Fact Sheet: Essential Glossary of Investment and Impact Investing Terminology

Glossary of Essential Terms

To support Foundations and their Boards in engaging with Impact Investing, we know that it is often helpful to have a shared language that we can all speak in common, and that unfamiliar terminology is often used in the private investment market. This glossary provides a essential terms foundations are likely to encounter as they engage with this field.

Related to General Financial Terminology, Investing, and Grant making

Accredited Investors: Investors who are exempted from requiring a ***prospectus*** to invest in a business because they are assumed to be able to get and analyze the required information and can bear the loss if things go wrong. While definitions vary province to province, a typical standard is owning financial assets of $1 million net of liabilities. Registered charities are also often considered accredited investors.

Annual Spending Requirement (Disbursement Quota): The requirement by the CRA that Foundations spend 3.5% of the average value of their property (calculated over a 24-month period) on its own charitable activities or gifts to ***qualified donees.***

Below-Market Rate: Any investment made at a concession primarily for your programmatic purposes without the expectation of a risk-adjusted market-rate return. See ***PRIs.***

Due Diligence: An in-depth process of evaluating a potential investment, including the careful confirmation of all critical assumptions and facts presented by a potential investee. This involves assessing the feasibility of financial and social goals and the capacity of the organization to achieve them.

Environmental, Social, and Governance (ESG) Integration: An investment strategy that incorporates ESG criteria into investment analysis and portfolio construction across asset classes. Examples include selecting investments for the positive ESG performance of a sector, company, or project relative to industry peers; excluding certain sectors or companies from a fund based on specific criteria. See ***The Impact Investing Spectrum [LINK].***

Liquidity: The availability of easily sellable financial assets and cash to pay for expenses. For example, Foundations that have made multi-year grants require the current income or other cash assets necessary to distribute these grants to their supported charities.

Market-Rate: The risk-adjusted financial return on an investment that a conventional investor expects for a given type of investment. Market-rate is often determined based on what comparable investments are priced at. For example, a market-rate mortgage would be the usual rate charged by commercial banks.

Mission-Related Investements (MRI): These are impact investments made with the expectation of generating social or environmental benefits and risk-adjusted market-rate returns. MRI investments are made from a Foundation's total assets, such as its endowment.

Off-balance sheet: Those financial liabilities or assets which don't appear on the foundation's financial statements or reporting. For example, the foundation may plan to make significant grants in the coming years, or they may anticipate a significant donation after conferring with a donor.

Program-Related Investments (PRI): These are a category of impact investments that are specifically available to foundations who are looking to make below-market rate investments. In Canada, these investments must be 1) made in a **qualified donee** or be shown to meet the "own activites" requirements of the Income Tax Act and 2) directly further the Foundation's stated charitable purposes. The difference between market yield and the investment yield is considered a "gift" of charitable assets by the CRA. See ***Legal Fact Sheet [LINK].***

Prospectus: A formal legal document that is required by and filed with a Securities Commission that provides details about an investment offering for sale to the public. This legal document is not required in the case of Foundations when they are **accredited investors.**

Qualified Donee: Organizations that under the Income Tax Act can issue official donation receipts for gifts. These organizations can be eligible for **Program-Related Investments**.

Socially Responsible Investing (SRI): An approach to aligning an investment portfolio with an investor's values by excluding companies or industries. See **Complementary Approaches.**

Unrealized Gain/Loss: The gains or losses in an investment's value that occur prior to it being sold or liquidated. For example, a venture capital fund may have portfolio companies with growing valuations, which are unrealized gains for investors until the point that the fund's investment positions are sold.

Unrestricted Assets: Assets that do not have a programmatic or investing requirement outside of the purposes of the Foundation. For example, a Community Foundation will often have Donor Advised Funds (DAFs) that are restricted to specified purposes, whereas other endowment funds are not as restricted.

Glossary Related to Impact Investing Instruments

Impact investing takes place across a variety of asset classes, by which we refer investments that have similar characteristics. This section provides some useful definitions in understanding different types of investments.

Grant Support: A sum of money given away charitably in pursuit of a particular social or economic purpose that has no financial return.

Equity (Stock): An ownership stake in a company that entitles the owner to economic benefits such as dividends and voting rights.

Loans: A repayable investment, typically with a defined interest rate and duration.

- **Secured Loan:** A loan that has some collateral acting as "security"
- **Unsecured Loan:** A loan made without collateral
- **Subordinated Loans:** A loan repaid after other loans in regards to claims on assets or earnings in the event of bankruptcy or default. Creditors in a subordinate position do not get paid out until others in a more senior position are paid out in full
- **Senior Loans:** A senior loan is returned first to the lender before other claims against a borrower.

Cash: Deposits that are CDIC are traditionally offered by banks and credit unions. Most often these cash deposits serve as the backing for lending activities.

Guarantees: A promise to provide capital if another borrower is unable to repay a loan. Guarantees can be used by Foundations to help a borrower who would otherwise be ineligible to obtain financing. Guarantees can either be funded (such as providing a cash deposit that will only be drawn in the event of a default) or unfunded (where it is a promise to repay).

Fixed Income: Most commonly, a bond. These are contractual obligations that an investor will receive fixed payments over a set period of time with the principal either repaid over this period or at maturity.

Fund of Funds: Where a fund purchases positions in multiple other funds, it is a "fund of funds". This approach is common when underlying funds are small or don't individually provide the diversification that an investor is seeking, or the transaction costs of an individual investor participating in each fund is too high.

Private Equity: stock in companies that is not traded on the stock market. Private equity is commonplace in small and medium sized enterprises that are not yet large enough to trade publicly. Private equity is often not very liquid as it is difficult to sell quickly at a fair price.

Public Equity: stock in companies that is traded on the stock market (e.g., the TSX). Typically public equities are where most ESG and Responsible Investment strategies are deployed. See ***The Impact Investing Spectrum [LINK].***

Real Asset: Investments that are made in some tangible, physical property, such as buildings, timberland, or farm land.

Social Impact Bond (Pay-for-Success): A performance contract between government and a human services charity or non-profit where investors provide working capital for the service's delivery with the right to receive payments from the government if the project successfully delivers against defined performance benchmarks.

Venture Capital: Investments made in early-stage businesses on the expectation of significant growth and development.

Angel Investment: Investments made in start-up ideas at a very early stage. Often angel investments are the first investments an entrepreneur receives outside of their family.