever their motives. On the other hand, all taxpayers have an interest in fair uninflated valuations, for it is ultimately they who pay to keep cultural property in the country. The problem of inflated valuations leading to "profitable" donations has arisen before, and the chair of the Board may well have been responding to this more general concern. But whether, in this case, the Board's valuation was, or was not, a correct one, it was made in very unusual and suspicious circumstances and was at odds with the preponderance of the evidence.

The Board Chair involved in this case has since resigned. This decision will probably prevent his successor or other members of the Board from acting inappropriately in future cases, whatever their motives. Given the substantial sums involved, and given that recipient institutions and Revenue Canada en-

gage lawyers to prepare submissions to the Board anyway, the government might also consider holding hearings as a matter of course.

Alberta's *Charitable Fund-Raising Act*

A recent issue (12,2) of *The Philanthropist* contained a report of the Alberta Court of Appeal's decision in *Epilepsy Canada* v. *Attorney-General* (1994), 115 D.L.R. (4th) 501 (Alta. C.A.), a decision which held provisions of Alberta's *Public Contributions Act* (R.S.A. 1980, c. P-26) to be unconstitutional. Readers should also note that this issue has a lengthy discussion of the arguments in that case, by Forrester and Chipeur. (p. 29) In fact the Court of Appeal's decision was stayed until 30 April 1995 to allow the legislature time to amend the *Act*, and on 1 May 1995 the *Charitable Fund-Raising Act* (S.A. 1995, c. C-4.5) became law in Alberta. There is not space here to review the *Act* extensively, but two principal points are worth noting. First, part 1 of the *Act* regulates the solicitation of contributions. Applying only to persons who raise $10,000 or more a year from people in Alberta, it regulates principally how solicitation may be done, creates a duty to maintain records and provide receipts and information, and mandates that funds received by professional fund raisers be held in trust for the charitable organization.

Second, part 2 of the *Act* makes it possible to limit who may solicit. Section 12 (1) states that "no charitable organization may make a solicitation to an individual unless the charitable organization is registered". Section 12 (3) limits the application of this regulation to organizations which raise $10,000 or more, and section 13 prohibits unregistered organizations from using professional fund raisers. The provisions on registration lay out the grounds on which the Minister may refuse a registration. These include prior convictions of the organization's principals, such that "in the Minister's opinion...the person convicted is unsuitable to deal with contributions or make solicitations". Other grounds for refusing registration are laid out. Essentially the *Act* provides that if the Minister believes with good reason that an organization is controlled by a person or persons who is or are "unsuitable to deal with contributions" or "will contravene the *Act*" registration may be refused. If registration is refused, the parties concerned have the right to be notified of why and may make representations concerning the refusal. A further set of provisions establishes a licensing scheme for "professional fund raisers", one that is essentially the same as the registration scheme for charitable organizations discussed above.

These registration and licensing provisions are the key changes from the old law. The prior statute was found unconstitutional, not because regulating solicitations was wrong, but because the statute was overbroad—it applied to everybody, large and small, it required approval for every campaign and, most importantly, it gave a nearly total and unprincipled discretion to government to refuse permission. The *Charitable Fund-Raising Act* turns this around; every-

body has a "right" to be registered or licensed, as the case may be, and the Minister must justify refusals. The admirable principle of regulating the ways in which the charitable sector raises money from the public is retained, the unconstitutional aspects of the way in which this was to be done have, in my view, been removed.

FOOTNOTES

1. These benefits, and the relationship between the *Cultural Property Export and Import Act* and the *Income Tax Act*, are described in H. Erlichman, "Case Comment: Profitable Donations—What Price Culture" (1992), 11 *Philanthrop.* No.2, pp. 3-8.