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"LOOKING A GIFT HORSE IN THE MOUTH"
AVOIDING LIABILITY IN CHARITABLE FUNDRAISING
(Current to March 22, 2004)

By Terrance S. Carter, B.A., LL.B

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1. INTRODUCTION

This paper is intended to provide a practical overview of the legal risks associated with charitable fundraising in Canada, with a particular emphasis on charities that operate in Ontario. The paper discusses practical steps that can be taken to avoid such legal liability, where possible. An earlier version of the paper was presented for the Law Society of Upper Canada 2nd Annual Trusts and Estates Forum held in November 1999, was then subsequently updated on October 5, 2001, and has now been significantly updated and expanded since then to reflect recent changes in the law.

The paper is primarily directed to fundraisers and senior managers who either work for or act on behalf of charities, as well as to lawyers who advise charities or who themselves serve on the boards of charitable organizations.

At the outset, it is important to establish the terms of reference and limitations that apply to this paper:

* The author would like to recognize and thank Mark Wong for his contributions on the sections dealing with PIPEDA, the new federal privacy legislation, Mervyn White for his contributions on the sections entitled "Legal Issues Involving Fundraising on the Internet" and "Implications of Bill C-45 (Westray Mines) on Fundraising", and Suzanne E. White, articling student and R. Johanna Blom, for their assistance in helping to research, edit and update this version of the paper. Any errors are solely those of the author.

- First, the terminology of "fundraising" is used in its broadest sense to encompass the full range of fundraising activities undertaken by charitable organizations and professional fundraisers, which activities are often referred to as "planned giving", "stewardship programs", "deferred giving", "strategic fundraising", "donor development", "recognition opportunities", "prospect research", "moves management", and everyone's favorite, "the ask".

- Second, while the paper focuses on legal liability associated with various fundraising vehicles, it does not purport to provide anything more than a brief explanation of how those fundraising programs in fact operate.[1]

- Third, given the vastness of the legal issues that impact upon charitable fundraising, the paper does not attempt to cover all of the relevant liability issues, nor are the issues that are included in this paper discussed in a comprehensive or detailed manner. Instead, the issues that are addressed reflect an acknowledged preference by the author toward topics that have proven to be either relevant or challenging in day to day practice.

- Fourth, by design, this paper provides only a brief discussion of tax issues involving fundraising under the *Income Tax Act*[2] (the "*ITA*"), since the tax treatment of donations and charities has already been thoroughly canvassed by others.[3]

- Fifth, in order to provide as practical a paper as possible on what is acknowledged to be a broad topic, the approach that has been adopted is to highlight a wide range of legal issues, but limit the commentary on each issue to a summary only. Any comments in the paper that are of a more lengthy nature simply reflects the personal interest of the author on the topic and is not intended to diminish the importance of the other issues that are discussed in less detail. With some of the topics where the author has already prepared outlines on the issues, copies of the outlines have been attached as Appendixes to this paper for ease of reference.

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[1] For a practical overview of various fundraising programs and techniques, reference can be made to E. Pierce & S. R. Kushner, *Planned Giving: Making it Happen,* Vol. 1 (Toronto: Strategic Ink Communications, 1998). See also F. Minton & L. Somers, *Planned Giving For Canadians* 2d ed. (Waterdown: Somersmith, 1997); and Donald J. Bourgeois, *Charities and Not-For-Profit Fundraising Handbook* (Toronto: Butterworths, 2000).

[2] R.S.C. 1985, c.1 (5th Supplement) as amended.

[3] For a detailed discussion of tax treatment of charitable gifts, reference should be made to Arthur Drache, *Canadian Taxation of Charities and Donations* (Toronto: Carswell, 2000). See also M. Elena Hoffstein, "Impact of Recent Budgets on Gift Planning" in *Charities and Not-for-Profit Law* (Continuing Legal Education of the Canadian Bar Association, Toronto, 1998)., J. Donald Bourgeois. *The Law of Charitable and Non-profit Organizations*, 3rd ed. (Toronto: Buttersworth, 2003); Jim Parks, "The State of Estates: Recent Developments Affecting Clients, Professional Advisors and Trustees – Charitable Gift Planning", presented at the 2000 Institute of Continuing Legal Education, Ontario Bar Association, Toronto, Ontario, January 28, 2000; Ontario Bar Association, "Issues in Charity Law: A Pot Pourri", Toronto, Ontario, October 22, 2002., Maria Elena Hoffstein, Terrance S. Carter, and Adam Parachin, *Charities Law – 2003-2004 Edition*, (Markham, Ontario: Lexis-Nexis, Butterworths, 2003).

Clearly, both the quantity and complexities of the legal issues involving charitable fundraising are such that a single paper can only touch the surface of the liability issues that a lawyer will need to advise a charity on from time to time. However, it is hoped that this paper will serve as a practical reference tool for management and fundraisers of charities, as well as lawyers who wish to become familiar with the various areas of the law that a charity should be aware of in fundraising. For situations where the lawyer who is giving advice to a charitable client needs to conduct further legal research on a topic discussed in this paper, a selective bibliography of resource materials on legal issues in charitable fundraising can be referred to at the end of this paper.

2. LEGAL RISK MANAGEMENT IN FUNDRAISING: A NEW APPROACH

A. "For Every up There Is a Down"

Fundraising, by necessity, is occupying a greater role for charities in recent years, due to a combination of government cutbacks in support for charities, competition amongst charities for available donations, and an increased demand for services being placed upon charities by the public. The reality of increased budgetary pressures to achieve and maintain an ongoing source of funds often precludes a charity from having the luxury of time to properly evaluate the legal consequences of the various fundraising programs that it undertakes.

The risks associated with improper fundraising programs can, however, easily negate any benefit that is realized. In fact, the potentially damaging effect from even just one improper fundraising program could quickly become a major liability for the charity that might seriously reduce other sources of income for the charity, or possibly even prejudice its' operating capital. Such negative financial consequences to the charity could expose both directors and officers to personal liability.

The necessity of operating an effective fundraising program for most charities is now *sine qua non*. Most large charities could not exist without large scale fundraising programs and departments. This is particularly true of universities and hospitals. The University of Toronto, for instance, is reported as having devoted approximately six million dollars ($6,000,000.00) a year and approximately forty (40) senior staff to fundraising in an effort to raise half a billion dollars in private money in 1999.[4] In 2004, the University of Toronto celebrated a significant achievement in fundraising, having reached the $1 billion mark since launching the "Campaign for U of T" fundraising initiative in 1997.[5]

Structured fundraising programs are focussed on donors of all ages, especially in light of the fact that it has been estimated that more than $41 trillion USD will be transferred to heirs in the next 55 years, $6 trillion of which is expected to go to charities.[6] In this regard, research has revealed charitable giving trends that defy commonly held perceptions that only people of retirement age are interested in philanthropy. Although each generation cohort tends to have different giving practices, Generations X and N are just as charitably minded as philanthropists born in the post-war baby boom era.[7]

With the increased dependency on fundraising and the proliferation of various fundraising vehicles that are in use, there is an increasing demand for accountability in fundraising from members of the public, the government, as well as by umbrella organizations, such as the Canadian Centre for Philanthropy. In the Final Report of the *Broadbent Panel on Accountability and Governance in the Voluntary Sector* released in February of 1999, the public demand for increased accountability was succinctly stated as follows:

> Fundraising, perhaps more than any of the other activities of voluntary organizations, is under enormous public scrutiny. The solicitation of funds is the only contact that many people have with voluntary organizations and their impression of the sector is shaped by this. Cuts in existing funding and

[4] Sara Scott, "The Ask", *The Globe and Mail Report on Business Magazine* (October 1999) 71 at 74.

[5] University of Toronto, "Celebrating a Milestone", *available at* http://giving.utoronto.ca/thecampaign/fullstory.html (accessed March 11, 2004).

[6] "Are You Prepared for the Donors in Your Future? – What can demographic trends tell us about fundraising in 10 years?", *Advancing Philanthropy*, May/June 2002, p. 17.

[7] *Ibid* at pp. 17 & 18.

> rising demands for services have created fierce competition for limited dollars and ever greater innovation in fundraising methods.[8]

The National Survey of Giving, Volunteering and Participating of 2000 found that approximately 46% per cent of Canadian donors fear their money will not be used in a proper fashion, with 47% disliking the fundraising methods used by charities, and as a result of these sentiments, these same donors limit their giving.[9]

To encourage the boards of charities to be more accountable in fundraising, various codes for ethical fundraising have developed in recent years. These initiatives include codes by professional organizations for fundraisers such as the Canadian Association of Gift Planners and the Association of Fundraising Professionals. The Canadian Centre for Philanthropy ("CCP") has produced the *Ethical Fundraising and Financial Accountability Code* (the "Code") a copy of which is attached as Appendix 1 to this paper ("the paper"). The Code describes a mechanism to facilitate queries and complaints arising from the Code from donors and the public generally. The Code also introduces a method by which charitable organizations can become recognized as *"Ethical Fundraising and Financial Accountability Code Adherents."* A charity may become an *Adherent* by having its governing board pass a formal resolution and informing CCP that such has occurred. Being an *Adherent* entitles a charity to be listed on the CCP's website, and to use CCP's Ethical Fundraising logo, introduced in 2003, on all its stationary and promotional materials.

In a letter from CCP to its members in October 2003, Peter Broder, Vice-President, Public Affairs (Interim) wrote,

> "Part of the rationale for the Code was that donors' decisions about supporting a charity should be about more than number crunching. We have recently added a logo for Code adherents to our program, and part of the licensing revenue from the logo will be used to raise public awareness of what constitutes reasonable fundraising practice. By supporting the Code

[8] Report on Accountability and Governance in the Voluntary Sector: *Building on Strength: Improving Governance and Accountability in Canada's Voluntary Sector* (Ottawa: Queen's Printer, February 1999).

[9] "Highlights from the 2000 National Survey of Giving, Volunteering and Participating", Statistics Canada, Catalogue No. 71-542-XIE, http://www.givingandvolunteering.ca/pdf/n-2000-hr-ca.pdf (accessed: October 23, 2003) at p. 14.

> logo, you will be contributing directly to our efforts to develop greater public understanding of and support for good fundraising practice."[10]

Another code entitled "*A Donor's Bill of Rights*" is attached as Appendix 2, and has been developed by four organizations: the American Association of Fund Raising Counsel (AAFRC), the Association for Health Care Philanthropy (AHP), the Council For Advancement and Support of Education (CASE), and the Association of Fundraising Professionals (AFP). The latter organization also established the "*AFP Code of Ethical Principles and Standards of Professional Practice",* a copy of which is attached as Appendix 3.

It is important for charities to keep informed about initiatives to promote ethical standards in fundraising. It would also be advantageous from a marketing and public relations standpoint for a charity adopting a code to publicly advise its supporters. A charity, though, must be careful not to rely solely on codes of ethics. It must first and foremost keep informed of and adhere to requirements placed upon the charity at law.

B. The Legal Responsibility of Directors to Oversee Fundraising Programs

Generally, most directors of charities consider the legal responsibility for fundraising to lie with either the professional fundraisers who are retained or employed by the charity or with the management of the charity. Evaluation by boards of directors of fundraising efforts is primarily based upon monetary performance and the financial results achieved instead of exercising the due diligence expected by them at law to review the appropriateness of the various fundraising vehicles that are utilized to achieve the monetary goals set by the boards of directors. While the boards of directors of most large charities (72% in 1996) do evaluate the cost effectiveness of fundraising practices of their respective organizations, a survey published by the Canadian Centre for Philanthropy found that the same boards generally do not take an active role in reviewing policy issues related to fundraising.[11]

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[10] Peter Broder, "Letter to CCP Members from Peter Broder, Vice-President, Public Affairs (Interim)", Toronto: Canadian Centre for Philanthropy, October 2003.

[11] Michael H. Hall, *Charitable Fundraising in Canada* (Toronto: Canadian Centre for Philanthropy, 1996) at 53.

This general lack of interest in reviewing the policies and risks associated with fundraising is not consistent with the fiduciary duty placed upon directors to exercise prudence in overseeing the operations of a charity and protecting its charitable property.[12] The duty of directors in this regard has been succinctly summarized in *"Charities Bulletin, No. 3"* published by the Public Guardian and Trustee of Ontario:

> Directors and trustees must handle the charity's property with the care, skill, and diligence that a prudent person would use. They must 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 must ensure that no excessive administrative expenses are incurred.[13] [Emphasis added]

(1) The *AIDS Society for Children* Case

The high fiduciary duty placed upon directors of charities from fundraising program was underscored in the case of *Ontario (Public Guardian and Trustee) v. The AIDS Society for Children (Ontario)* (hereinafter "The *AIDS* Society for Children (Ontario)).[14] The *AIDS* Society for Children (Ontario) (the "*AIDS* Society") was incorporated on November 28th, 1994, and obtained charitable status from Revenue Canada (now Canada Revenue Agency "CRA") three days after the date of incorporation on December 1st, 1994. The *AIDS* Society operated offices in various southern Ontario cities and distributed pamphlets indicating that the monies raised from public donations would be used to build a home (hospice) for children living with HIV/AIDS. The *AIDS* Society subsequently entered into fundraising agreements with two fundraising companies in 1996. One company was retained to solicit charitable donations from the public by telephone. The other company was retained to solicit charitable donations using door-to-door canvassing.

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[12] Ontario Law Reform Commission, *Report on the Law of Charities,* Vol. 2 (Toronto: Ministry of the Attorney General, 1996) at 570.

[13] "Duties, Responsibilities, Powers of Directors and Trustees of Charities" *Charities Bulletin No. 3: Information from the Public Guardian and Trustee's Charitable Property Program* (Toronto: Office of the Public Guardian and Trustee of Ontario, July 1999). (Also found at www.attorneygeneral.jus.gov.on.ca\htm\PGT\bullet3.htm).

[14] *Ontario (Public Guardian and Trustee) v. The AIDS Society for Children (Ontario),* [2001] O.J. No. 2170.

The contracts with the third party fundraising companies involved different arrangements, but both required that all expenses involved with the applicable fundraising were to be paid by the *AIDS* Society and that the fundraising company would then receive a percentage of the remaining amount raised. Of the $134,380.00 raised by the telephone campaign, 76% of those monies, or $102,216.00, was paid to the fundraising company retained to conduct the telephone campaign for its fees and expenses, with only the remaining 24%, or $32,163.00, being paid to the *AIDS* Society. Of the $241,012.00 raised through door-to-door canvassing, 80% of the monies raised or $193,238.00 was paid to the fundraising company conducting the door-to-door campaign for fees and expenses, and only the remaining 20% or $47,774.00 was paid to the *AIDS* Society.

In 1996, the Public Guardian and Trustee ("PGT") began receiving complaints from the public, other *AIDS* organizations as well as the media about the AIDS Society, specifically that the AIDS Society was not applying its funds for its charitable purposes. The PGT discovered, from admissions of the Directors of the AIDS Society, that despite raising $921,440.00 through public donations, no funds had been expended on the charitable programs of the AIDS Society and that in fact the AIDS Society was in debt. Through an initiative of the PGT, the activities of the AIDS Society were suspended by the Court and the PGT was made trustee of all of its assets.

In 1997, CRA subsequently revoked the charitable registration number that it had issued to the AIDS Society. The PGT brought an application for the passing of accounts pursuant to the *Charities Accounting Act* (Ontario) (the "*CAA*"). In the course of making the application, the PGT sought directions from the Court concerning the following questions:

1. Is the AIDS Society and/or its directors responsible as fiduciaries to the public for all of the funds collected from the public, including the gross amount of funds received by the two fundraising companies?

2. What is the nature of the legal relationship between the individual donor, the canvasser, the unit/crew manager, the fundraising companies and the AIDS Society?

3. Does the duty to account by the fundraising companies extend to the gross receipts collected from the donors on behalf of the AIDS Society?

4. Is all or part of the fundraising agreements void or voidable as being contrary to public policy or for some other reason?

5. Did the AIDS Society offend the 80/20 disbursement rule under the *ITA*, and, if so, what is the effect, if any, upon the contractual arrangements between the AIDS Society and the fundraising companies?

In its decision the Court first re-affirmed that it had inherent jurisdiction to direct or control the administration of charities and that the PGT as nominee of the Attorney General acts in a *parens patriae* role in overseeing the administration of charitable property in accordance with the power historically given to the Crown over charities and charitable property. As a result, the Court therefore had no difficulty with exercising jurisdiction in responding to the questions put to it by the PGT.

Similarly, the Court held that directors of a charity, although not strictly trustees, at law have a fiduciary obligation to the charity and the charitable property held by the charity. The Court went on to explain that while a fiduciary is someone who stands in a position of trust to another individual, a fiduciary relationship does not require that a "true trust" relationship exist. Accordingly, it is not necessary that the legal title of property be held in trust for another individual, only that there is a legal obligation on the part of the fiduciary to another individual to put the interest of that other individual ahead of the interests of the fiduciary.

The comments and answers provided by the Court in response to the questions submitted to it by the PGT are summarized below as follows:

1. Although charitable corporations do not hold their unrestricted property as trustees for the general charitable purposes of the charity, they do have a fiduciary obligation to hold property that the charity receives for the charitable purposes of the charity. As such, the AIDS Society, as a fiduciary of the monies donated to it, is responsible to account to the public for all monies publicly raised from it, including the gross amount of monies raised by the fundraising companies, and not simply the net balance that was eventually turned over to it by the fundraising companies. Similarly, the directors of the AIDS Society have a similar fiduciary duty to account for all of the monies raised by the AIDS Society from the public and to utilize such monies to further the objects of the AIDS Society as a charitable institution.

   Without commenting upon whether or not entering into the fundraising agreements were in fact a breach of fiduciary duty, the Court was careful to point out that a fiduciary relationship can be breached whether or not a loss occurs. As a result, the fact that a charity and its board of directors may have entered into an improvident fundraising contract may in and of itself be a breach of their fiduciary relationships to the public, regardless of whether or not any loss subsequently occurs.

2. The Court found that the contract entered into between the AIDS Society and the fundraising companies established a principal/agent relationship. This means that the actions of the fundraising companies are deemed to be the actions of the AIDS Society as its agents, thereby exposing the AIDS Society to liability as the principal. As agents of the AIDS Society, the fundraising companies had a duty to account for the monies received by it on behalf of the AIDS Society, although not necessarily a fiduciary duty. The Court stated that upon the passing of accounts, aspects of a developing fiduciary relationship between the fundraising companies and the Aid Society would likely become clearer in relation to the duty of the fundraising companies to account for the monies raised from the public on behalf of the AIDS Society.

The Court explained that there is a fiduciary obligation placed upon the AIDS Society and its directors to apply the monies raised from the public for the purposes of the AIDS Society. However, there is no legal relationship between donors and the fundraising companies, their canvassers, and/or their unit/crew managers.

3. As agents of the AIDS Society, the fundraising companies have a duty to account for the gross amounts of monies raised as donations from the public and not simply the net amount that was to be paid to the AIDS Society by the fundraising companies pursuant to the terms of the fundraising contracts.

4. In relation to the question concerning whether the fundraising contracts were either void or voidable as being contrary to public policy or for any other reason, the Court indicated that Courts in the past have been normally loath to interfere with freedom of the parties to enter into contracts. However, given public charitable giving, the nature of the administration of charitable property, and the fact that donors were not advised that between 70% to 80% of the donations would be deducted for expenses, the Court held that the fundraising contracts could be voidable as being contrary to public interest. The voidability of the contracts would be based upon breach of public policy, as well as misrepresentation to donors concerning the amount of money raised that was actually going to fulfil the charitable purposes of the AIDS Society.

5. Although the Court recognized that the failure of the AIDS Society to comply with the 80/20 disbursement quota might be a material factor to be considered by the Court, the Court held that there was no evidence available before it to determine whether or not the disbursement quota under the *ITA* had been complied with. Therefore, the Court declined to comment upon the impact of the 80/20 disbursement quota rule in relation to the AIDS Society.

The following implications can be drawn from the decision of the Court in the AIDS Society case:

1. Although the Court confirmed that unrestricted gifts to charities are owned by the charity beneficially and not held in trust for the charitable purpose of the charity, the charity still has a fiduciary obligation to apply the gifts received for its charitable purposes. As a fiduciary, a charity has some of the characteristics of a trustee, including the responsibility to account for the application of funds that it receives from the public.

2. A charity is responsible as a principal for the actions of its fundraiser, and any sub-contractors of the fundraiser, as agents of the charity. A charity cannot avoid responsibility for its fundraiser by describing it as an independent contractor.

3. If a charity engages fundraisers for the purpose of soliciting funds, regardless of whether or not the fundraiser is entitled to receive some portion of the funds raised, the charity is responsible to account for the gross amount of all donations received from the public and not simply the net amount payable to the charity in accordance with the contract with the fundraisers.

4. The charity, as principal, has the power to require the fundraiser, or sub-contractors of the fundraiser, to account for the full amount of monies that the fundraiser has raised, and the charity must do so in accordance with the fiduciary relationship between the charity and the public.

5. The directors of a charity stand in a fiduciary relationship to a charity akin to that of a trustee. Therefore, directors have a fiduciary relationship not only to the charity but to the public at large. Directors of charities are personally responsible to account for all monies raised by its fundraisers and their sub-contractors.

6. Exposure to liability by the charity and its board of directors is not limited to only losses of charitable monies. Rather, the fiduciary relationship will have been breached if the charity and its directors are found to have entered into a contract which may tend to cause a prejudice to the charity.

7. Directors of a charity must therefore proactively review, approve and oversee all fundraising activities of a charity, including the terms of contractual relationships with professional fundraisers.

8. Although there is a distinction at law between a charity receiving unrestricted gifts as property that it holds beneficially for its charitable purposes and gifts received in trust for specific charitable purposes, given the fact that a charity and its board of directors have a fiduciary obligation to the public to apply the funds received for its charitable purposes, there is little difference in a practical sense. A finding of a breach of fiduciary duty by a charity and its board of directors could be every bit as damaging as a finding of a breach of trust.

9. Given the fiduciary obligation of a charity and its board of directors to apply donations received by a charity for the stated charitable objects of the charity, it is essential that a charity carefully review its charitable objects on a regular basis and revises and/or expands them as necessary, i.e. to include the ability to make donations to other qualified donees.

10. Given that a fundraising contract can rendered voidable if there had been misrepresentation to the public by fundraisers who do not disclose fundraising costs, the determination of the fiduciary obligation between the charity and its donor is a subjective one in the minds of the donor, i.e. what did the donor think that the donation would be used for. As a result, it is essential that a charity review all aspects of fundraising literature and communication to determine what impression is left with the donor concerning the application of donations by the charity. This

determination of the reasonable interpretation by a donor concerning how the funds would be used will become the standard by which the charity and its board of directors in the future will be called to account in relation to the fulfilment of their fiduciary duty.

Based upon the directions given by the Court, the PGT proceeded with a judicial passing of accounts of the AIDS Society on May 9th, 2002. The Judgment consists of answers to various questions that were put to the Court. As only answers to questions are available instead of a full judicial decision, the significance of the Judgment lies more in conclusions that can be drawn from the monetary impact of the answers to the questions than in any substantive comments that might add to what the Court had said in its earlier decision.

The questions put to the Court and answers provided are summarized below, together with a commentary on the implication of the Court's answers:

1. The Court was asked whether the fundraising contracts between the AIDS Society and the two fundraising companies were void for being contrary to public policy. In this regard, it was alleged by the PGT that the contracts should be found void because the percentage of fundraising costs was unreasonable. The Court answered that the contracts were indeed void as being contrary to public policy because the fundraising contract provided that seventy to eighty percent (70%-80%) of the proceeds were to be paid to the fundraising company. The consequences of this decision are significant for charities, their directors, and third party fundraising companies where the payment under a fundraising contract entitles the fundraising company to receive a high percentage of the donations, i.e. 70%. It is not clear whether other similar fundraising contracts would be found to be void as being contrary to public policy. However, given the judicial pronouncement in this case and in the *Ontario Public Guardian and Trustee v. National Society for Abused Women and Children* (hereinafter "*National Society for Abused Women and*

Children")[15] case there is a distinct possibility that other similar types of fundraising contracts might be found void by the courts. It would therefore be important for both charities and third-party fundraising companies to carefully review the terms of their fundraising contracts to ensure that the resulting percentages of fundraising costs will not be found objectionable in the opinion of the Court, or in the alternative, to seek direction of the Court if there is uncertainty in this regard.

2. The Court was next asked whether the fundraising contracts, if not found void based on unreasonable fundraising costs, would be void as being contrary to public policy because of a violation of the 80/20 disbursement quota under Section 149.1 of the *ITA*. The Court declined to answer this question, since the Court had already determined that the fundraising contracts were void. However, the fact that the PGT had submitted to the court that non-compliance with the 80/20 disbursement quota might void a fundraising contract on this basis will mean that charities and their directors will need to determine whether there is compliance with the 80/20 disbursement quota in relation to fundraising expenses, an issue that is not always easy to get clarity on.

3. Having found that the fundraising contracts were contrary to public policy, the Court was next asked what percentage of the disbursement paid by the AIDS Society to the fundraising companies were reasonable fundraising costs that could be kept by those companies. The Court answered that none of the fundraising costs were reasonable. Whether this blunt response was based on the fact that no monies had been used for the charitable purpose of the AIDS Society or because the percentage of fundraising costs was excessive is not clear. However, what is evident is that where fundraising contracts are found to be void, the Courts may have no alternative but to find that all of the fundraising costs, even those at a lower percentage, are unreasonable and cannot be found to be justified. In other words, too high of a percentage share of fundraising proceeds may result in voiding all of the fundraising costs, not just the

[15] [2002] O.J. No. 607 (Sup. Ct. Jus.) [hereinafter "*National Society for Abused Women and Children"*].

fundraising costs above an acceptable amount, whether that reasonable amount is determined to be the statutory 20% provided for under the 80/20 disbursement quota under the *ITA* or some other percentage.

4. Having found that the fundraising contracts were void as being contrary to public policy and that no fundraising costs or disbursements in the accounts were acceptable as reasonable fundraising costs, the Court was then asked to determine whether the AIDS Society and its three (3) directors were liable for the amount of disallowed disbursements. The Court answered that both the AIDS Society and all three of its directors were liable for the disbursements and determined that the amount of unreasonable fundraising costs that they were liable for was $736,915.71. This liability was joint and several to each of the directors. What is important to note is that the breach of the directors' fiduciary duty arose from the fact of having entered into an imprudent contract, not from any conflict of interest or any personal benefit they might have received from the transaction, as was the situation in the *National Society for Abused Women and Children* case. Instead, the directors of the AIDS Society were personally liable for all of the fundraising costs even though there was no evidence that they had received any personal benefit whatsoever from the objectionable fundraising arrangements.

5. The Court was then asked whether the two fundraising companies were liable for the unreasonable fundraising costs along with the AIDS Society and its directors. The Court answered that the fundraising companies were liable on a joint and several basis with the AIDS Society and its directors. Given the Court's extension of liability to the fundraising companies to repay fundraising costs they had received, third party fundraising companies will now have a vested interest in ensuring that their fundraising contracts are acceptable to the Courts and to the PGT for their own protection, in addition to ensuring that fundraising contracts are legal from the standpoint of their clients.

6. The Court was then asked whether or not the matter was an appropriate case to impose a penalty by way of a fine upon the AIDS Society and the fundraising companies pursuant to Section 4(k) of the *Charities Accounting Act* ("*CAA*").[16] In this regard, section 4(k) of the *CAA* provides as follows:

> "(k) imposing a penalty by way of fine or imprisonment not exceeding twelve months upon the executor or trustee for any such default or misconduct or for disobedience to any order made under this section;"

The Court answered the question by imposing a $50,000.00 penalty upon the directors of the AIDS Society, but surprisingly did not do so to either the AIDS Society or the fundraising companies. The decision not to impose a penalty upon the AIDS Society likely reflects the fact that the AIDS Society did not have any assets. The fact that the directors of the AIDS Society were the ones held liable for the $50,000.00 penalty underscores the fact that, at the end of the day, where a charity itself is held liable at law for a matter, the directors of the charity will generally be held to account personally where the directors have failed in their duties to adequately manage and protect the charitable property entrusted to them.

7. The final question that the Court was asked to determine was "what should be done with the $37,935.50, which the Court was holding in trust." The Court decided that those monies would be paid between two (2) charities presumably having similar charitable purposes to the AIDS Society in accordance with the "cy prés" jurisdiction that the Courts have over charitable property, i.e. to apply the property as "near as possible" to its original charitable purpose.

Given the devastating financial consequences to the directors of the AIDS Society on a personal basis from having authorized unreasonable fundraising contracts, this case will no doubt result in directors and charities now wanting to carefully review contracts entered into

[16] R.S.O. 1990, c. C-10.

with third party fundraising companies with their legal counsel in order to ensure that the contracts comply with the Courts' expectations. In addition, directors of charities may also need to look at the fundraising costs associated with retaining fundraisers as employees as well, since the Court did not draw any distinction between the cost of third party fundraising arrangements and employing fundraisers in relation to determining what are reasonable fundraising costs.

As many charities that retain third party fundraising companies or employ professional fundraisers may have difficulty meeting the 80/20 percent disbursement quota required under the *ITA* with regard to fundraising costs, there would now appear to be cause for concern by directors of such charities, particularly since directors could be faced with personal liability for having permitted unreasonable fundraising costs. However, since the courts in Ontario have not articulated what are reasonable fundraising costs, it is difficult for directors of charities, as well as third party fundraising companies, to know what will be acceptable to the Court. In this regard, it may be in the best interest of charities, directors, and third party fundraising contractors to have the matter clarified, either through the introduction of fundraising legislation in Ontario or by an application for directions from the Courts to determine the viability of normal third party fundraising contracts which involve fundraising costs that exceed twenty (20%) percent of the donations received.

Until this matter is clarified, either through legislation or through judicial interpretation, charities which raise funds in Ontario will continue to face considerable uncertainty in fundraising. This uncertainty may also impact on third party fundraising contracts elsewhere in Canada, given the fact that courts in other provinces will often follow Ontario decisions. This possibility is now particularly relevant in the Province of Saskatchewan where the new *Charitable Fundraising Businesses Act*, partially in force since July 15, 2002, permits a charity to apply to a court to obtain an order declaring a fundraising contract void for being contrary to public policy.

The issues raised in the AIDS Society case are ones that charities, directors of charities, their legal counsel, and third party fundraising companies will need to closely monitor instead of dismissing as an anomaly.

(2) The *National Society for Abused Women and Children* Case

In another third-party fundraising contract case, *National Society for Abused Women and Children,* the Court came to many of the same conclusions as in the *Aids Society for Children (Ontario)* case. The case involved three individuals who incorporated the National Society for Abused Women and Children (the "Society") in 1999, subsequently arranged for the Society to obtain charitable status, and then entered into fundraising contracts with businesses that the directors of the Society either owned or were employed by. The fundraising efforts for the Society raised close to $1,000,000.00, but only $1,365.00 made its way to charitable work. The fundraising contracts provided for percentage commissions of between 75% to 80% of the gross funds raised, together with additional monthly administrative fees on one of the contracts of $1,500.00 per month.

The Court found that the fundraising contracts were void *ab initio,* as the amount of compensation paid to the fundraising companies under the contracts was found to be unconscionable. This resulted in the Court requiring the directors of the Society to pay all monies that they had received from the Society through the fundraising companies over to the PGT. Once the monies had been paid over to the PGT, then the directors could seek compensation, but only if such claims for compensation were properly documented and received, subject to approval by the Court.

Given the brevity of the decision, the intensity of the comments by the presiding Judge, and the serious consequences arising from the Court's decision for charities in Ontario, the decision is set out in its entirety below, followed by a commentary on some of the practical implications of the decision.

"IN THE MATTER OF NATIONAL SOCIETY FOR ABUSED WOMEN AND CHILDREN" - LOUKIDELIS, J.

1. A distinct odour emanates from the facts of this case.

2. The ability and swiftness by which the main principals or indeed anyone acting within the system can extract from trusting citizens a large amount of money is rather stunning.

3. Here the 3 main principals Perrin, Corriero and Dobbs without any background training or expertise in child or women abuse, but only a stated desire "to give something back", obtained a charter for a non-profit organization, the objects of which were to "promote awareness…and to assist abused women and children". The 3 named were the first directors. The corporation was given a high sounding name. The charter was issued March 2, 1999. Its objects were approved by the applicant and it was registered as a charitable organization. They were then ready to do business.

4. Thereafter, they proceeded without advice to break statutory, common law and common sense rules, mixing their personal interest with those of the Society in a totally inappropriate manner.

5. The laudable objectives were used as a cover to raise from unsuspecting donors close to 1 million dollars of which $1,365 actually found its way to a deserving charity.

6. Thanks to the vigilance of the press the Society's fundraising methods and the conduct of its directors was brought to the applicant's attention resulting in this application.

7. The Society entered into 3 separate fund raising contracts between March 1999 and March 2000, all of which were shocking, paying to the collecting agency 75 to 80% of gross receipts.

8. The first was Community Fundraising Consultants, a now defunct company where Corriero and Dobbs at the time were both employed. This was an obvious conflict of interest that all 3 directors should have known.

9. There was no indication that the directors searched for other agencies with better rates. The suggestion that other new charities engaged this type of collector is not a valid answer.

10. The second contract was with a partnership known as Canadian Care Marketing Associates – the partners being Perrin and Corriero. While the commission was 75% rather than 80% of gross receipts there was an additional $1,500 monthly charge.

11. Contrary to Perrin's evidence I am satisfied that at the time that contract was signed, Perrin and Corriero were still directors of the Society; a clear conflict of interest and breach of their fiduciary duty as directors of a charitable organization. I note also that this contract was for 3 years which places in considerable doubt their now stated position that the contract was a temporary measure until a data base of contributors had been established.

12. The third contract was with OFC Charity Call Centre.

13. The whole operation was a scheme whereby charity was used as a cover to raise money for the benefit of the collection agency.

14. While the principals did collect some clothes and toys and distributed same, these items were donated to them at no cost. They were careful also to collect some thank you letters.

15. Mr. Andreou raised a spirited argument on behalf of the respondents. I cannot accept that the principals were naïve or that this is the accepted and appropriate manner of doing things for new charities.

16. Corriero and Perrin profited in numerous ways because of their conflicts and by breaching their fiduciary duties as directors. They had no right while directors, or after, to charge food and car expenses to the Society. Perrin's claim for reimbursement of a loan is undocumented.

17. They also charged partnership expenses to the Society when they carried on their business from the same location as the charity.

18. The inappropriateness of their conduct is more particularly set out in the detailed letter of administrative fairness from Revenue Canada dated September 29, 2000.

19. Ms. Dobbs also received a personal benefit by way of expenses which was improper.

20. These 3 principals particularly Corriero and Perrin, treated the Society as a personal fiefdom with a nice treasury for their own purposes.

21. I am not prepared, therefore, to approve the Society's accounts as stated.

22. Each of the 3 principals should repay all monies received from the Society if demanded by the applicant. Upon submitting proper documentation in support to their claims, approval by the Court may be granted after which they will be paid by the applicant from funds ordered to be returned.

> 23. If there is a dispute as to the amount owing by each, the applicant may arrange to reattend before me to determine the amount from the material already filed.
>
> 24. The contract between Canadian Care Marketing Associates (CCMA) and the Society was obviously improper at the time and was, I find, void ab initio. The profit shown by CCMA on its filed statement of some $28,000 should also be paid to the applicant by Corriero and Perrin.
>
> 25. Turning now to the issue of the collection agencies. Their share of 75 - 80% of gross receipts if known, is bound to shock the conscience of any citizen. If any prospective donor knew the true facts, I doubt that a penny would have be given. They claim to speak for a charity, but are careful not to reveal what the charity will receive. The main beneficiary is the collection agency. If not an outright fraud, it is clearly wrong.
>
> 26. Every charitable donor expects a charity to have some administrative costs. But in circumstances like this where the actual amount used for charitable purposes was a fraction of 1%, it is clearly unconscionable.
>
> 27. Some mechanism should require canvassers for such collection agencies to be forthright in divulging collection and administration costs.
>
> 28. If any funds are collected as a result of my order, the applicant hopefully might distribute same to authorized shelters in the areas where these funds were collected.
>
> 29. The Society as well as the respondents or their agents are prohibited from seeking further donations from the public on behalf of the Society.
>
> 30. Also the respondents Corriero, Perrin and Dobbs are prohibited from acting as directors of any other charitable organization until the accounts of the Society have been approved."

The practical consequences of the *National Society for Abused Women and Children* decision are summarized below as follows:

1. The intensity of the comments by the Court reflect the offensive nature of the facts involved in the case. The Court found that the whole *modus operandi* was "*a scheme whereby the charity was used as a cover to raise monies for the benefit of the collection agency*". However, the decision is not limited to the specific fact situation

involving this particular charity but has application to any charity that fundraises by utilizing third party fundraising companies.

2. The Court found that the compensation to third party fundraisers of 75% to 80% of the gross receipts for the donations was unconscionable and would "*be bound to shock the conscience of any citizen*". These comments were made notwithstanding that legal counsel for the three directors of the Society argued that the fundraising practices for the Society were similar to those carried out by other new charities and were done for purposes of establishing a database for future contributions. This would suggest that the Court will compare fundraising expenses to the gross amount of donations received in the same year, instead of amortizing those expenses over a number of years to reflect the long term benefit of the fundraising database that was being established.

3. The Court found that the three directors of the Society were in a clear conflict of interest when they arranged for the Society to enter into contracts with fundraising companies that were either owned by them or employed by them. The Court held that by entering into these contracts, the directors breached their fiduciary duty as directors of the Society. For background information concerning the common law rule prohibiting remuneration of directors of charities, as well as a discussion of the decision by the PGT not to introduce regulations to permit remuneration of directors.[17] The practical difficulty that can arise from conflicts of interest where directors receive, either directly or indirectly, remuneration from a charity is made all the more problematic in extreme fact situations such as the one in this case.

4. Once the Court identified that the directors of the Society were in conflict of interest by directing the Society to enter into the fundraising contracts, the Court went on to require that the directors account for all monies that they had received from the

[17] See *Charity Law Bulletin No. 2* dated March 20, 2001, and an article entitled "*Remuneration of Directors in Ontario and Update of Remuneration of Directors in Ontario*", available at www.charitylaw.ca.

fundraising companies that they either owned or were employed by. This aspect of the decision underscores that where directors of a charity are found to be in breach of their fiduciary duties, the directors will personally be liable to repay the monies that they have received back to the charity, whether such monies have been received directly or indirectly, including monies received through fundraising contracts.

5. The Court also confirmed the fiduciary duty that directors in Ontario have to disclose unreasonable fundraising costs to donors. This decision of the Court is similar to the position taken by the Court in the *Aids Society for Children (Ontario)*, discussed above, in which the Court held that directors of a charity have a fiduciary obligation to disclose fundraising costs to donors where such costs exceed 70% of the gross receipts. In *National Society for Abused Women and Children* decision, the Court was particularly critical of the fundraising arrangement that allowed a fundraising company to "*speak for the charity*" and receive 75% to 80% of the gross receipts, but failed to disclose what those costs were and what the charity was actually receiving. This aspect of the decision emphasizes that directors of a charity have a fiduciary obligation to ensure that fundraising expenses are kept within the reasonable expectations of donors. What the reasonable expectations on fundraising expenses are was not identified by the Court, nor was there any reference to the 80/20 disbursement quota rule required for registered charities under the *ITA*. However, what is clear from the decision is that fundraising administrative costs of 75% to 80% of gross receipts is much higher than what the Court was prepared to consider as reasonable in the circumstances.

6. The common law fiduciary obligation placed upon directors of a charity would appear to be in addition to the increasing legal obligations imposed upon directors by statute concerning fundraising, such as the requirements under the federal *Competitions Act*, the federal *Personal Information Protection and Electronic Documents Act*, and the proposed Ontario *Privacy of Personal Information Act*.

7. It is possible that the decision of the Court in the *National Society for Abused Women and Children* case, as well as the earlier decision in the *Aids Society for Children (Ontario)* case, may become the impetus for fundraising legislation in Ontario similar to what has been put in place in other provinces, such as Alberta. Whether the provincial Government, the charitable sector, or the third party fundraising community will take the initiative in this regard remains to be seen.

The National Society for Abused Women and Children decision is important for the numerous observations, findings and conclusions of the Court concerning the inappropriateness of fundraising activities carried out by the Society, as well as the recognition that the PGT will not hesitate to seek an order for a judicial passing of accounts under the *CAA* where fundraising arrangements are considered to be patently unreasonable. It will now be more important than ever for charities that are fundraising in Ontario to be diligent in ensuring that they not only comply with statutory requirements involving fundraising, but also comply with common law fiduciary duties imposed upon directors of charitable corporations in relation to the expectations of donors concerning reasonable administrative expenses involved in fundraising. It is clearly a new day in Ontario, and possibly across Canada, for charitable fundraising that will need to be closely monitored by charities, their directors, legal counsel who advise them, professional fundraisers, as well as the third party fundraising community.

As discussed later in this paper, there are serious legal consequences that directors may face if they allow a charity to become involved in an improper fundraising practice. Those consequences range from breach of trust, public inquiries under the *Public Inquiry's Act*[18], as well as a court ordered audit under the *CAA*. As a result, it is essential that the board of directors of a charity understand that it has both a legal obligation as well as a vested personal interest in ensuring that the fundraising programs undertaken by a charity are carefully scrutinized in order to evidence that the board of directors has exercised the due

[18] R.S.O. 1990, c. P-41.

diligence required of it in its fiduciary capacity to manage and protect the charitable property that has been entrusted to it.

In light of this legal responsibility, directors of charities need to become pro-active in establishing policy guidelines for fundraising programs and then carefully monitor and evaluate how those programs are being implemented on an ongoing basis. Similarly, professional fundraisers and management of charities need to be equally pro-active in ensuring that the board of directors of a charity are kept well informed about the fundraising programs that are being undertaken so that the directors will be able to identify and evaluate the legal risks involved in those programs. A director should actively oversee the organization's fundraising initiatives, for example, to ensure that its charitable organization complies with the terms of special purpose trust, discussed in more detail below. If not, all of the charities' directors may be in breach of trust, and liable for the loss incurred both in their personal capacities and as a group.[19] Ultimately, the "buck stops" with the board of directors of a charity. It is therefore essential that fundraisers and management of a charity respect this fact in the nature and thoroughness of their communication and interaction with the board of directors.

C. The Danger of the "Follow the Leader Syndrome" in Fundraising

Part of the problem associated with the increasing legal liability involved with fundraising programs is the presumption that if one charity has already undertaken a particular fundraising program, then it must be "OK" for another charity to "follow the leader." This trend often extends not only to the second charity adopting the same program as the initial charity, but even to the point of the second charity copying the specifics of the program word for word.

The inherent problem, though, with the "follow the leader syndrome" in fundraising is that no one involved with the first charity may have conducted an appropriate "due diligence" review of the

[19] Peter Broder, ed., *Primer for Directors of Not-For-Profit Corporations (Rights, Duties, and Practices),*, (Ottawa: Industry Canada, 2002), pp. 19¸ and 20.

legal liability or the appropriateness of the fundraising program in question. Some of the problems that can occur when a charity simply copies the fundraising program of another charity without conducting its own "due diligence" review may include some, if not all, of the following:

- The fundraising program in question may have originated from the United States and been adopted in Canada without taking into account the differences in the statutory regimes between the two countries. For instance, a charitable gift annuity or a forgivable debt instrument may be dealt with very differently in the United States under state and U.S. federal law from how it would be dealt with in Canada under provincial and federal law on matters such as insurance and income tax. Notwithstanding these obvious differences, some charities, particularly smaller and less sophisticated ones that operate in effect as "branches" of the U.S. "parent" charity may be tempted to simply photocopy fundraising materials that have been successfully used in the U.S. for use in Canada.

- The corporate objects and powers of one charity may be very different from those of another charity. Such differences may limit the ability of one charity to adopt the fundraising programs of another charity. For instance, just because one charity has specific corporate power to issue annuities does not mean another charity will have similar corporate authority to do so, not to mention having to comply with provincial insurance legislation, discussed later in this paper.

- Even if a legal opinion has been obtained by one charity concerning the legality of a fundraising program, that legal opinion will not have application to another charity, even if a photocopy of the legal opinion has been given by the first charity to a subsequent charity. The fact that charities may copy legal opinions and distribute them between themselves underscores the importance of a lawyer who is giving a legal opinion on a fundraising program to ensure that such opinion is clearly marked "private and confidential", and is coupled with a statement that the legal opinion cannot be relied upon by any other person or organization without the written permission of the author.

- Even if a fundraising program is determined to comply with all applicable law, it may not be practical for another charity to undertake the same program, due to the inexperience or size of that charity. For instance, although an endowment program would be an effective means of developing long term stability for a charity, the ability of a small charity to properly manage and invest multiple endowments on a perpetual basis may not be realistic or advisable in the circumstances.

An instructive illustration of what can go wrong when a fundraising program is not properly evaluated can be found by examining the "New Era Scandal" that occurred in the United States in

1995. For a discussion of the "New Era Scandal" that eventually became the largest charity fraud in U.S. history, reference can be made to an article by the author dealing with the lessons to be learned in Canada from the U.S. experience, a copy of which is attached to this paper at Appendix 4.

In summary, the "New Era Scandal" involved a matching gift program initiated by the New Era Foundation in Boston that promised to double investments from participating charities within six months. A number of prominent charities in the United States, including some large religious charities, as well as a number of high profile philanthropists, including Laurance S. Rockefeller, the brother of David Rockefeller, and Sir John Tempelton, "invested" collectively more than $250,000,000.00 in the New Era Foundation. However, after an accountant from one of the participating charities questioned the proprietary of the program and eventually called in state and federal authorities, it was found that the New Era Foundation was nothing more than an elaborate "ponzi scheme", i.e., a scheme where new monies being deposited were being used to pay out past promises after the scheme organizers had "skimmed" some of the monies for themselves.

Although much of the lost investment monies were eventually recovered, due to a voluntary adjustment by charities that received net gains with those charities that suffered net losses, there were still considerable losses incurred by numerous charities amounting to tens of millions of dollars. The founder of the New Era Foundation was indicted on 82 counts of fraud and tax evasion and eventually sentenced to twelve (12) years in prison.

As the attached article explains, one of the lessons to be learned from the collapse of the New Era Foundation is that if a fundraising program appears to be "too good to be true", it probably is, and just because another charity is undertaking a fundraising program, even if it is a large and well known charity, that does not necessarily mean that other charities should blindly follow. In addition, the New Era scandal emphasized the importance of allowing management staff, including professional fundraisers, to raise questions about the propriety of a fundraising program without fearing that they are at risk of losing their jobs or their professional reputations. It is important that internal accountability be encouraged and that individuals who might otherwise be labelled as "whistle blowers" are not deterred from taking reasonable steps to question and evaluate all aspects of a fundraising program in accordance with the fiduciary duty placed upon both directors and employees of a charity.

D. Developing a Pro-Active Legal Risk Management Approach to Fundraising

Given the increase in legal risks associated with charitable fundraising, it is incumbent upon charities, their boards, staff, and legal counsel to become "pro-active" in identifying and minimizing such legal risks whenever possible.[20] The type of consideration involved in implementing a "pro-active" legal risk management approach to fundraising is summarized below:

- The charity should stop and evaluate the legal risks involved in a fundraising program before the program is implemented, expanded or continued.

- The charity should be encouraged to obtain appropriate professional, legal and accounting advice as necessary, rather than expecting management, staff or professional fundraisers to provide advice outside their areas of expertise.

- A legal review or "audit" of a new or potentially problematic existing fundraising program should be conducted and an opinion obtained to evidence due diligence by the board and management of the charity.

- The charity should develop and comply with an appropriate standard of conduct for fundraising in accordance with sample codes established by umbrella organizations, such as the Canadian Centre for Philanthropy, the Canadian Association of Gift Planners or the Association of Fundraising Professionals.

- In the event that legal risks are identified through a legal review or audit, those risks should be communicated to the board of directors, who would then need to decide whether or not such legal risks are acceptable and reasonable in the circumstances, keeping in mind the responsibility of the board of directors to exercise a fiduciary duty of prudence in managing the charity's property.

- The board of directors should be informed of its legal obligations to oversee charitable fundraising and the directors' exposure to personal liability if they do not exercise due

[20] For a more detailed discussion of what "pro-active legal risk management advice" involves, see Terrance S. Carter, "Advising the Charitable Client: Pro-Active Legal Risk Management Advice" in *Law Society of Upper Canada, Special Lectures* (Toronto: Carswell, 1996) at 267 (also available at **www.charitylaw.ca**)

diligence in protecting the charitable property of a charity or in ensuring that the rights of a donor have been adequately protected.

3. FUNDAMENTAL LEGAL CONSIDERATIONS INVOLVED IN FUNDRAISING

A. Fundraising is Not an End in Itself

The Public Guardian and Trustee of Ontario, in its 1998 edition of the *Not-For-Profit Incorporators Handbook*, explains its concern that fundraising should not become an end in itself:

> Fundraising is not, of itself, a charitable purpose. It is, however, permissible as one of the incidental and ancillary powers of a charity. Where the fundraising activities of the charity become a purpose, or where fundraising becomes a means of providing a livelihood for members or managers, serious concerns obviously arise as to whether the organization is, in fact, established and operating exclusively for purposes charitable in law.[21]

While the ability of a charity to carry out fundraising activities could arguably be inherent from the incidental corporate powers of a corporate charity, it is advisable to include a specific fundraising power clause in the letters patent for the charity, whether incorporated federally or provincially. However, whether fundraising could ever be elevated into a secondary charitable purpose for a charity is unlikely, since in doing so, the means of achieving the charitable purposes of a charity would have become an end in itself.

B. Fundraising Must Comply with the Applicable Corporate Objects and Powers of the Charity

A fundamental requirement of any charity involved in fundraising is that all fundraising activities carried out by a charity must fall within the authorized charitable purposes or ancillary power clauses of the charity as set out in its letters patent or special incorporating legislation, failing which such fundraising activity might be declared void as being *ultra vires* the corporate power of the

[21] Ministry of Consumer and Commercial Relations and The Office of the Public Guardian and Trustee for Ontario, *Not-For-Profit Incorporators Handbook*, (Toronto: Queen's Printer for Ontario, 1998) at 62.

charity[22]. This in turn could leave the board of directors exposed to the possibility of personal liability.

Some situations were the doctrine of ultra vires could impact the fundraising programs of a charity are summarized below as follows:

(1) The Fundraising Program Must Not Be Ultra Vires

A charity must be careful to ensure that there is the requisite corporate authority to carry out the fundraising program being undertaken. For instance:

- A charity may not have the corporate authority to issue self insured annuities.
- A charity may not have the corporate authority to enter into a joint venture or partnership arrangement with a business sponsor.
- A charity may not have the corporate authority to hold charitable property in trust for other charities.
- A charity may not have the corporate power to manage investment funds on behalf of other charities.

(2) The Charitable Purpose Being Furthered by Fundraising Must Not Be *Ultra Vires*

Although identifying the charitable purpose for which monies are being sought will often assist in promoting a fundraising program, it is important that the charity ensure that such charitable purpose falls within the authorized charitable objects of the charity as set out in its letters patent, supplementary letters patent, or incorporating legislation. For instance, a charity that is authorized to operate a counselling service for terminally ill patients may not have charitable objects that are broad enough to authorize the construction and operation of a hospice and/or a respite centre. The personal risk to directors that can result in establishing and operating an *ultra vires* charitable program underscores the importance in having the

[22] For a discussion of the doctrine of *Ultra Vires*, with non share capital corporation, see *Stanishewski v. Tkachuk* [1955], O. R. 67, [1955], 4 D.L.R. 517 (Ont. S.C. (High Crt. of Justice)); *Berry v. Indian Park Association* (1999), 44 O.R. (3d) 301. (Ont. C. A.).

directors, management and fundraisers of a charity become familiar with the applicable constating documentation that sets out its charitable purposes.

Where a charity does not have the requisite charitable purposes to carry out the charitable program from which monies are being raised, it would be incumbent upon the directors of such charity to seek directions from the court on a *cy-prés* application concerning how such funds should be applied, failing which the court might order that the funds be returned to the donors. The responsibility upon directors to seek court directions in such situations is discussed later in the paper.

(3) A Donor Restricted Gift From Fundraising Must Not Be *Ultra Vires*

Where a charity accepts a gift resulting from a fundraising effort that is subject to a binding donor restriction, it is important that the charity first determine whether or not the donor restriction to be complied which falls within the charitable objects of the charity. If the charity agreed to accept a gift that was subject to a restriction that the charity did not have corporate authority to carry out, the charity would be acting *ultra vires* in doing so and would be exposing the directors to personal liability. A discussion concerning practical steps that can be taken by a charity to avoid liability involving donor restricted gifts is set out later in this paper.[23]

C. Fundraising Must Not Violate Applicable Statutory Provisions

In addition to having to operate within the applicable corporate objects and powers of a charity, a charity will also need to ensure that any specific or general legislation affecting either the charitable or fundraising programs of a charity are complied with. While it is beyond the scope of this paper to provide anything more than a cursory overview of the applicable statutes, a few of the more important provincial and federal acts that should be taken into consideration are listed below:

[23] For a more complete discussion of the legal issues involving donor restricted charitable gifts, see "Donor Restricted Charitable Gifts: A Practical Overview Revisited", by Terrance S. Carter in *The Philanthropist*, Vol. 18, No. 1 (September 2003) and Vol. 18, No. 2 (December 2003).

(1) Specific Charitable Statutes Affecting Fundraising

- the *Charities Accounting Act* of Ontario;
- the *Charitable Gifts Act*[24] of Ontario;
- the *Income Tax Act*;
- the *Charitable Fund-Raising Act*[25] of Alberta;
- the *Charities Endorsement Act*[26] of Manitoba;
- the *Religious Organization's Lands Act*[27] of Ontario;
- the *Charities Act*[28] of Prince Edward Island; and
- the *Charitable Fund-raising Businesses Act* of Saskatchewan[29];
- the *Taxation Act* of Québec.[30]

(2) General Statutes Affecting Charitable Fundraising

- the *Insurance Act*[31] of Ontario;
- the *Loan and Trust Corporations Act*[32] of Ontario;
- the *Securities Act*[33] of Ontario;
- the *Business Names Act*[34] of Ontario;
- the *Trustee Act*[35] of Ontario;
- the *Competitions Act*[36];
- the *Personal Information Protection and Electronic Documents Act*[37]; and
- *Charities Registration (Security Information) Act*[38].

[24] R.S.O. 1990, c. C-8.
[25] R.S.A. 1995,c. C-45, as am.
[26] R.S.M. 1993, c. 41, s. 10, as am.
[27] R.S.O. 1990, c. R-23.
[28] R.S.P.E.I. 1994, c.48, s.4, as am.
[29] R.S.S. 2002, c. C-6.2, as am.
[30] R.S.Q, c. I-3, as am.
[31] R.S.O. 1990, c. I-8, as am.
[32] R.S.O. 1990, c. L-25, as am.
[33] R.S.O. 1990, c. S-5, as am.
[34] R.S.O. 1990, c. B-17, as am.
[35] R.S.O. 1990, c. T-23, as am.
[36] R.S.C. 1985, c. C-34, as am.
[37] 2000, c. 5.

D. Fundraising Must Not Involve Gifts that are Contrary to Public Policy

(1) Charitable Gifts Involving Discrimination

A charitable gift that is otherwise charitable at law may be still found void as being contrary to public policy where the terms of the charitable program are found to be discriminatory on the grounds of race, colour, nationality, ethnic origin, religion or sex, as reviewed in the *Leonard Foundation Trust* case.[39]

The court, though, in the *Leonard* decision pointed out that not all gifts that are on their face discriminatory because they favour particular persons or group of persons will necessarily be found to be void as being contrary to public policy.[40] Where a charitable program is intended to support disadvantaged groups, such as qualifying students who would not otherwise be able to attend university without financial assistance, a gift to a program in such situations would not necessarily be objectionable to a point where it was considered to be so discriminatory as to be contrary to public policy. As a result, each program must be evaluated on a case by case basis. The court limited the scope of its decision in the *Leonard* case by stating that "*this case should not be taken as authority for the proposition that all restrictions amount to discrimination and are therefore contrary to public policy*".[41]

(2) Charitable Gifts Involving Illegal Activity

If the required means of accomplishing a charitable gift involves an activity which is on its face illegal, the gift will fail as being contrary to public policy. For instance, a gift to a bible society requiring that such monies be used to buy and deliver bibles into a country that the Canadian government had imposed a trade embargo against might be void as being contrary

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[38] Not enacted as of the date of revision of this article.

[39] *Canada Trust Co. v. Ontario (Human Rights Commission)* (1990), 38 E.T.R. 1, 69 D.L.R. (4th) 321 (subnom *Leonard Foundation Trust, Re*) (1987), 37 O.A.C. 191 (Ont. S. C. (C. A.)).

[40] *Ibid* at 26.

[41] *Ibid*. For further discussion of the impact of the *Leonard Trust* case, see Lalani, *infra,* note 46 at 49.

to public policy. If a gift is found to be initially void because it is illegal, it might be possible to vary the offending restriction through a *cy-prés* court application.[42]

4. DONOR'S RIGHTS AND REMEDIES IN FUNDRAISING

A. General Exposure to Liability Involving Donors

In discussing the extent of legal liability associated with charitable fundraising programs, it is important to keep in mind who it is that might be an aggrieved party and what remedies such aggrieved party may have against the charity and its board of directors. In this regard, the obvious, but not necessarily the only aggrieved party affected by an improper fundraising program would be the donor. Although the public has an overriding interest in fundraising in its role as an indirect beneficiary of all charitable purposes, the interest of the public is normally limited to the inherent jurisdiction of the court, as well as the *parens patriae* role of the Attorney General in dealing with charitable property through the office of the Public Guardian and Trustee in Ontario. Protecting the interests of the donor is normally not adequately addressed through the jurisdiction of the courts or the role of the Attorney General except in extreme situation[43]. Donors will therefore need to seek a more direct involvement to enforce their rights.

The general nature of liability exposure that a charity and its board of directors might face from aggrieved donors can be categorized into three general different situations, each of which is briefly summarized below as follows.

(1) Misrepresentation Involving Issuance of Charitable Receipts

The first situation involves donors who have made a gift to a charity expecting that they will be receiving a charitable receipt in a particular amount for the gift, only to find out later that a receipt is either not available, or if it is, the receipt is subsequently challenged by Canada Revenue Agency (formally known as "Canada Customs and Revenue Agency", hereinafter

[42] J. Warburton & D. Morris, eds,. *Tudor on Charities*, 8th ed. (London: Suite & Maxwell, 1995) at 395.
[43] See *The AIDS Society for Children (Ontario)*, *supra* footnote 14.

referred to in this paper as "CRA"). Alternatively, the amount shown in the receipt may not equate with the amount that the donor had expected. In either of these circumstances, the donor may decide to hold a charity liable for the loss or reduction in tax credits available to the donor. A claim in this regard could be based upon an allegation of negligent misrepresentation by the charity or its staff concerning the availability and\or the amount of the charitable receipt or other tax benefits that the donor had expected to receive.

(2) Failure to Comply with Donor Restrictions

The second situation is where a charity applies a gift in a manner that is different from what was directed by the donor, either because the gift is used contrary to the specific terms of the stipulated restrictions, or alternatively because the gift is applied in a way that is not in accordance with the donor's reasonable expectations of what the gift would be used for. The latter may occur, for example, where a surplus results from a fundraising campaign for a building program and such surplus is used for something other than the building program without the charity having disclosed such possibility to the donor when the fundraising was undertaken. Legal liability in this regard could result from allegations of breach of trust and/or negligent misrepresentation.

(3) Detrimental Reliance Upon Charitable Endorsements

The third situation involves the growing trend of charities to, either directly or indirectly, endorse the products and/or services of a business sponsor as discussed later in this paper. Legal liability in this situation may occur because the donor/purchaser of a product or service claims that the endorsement by the charity of the product or service which subsequently turns out to be defective or deficient was a major reason in why the donor/purchaser acquired the product or service in the first place. Such situation might allow the donor/purchaser to commence legal action against the charity and possibly its board of directors based upon allegations of detrimental reliance.

(4) Failure to Disclose Excessive Fundraising Cost

The Aids Society for Children (Ontario)[44] stands for the proposition that a charity and its board of directors have a fiduciary obligation to disclose to a donor the fundraising expenses that are grossly excessive when seeking a donation, as the case held that the a fundraising contract can be voidable for misrepresentation and breach of public policy.

B. Inherent Rights of Donors

In addition to the explicit exposure to legal liability from aggrieved donors, there is also the inherent moral, if not legal right, that charities, as well as directors and fundraisers owe to donors. Some of these inherent rights have been articulated in codes of ethical fundraising, such as the one prepared by the Canadian Centre for Philanthropy ("CCP") and attached as Appendix 1, as well as the "Fundraising Standards" adopted in Alberta under the *Charitable Fundraising Act* discussed later in this paper.

A non-exhaustive list of some of the more important inherent rights that donors may be entitled to are summarized below as follows. Whether or not all of the rights listed below would be recognized by a court remains to be seen.

(1) The Right to Disclosure

A donor should be entitled to full disclosure concerning the purpose of the fundraising, the costs associated with such fundraising, as well as whether the fundraiser in question is a paid fundraiser or a volunteer. *The Aids Society for Children (Ontario)* case imposed a positive duty on charitable fundraisers to disclose to the donors the cost associated with such fundraising, and the estimated amount going to the charity after deduction of the costs of the fundraising. Failure to disclose such information about grossly excessive costs may constitute a misrepresentation[45].

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[44] *Ibid.*
[45] *Ibid.*

(2) The Right to Transparency

A donor should be entitled to expect that the information provided about a charity or the fundraising program will be done in a manner that is transparent in allowing the donor to make an informed decision on whether to donate or not based upon an assumption that all relevant information concerning the fundraising program in question will have already been voluntarily given by the charity.

(3) The Right to Financial Information

A donor should be entitled to receive all relevant financial information necessary to make an informed decision concerning a donation and the charitable program that it will be used in conjunction with. This would involve the donor being entitled to receive a copy of the most recent financial statements of the charity, as well as an explanation of the cost of the project that the fundraising is being undertaken to fund.

(4) The Right to Protection from Undue Influence

A donor should be entitled to freedom from any form of direct or indirect undue influence in fundraising. This would include freedom from repetitive and persistent requests for funds, however made, particularly where such requests are being made of vulnerable individuals, such as the elderly. It would also include freedom from situations where a fundraiser or other representative on behalf of a charity intentionally develops a close relationship with a donor for the primary purpose of cultivating a source of trust and dependency between the donor and the fundraiser in order to facilitate a charitable gift.

(5) The Right to Expect Concern for the Donor's Well Being

To the extent that a relationship between donor and a charity is one where the donor is relying upon the charity for advice, there may be an obligation upon the charity to protect an overly eager donor from making a charitable gift to the charity if doing so would unduly overextend the financial resources of the donor or would otherwise not be in the best interests of the donor.[46] This is consistent with the *Aids Society for Children (Ontario)* case which held that the relationship between donors and involved charity in fundraising is a fiduciary relationship[47].

(6) The Right to Independent Legal Advice

Every donor has a "passive" right to obtain independent legal advice before making a gift. In some situations, though, there maybe an obligation placed upon the charity and its fundraisers to "actively encourage" the donor to seek independent legal advice. This "active" obligation may arise where there are specific income tax consequences unique to the donor that should be reviewed, where the type of fundraising vehicle being utilized involves an investment by the donor, such as a charitable gift annuity, where the donor is vulnerable, either due to health or age, or where the gift might negatively impact the donor's financial resources or the ability of the donor's estate to meet obligations to legal dependents.

(7) The Right to Compliance with Donor Imposed Restrictions

As discussed in more detail later in this paper, where a donor has imposed binding restrictions on a charitable gift, whether it be in relation to how the gift is to be used or if it is to be held in perpetuity as an endowment, the donor has an inherent right to expect that the terms of the restriction will be complied with by the charity and its board of directors.

(8) The Right to Confidentiality

Every donor should be entitled to confidentiality concerning their identity, and the nature of the gift that they have given, unless otherwise consented to. This would involve the right of

[46] Shamin Lalani, "Looking a Gift Horse in the Mouth" (1998) 14 *The Philanthropist* 42 at 48.
[47] *Supra*, footnote 14

a donor to be informed if a donor list is to be sold, rented or exchanged, together with a corresponding right to have his or her name removed from such list.[48]

C. Donor's Statutory Rights

In addition to the PIPEDA, as discussed above, some of the more important statutory rights that are available to aggrieved donors in Ontario are summarized below as follows:

(1) *Charities Accounting Act* (the "CAA")

The *Charities Accounting Act* of Ontario (the "*CAA*") contains a number of provisions that provide both direct and indirect statutory rights to donors concerning improper fundraising activities that are carried out by a charity in Ontario. Those statutory rights are summarized below as follows:

(a) Section 6 of the *CAA*

Section 6 of the *CAA* provides an effective way for a donor to make a complaint about the fundraising practices of a charity by simply delivering a written complaint to any judge of the Superior Court of Justice. The judge may then order an investigation by the Public Guardian and Trustee in the same manner as if the Public Guardian and Trustee were conducting a public inquiry under the Public Inquiries Act. In this regard, Section 6 (1) and (2) of the *CAA* provides for the following procedures:

> Section 6 (1) - Any person may complain as to the manner in which a person or organization has solicited or procured funds by way of contribution or gift from the public for any purpose, or as to the manner in which any such funds have been dealt with or disposed of.

[48] See Jacqueline M. Connor, Terrance S. Carter, and Mervyn F. White, "Donor Lists Protected as Charitable Property Under Canadian Law", *Charity Law Bulletin No. 15*, dated July 25, 2002, *available at* www.charitylaw.ca.

Section 6 (2) - Every such complaint shall be in writing and delivered by the complainant to a judge of the Superior Court of Justice.

Section 6 (6) of the *CAA* states that the report of the Public Guardian and Trustee's Office concerning the investigation is to be given to the judge who ordered the investigation, as well to the Attorney General of Ontario in writing. Under Section 6 (7) of the *CAA*, a judge may then subsequently order a passing of accounts of the charity that is being investigated. Section 6 (8) of the *CAA*, though, states that the right to complain to a judge about the fundraising practice of a charity does not apply to a "religious or fraternal organization".[49]

(b) Section 10 of the *CAA*

Section 10 (1) of the *CAA* provides a mechanism whereby two or more people can allege a breach of trust involving a charitable purpose and may apply to the Superior Court of Justice for an order or direction as the Court considers just, including an order for an investigation by the Office of the Public Guardian and Trustee. Such investigation could lead to a demand for a formal passing of accounts by the charity under Section 3 of the *CAA*, as well as an order under Section 4 (d) of the *CAA* to enforce donor directions as explained below.

(c) Section 4(d) of the *CAA*

Although not a specific right of a donor under the *CAA*, a complaint concerning the fundraising practices of a charity could result in the Public Guardian and Trustee seeking an order under Section 4(d) of the *CAA* that would indirectly cause a review of the fundraising practices of the charity. In this regard, Section 4 of the *CAA* provides a mechanism that allows a Public Guardian and Trustee to obtain a court order, amongst other remedies, to enforce directions established by a donor in

[49] For a more complete discussion concerning the effect of s.6 of the *Charities Accounting Act* and the applicable case law under it, see Carter, *supra*, note 23, Vol. 18, No. 2 at 126-127.

making a charitable gift. The relevant wording of Section 4 is set out below as follows:

> Section 4 - If any such executive or trustee,...
>
> (d) is not applying any property, fund or money in the manner directed by the will or instrument, ...
>
> a judge of the Superior Court of Justice upon the application of the Pubic Trustee, may make an order,
>
> (e) directing the executor or trustee to do forthwith or within the time stated in the order anything that the executor or trustee has refused or neglected to do in compliance with Section 1, 2 or 3, or with regulations made under this Act; ...
>
> (g) removing such executor or trustee and appointing some other person to act in the executor's, or trustee's stead;...
>
> (j) giving such directions as to the future investment, disposition and application of any such property, funds or money as the judge considers just and best calculated to carry out the intentions of the testator or donor; ...
>
> (k) imposing a penalty by way of fine or imprisonment not exceeding twelve months upon the executor or trustee for any such default or misconduct or for disobedience to any order made under this section... [Emphasis added]

The procedure set out in Section 4 of the *CAA* means that if a charity fails to comply with a direction by a testator in a will or by a donor in a written instrument, then the Public Guardian and Trustee, either on its own initiative or as a result of a complaint received from a donor or anyone else, has the ability to bring the matter before a court and request that the charity be removed as the trustee of the directed fund and appoint a new trustee, or alternatively to require that the charity comply with the terms of the directions given by the donor, as well as possibly requesting the imposition of a penalty or even imprisonment.

(d) Section 3 of the *CAA*

Another provision of the *CAA* that could be utilized by a donor indirectly is the general power given to the Public Guardian and Trustee under Section 3. If a donor made a complaint to the Public Guardian and Trustee concerning a fundraising practice of a charity or a misapplication of directed funds, the Public Guardian and Trustee would have the statutory right under Section 3 of the *CAA* to require a charity to submit its accounts for a formal passing of accounts before a judge. The relevant wording of Section 3 sets out the following procedures:

> Section 3 - Whenever required so to do by the Public Guardian and Trustee, an executor or trustee shall submit the accounts of dealings with property coming into the hands or under the control of the executor or trustee under the terms of the bequest or gift to be passed and examined and audited by a judge of the Superior Court of Justice.

The requirement for a formal passing of account could then result in the court issuing an order under Section 4 of the *CAA* as already discussed above.

(2) The *Income Tax Act*

Although there are no specific statutory provisions under the *ITA* concerning donors rights, from a practical context, if a donor is concerned about the operations of a charity and in particular whether its fundraising practices comply with the numerous requirements under the *ITA,* a complaint to the Charities Directorate of CRA would likely result in an audit being conducted into the operations of the charity to determine whether such operations, including fundraising practices, comply with the Charities Directorate requirements.

In consideration of the attention in the press concerning the alleged inability of CRA to stop abuses by charities, it is unlikely that the Charities Directorate would lightly dismiss a complaint brought to its attention by a member of the public about the fundraising activities of a charity. Rather, it is probable that the Charities Directorate would request the Audit Division to carefully investigate the complaint to ensure that CRA was not left vulnerable to public criticism at a later time. As such, an aggrieved donor has a very effective indirect means in having CRA investigate the fundraising practices of a charity, even though there is no formed statutory complaint process in place.

D. Preserving a Donor's Intent Through Use of Charitable Trusts

Although charities prefer to receive charitable gifts that are unrestricted, most donors of large gifts will want to exercise some measure of control over how the gifs are used. Wolfe D. Goodman, Q.C. in his paper "*Protecting the Donor of a Charitable Gift*"[50] comments that donors of large gifts in the past have often exercised control by making such gifts to the donor's own private foundation, which would then be controlled by the donor and/or successive members of his or her family, purportedly on an indefinite basis. The difficulty, however, in utilizing a corporation for a private foundation is that the charitable objects of the corporation in the future can be changed without a court order, although new objects would still have to be approved by CRA, as well as by the Office of the Public Guardian and Trustee of Ontario if the charity was incorporated in Ontario and was not adopting one of the pre-approved "boiler plate" charitable objects.

The probability that the original intent of the donor in creating a private foundation may eventually be lost was succinctly summarized by Wolfe Goodman, Q.C., as follows:

> ..."[T]he donor's children or grandchildren, may in future, alter the manner of operation of the foundation and the destination of its funds in a manner which the donor may not always find acceptable and may even change its objects so that it devotes its resources to entirely different charitable purposes".[51]

A means of overcoming the ability to vary the objects of an incorporated charity would be to utilize a charitable trust. This option is becoming more common in the United States in ensuring that the

[50] Wolfe D. Goodman, Q.C., "Protecting the Donor of a Charitable Gift" in *Charities and Not-for-Profit Law* (Continuing Legal Education of the Canadian Bar Association, Toronto, 1998) at page 1.
[51] *Ibid.*.

donor's wishes are respected on a perpetual basis.[52] The advantages in utilizing a charitable trust are summarized below as follows:

- The charitable trust is a flexible vehicle through which to craft the parameters and restrictions of the donor's intent, since it is not necessary to comply with corporate restrictions or obtain the approval of the Public Guardian and Trustee of Ontario.

- The objects of a charitable trust, once established, can only be changed by a court order and only then if the stated charitable objects have become impossible or impractical and the court is otherwise able to exercise its inherent *cy-prés* scheme making power.

- The donor, as well as the Public Guardian and Trustee of Ontario, may commence proceedings under the *CAA* to compel the trustees of the charitable trust to comply with the terms of the trust.[53]

- The problems inherent in selecting successor trustees to carry out the donor's charitable intent can be more easily customized to reflect the donor's desire for input from future family members, or alternatively the charitable trust could provide for the appointment of a corporate trustee to ensure that the control of the charitable trust did not fall into the hands of non-family members who might be less likely to respect the original intent of the donor.[54]

A few examples of how a charitable trust could be utilized to protect the intent of a donor are set out below as follows:

- A charitable trust could be used as an alternative to an incorporated private foundation, either at the time that the family foundation is created or subsequently in winding up the corporate foundation by receiving a transfer of the remaining capital in the incorporated private foundation before it is dissolved.

- A charitable trust could also be used as the basis for an endowment fund where the capital is to be held in perpetuity and the beneficiary charity acts as the trustee.

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[52] See James N. Donaldson, "Will Your Private Foundation Carry Out Your Intention?" *Trusts & Estates* (Aug. 1998) at 24.

[53] See s. 10 of the *Charities Accounting Act*.

[54] *Supra*, note 52 at 28.

- A charitable trust may also be used where money or property is gifted to a charity and the donor stipulates that the gift is to be utilized for a specific purpose, such as a building program. The recipient charity again would act as the trustee of such gift.

One application of the charitable trust referred to above that could prove to be timely is when a charity, such as an incorporated private foundation, decides to wind down its operations and wishes to ensure that its remaining charitable property will be used only in accordance with the current charitable purposes of the foundation. This objective could be accomplished by transferring the remaining assets of the charity to be wound down to a recipient charity, such as a community foundation, pursuant to a charitable trust agreement that would require that the capital be held in perpetuity in accordance with a particular set of charitable purposes or be expended in accordance with the terms of the charitable purposes of the transferring charity.

If the charity is concerned about the ability of the recipient charity to manage an endowment fund in perpetuity or is concerned about the possibility that the board of that charity might not be inclined to comply with the restrictions imposed in the trust agreement, consideration could be given to the creation of a new charitable trust utilizing a trust company as the trustee. Using a trust company would have the advantage of providing assurance to the transferring charity that the terms of the applicable charitable trust would be complied with. Notwithstanding that there would be an increase in administrative costs associated with utilizing a trust company, there may be circumstances where this increased expense may be justified.

Although there are drawbacks in utilizing charitable trusts, such as the trustees being exposed to personal liability, in the limited context of providing an alternative to an incorporated private foundation, there would be merit for the lawyer advising the private foundation to consider the advantages associated with utilizing a charitable trust to preserve the intent of the original donor or donors to the private foundation.

5. AVOIDING LIABILITY IN FUNDRAISING FROM TESTAMENTARY GIFTS

A. Reducing Legal Risks From Estate Planning Programs

In accordance with a national survey of fundraising practices of Canadian charities carried out by the Canadian Centre for Philanthropy in 1995, the use of bequests and other testamentary gifts involved in planned giving programs would appear to be the third most successful means of fundraising in Canada, second only to direct mail and special events.[55] However, fundraising programs involving testamentary gifts also involve a heavy exposure to liability for the charity, its board of directors, as well as its fundraisers.

Legal liability may occur where there is a challenge to the validity of a testamentary gift based on allegations that the charity and/or its fundraisers may have exercised undue influence. As well, there could be exposure to a higher level of professional liability in the event that the charity or its fundraisers provide legal services, such as preparing a last will and testament or a power of attorney for a donor, or even from advising on the structuring of a last will and testament without the donor being advised to obtain an independent legal review of the will provisions before the will is prepared and signed. In addition, there may be exposure to liability where a charity is given a testamentary gift in kind, such as a building, that may carry environmental risks, or the testator imposed restrictions in the estate gift that the charity is either unable or unwilling to comply with. Such risks are discussed in more detail later in this paper.

Given the significant exposure to legal liability involving a testamentary gift, a charity should develop and adopt a strategic plan to both identify and reduce legal risks associated with estate planning as much as possible. A strategic plan in this regard would include, amongst others, the following considerations:

[55] *Supra* note 11 at 13.

(1) Shift the Legal Risk Away from the Charity

The charity, its board of directors, administrators and fundraisers should take steps to "shift the legal risk" away from the charity in estate planning programs by doing some or all of the following:

- Both the charity and the donor should utilize professional advisors wherever possible, such as lawyers and accountants, in order to establish evidence of due diligence by the charity and its board of directors.

- The shield of insurance should be raised to cover potential third party liability claims associated with estate planning programs by ensuring that the insurer and the broker are made fully aware in writing of all aspects of the estate planning program operated by the charity. Doing so would assist in preventing the insurer for the charity from attempting to deny liability coverage based on an alleged failure by the charity to disclose a material risk.

- Any original wills or codicils belonging to donors that are being stored by the charity should be returned to the donor or to his or her solicitor.

- A gift from an estate of real property should not be accepted until an environmental assessment of the property has been completed to avoid "flow through" liability to the charity and/or its directors for the cost associated with cleaning up any contamination that may be found.

- A charity should not accept a gift from an estate that is intended for another organization, otherwise the charity will be at risk in becoming simply a "conduit" for gifts to other registered charities or to a non-qualified donee in contravention of the position of CRA and that of the courts.[56]

(2) Avoid Circumstances Conducive to Allegations of Undue Influence

To avoid a charity and/or its fundraisers being exposed to allegations of undue influence by family members of a testator, the charity should refrain from doing any of the following:

[56] See *Beaudry v. R* [1998] 1 C.T.C 2042 (T.C.C.).

- directing legal work to one lawyer who may be or may appear to be dependent upon referral work from the charity;
- paying for any portion of the legal costs of the donor, such as the legal costs to prepare a will, a power of attorney, or obtain estate planning advice;
- acting as either an estate trustee of a will, or an attorney under a power of attorney for the donor;
- preparing the last will and testament or a power of attorney for a donor or the spouse of a donor;
- providing advice on how to structure a disposition clause in a will without the donor obtaining independent legal advice;
- providing recommendations on how much of the estate should be given to a charity without obtaining independent legal advice;
- completing a will guide on behalf of the donor instead of have it done by the donor;
- meeting with the lawyer and donor when the donor is giving instructions to prepare a last will and testament or power of attorney;
- being present when the will is signed, either as a witness or as an observer; or
- offering to store an original will, codicil to the will, or power of attorney on behalf of the donor.

(3) Focus on Developing an Informational and Resource Role

Notwithstanding the restrictions concerning what a charity should not be involved with when a donor is making a testamentary gift, it is appropriate for a charity to provide information on estate planning considerations and the testamentary options that are available to a donor, provided that the donor is not being directly or indirectly influenced by the charity concerning testamentary dispositions. In this regard, the type of information that would be useful for a charity to provide to a prospective donor that would not be susceptible to allegations of undue influence would include the following:

- an explanation of why a will and power of attorney are fundamental estate planning documents for a donor to have, whether or not they give a gift to a charity;
- an explanation of what happens if the donor has no will or power of attorney;
- general information concerning estate planning options;
- an explanation concerning how the donor can complete a basic will guide;
- a written description of the full legal name of the charity to ensure that the lawyer preparing the will properly describes the legal name of the charity; and
- explaining the type of disposition clauses that might be appropriate for the donor, provided that the donor is also advised to review the suggested disposition clauses with their own lawyer before having the will prepared.

B. Managing Testamentary Gifts

Once notice of a testamentary gift has been received by a charity, there are a number of steps that the charity should take to reduce the risk of liability associated with managing an estate gift. The following suggestions have been adapted from comments given by Eric Moore, the former Director and Legal Counsel of the Charitable Property Division of the Office of the Public Guardian and Trustee, at the 1996 Law Society Special Lectures on Estates and Trusts.[57]

- Ensure that the charity receives a complete copy of the will and that it is carefully read in its entirety.
- Determine whether the testamentary gift is subject to conditions or is contingent upon the failure of another gift before it can be distributed.

[57] Reported by Patricia Rubin in *Charitable Thoughts*, a newsletter of the Charity and Not-for-Profit Law section of the Canadian Bar Association of Ontario. (Nov. 1999)

- Review the terms of the will to ensure that the charity is properly described using either the full legal name of the charity or one of its registered operating names.

- Review the terms of any applicable donor restriction to identify the restrictions that may need to be complied with and whether or not the charity is able or willing to comply with such restrictions.

- Communicate with the estate trustee or the estate solicitor and request regular communications concerning when the gift is likely to be received.

- Diary ahead when an answer is expected from the estate solicitor and follow up with letters at regular intervals.

- Consider whether the charity receiving a testamentary gift after the "executor's year" should be entitled to interest on the gift.

- Refrain from signing releases in favour of the estate trustee until the charity is fully satisfied that it is receiving all of the monies and property that it is entitled to and that the estate trustee's compensation and solicitors costs are reasonable in the circumstances.

- Ensure that tax credits are used against 100% of the income acquired in the year of death and carried back on year, if necessary.

C. Resisting Voluntary Renouncement of a Charitable Gift

Often a charity that is entitled to a testamentary gift will be contacted by either the estate trustee or the solicitor for the estate to advise that there is some financial hardship being faced by family members of the testator. As a result, the charity may be requested, as an act of compassion towards the family members of the deceased and out of respect for the testator, to renounce a part or all of the charitable gift intended for that charity.

Although there may be compelling reasons for the request, the case law is clear that a charity and its board of directors have no authority to voluntarily renounce a gift that a testator intended for a charity, other than as directed by a court order.[58] In this regard, the Public Guardian and Trustee takes the position that the discretion available to a court in determining whether or not a charity can renounce a gift should not be exercised lightly or *"on slender grounds*" and that it is a discretionary power to be exercised *"only where one could conclude that it would be morally wrong to refuse the payment"*.[59]

6. AVOIDING LIABILITY INVOLVING DONOR RESTRICTED CHARITABLE GIFTS

A. The Difference Between Unrestricted and Donor Restricted Charitable Gifts

Probably the greatest area of liability exposure for charities and their boards of directors involves the misunderstanding and misuse of donor restricted charitable gifts. Although it is beyond the scope of this paper to provide a detailed discussion of the legal issues involved in donor restricted charitable gifts, the following is a brief summary of some of those issues.[60]

(1) What is an Unrestricted Charitable Gift?

An unrestricted charitable gift is generally considered to reflect the following characteristics:

- It is a gift given to further the general charitable purposes of a charity and is not subject to any restrictions or limitations imposed by the donor.
- It is a gift that can be used by the board of directors of the charity in their sole discretion to pursue any of the general charitable purposes of the charity as authorized in the constating documents of the charity.
- The board of a charity may designate the gift to be used for a specific purpose and then subsequently redesignate that gift for another purpose without violating any donor

[58] *Re Snowden and Re Henderson*, [1970] Ch. 700, [1969] 3 ALL E.R. 208.

[59] *Supra*, note 21 at 60.

[60] For a more complete discussion of the legal issues involving donor restricted charitable gifts, see Carter, *supra* note 23.

restrictions or otherwise causing a breach of trust. Such funds are often referred to as "board designated funds" or "internally restricted funds".

(2) What is a Donor Restricted Charitable Gift?

A donor restricted charitable gift is generally considered to include the following characteristics:

- It is a gift for a charitable purpose that is subject to certain binding restrictions, conditions, or limitations imposed by the donor, either directly or indirectly.
- Different types of donor restrictions will result in different legal consequences, i.e., a restriction to hold a capital endowment in perpetuity and disperse the income will generally have to be managed in a more sophisticated manner than a contribution to a building fund that is to be expended over the course of only a few months.
- A donor restricted charitable gift must be complied with, except where it is void as being contrary to public policy or where varied by a court order, failing which the board of directors of a charity may be found in breach of trust.
- A donor restricted charitable gift generally constitutes a charitable trust. As such, the gift constitutes a form of "a charity within a charity".

As a result of the *Christian Brothers of Ireland in Canada (Re)* decisions referred to below, the issue of what is required to constitute a donor restricted charitable trust is unclear. The Ontario trial division court in *Christian Brothers* [61] suggested that before there can be a "true charitable purpose trust", there must be the three certainties required of a trust, i.e., certainty of intention, certainty of subject matter and certainty of objects. As a result, unless terminology such as "in trust" is used in creating a donor restricted charitable gift, an enforceable donor restricted charitable gift might not be created at all. Despite the fact that it was reversed on appeal, that portion of the *Christian Brothers Gen. Div.* decision that dealt with a "true charitable purpose trust" as discussed above, was not specifically

[61] *Christian Brothers of Ireland in Canada (Re)* (1998), 37 O.R. (3d) 367 (Ont. Ct. (Gen. Div.)), 21 E.T.R. (2d) 117, rev'd (2000), 47 O.R. (3d) 674 (Ont. C.A.) [hereinafter *Christian Brothers Gen. Div.*].

addressed in the decision of the Ontario Court of Appeal.[62] In addition, the position taken in the *Christian Brothers Gen. Div.* was not followed in the British Columbia *Christian Brothers (B.C.S.C.)* decision[63]. Whether this restricted position of the *Christian Brothers Gen. Div.* will prevail in the future is unknown. As such, it would be better to take a cautious approach and utilize trust terminology when creating a donor restricted gift.

Even if the restricted position of the *Christian Brothers Ont. C.A.* decision is not reversed, it may very well be limited to the particular facts of that case involving a determination of what charitable assets can be seized on the insolvency of a charity.[64] In addition, it is likely that the office of the Public Guardian and Trustee of Ontario may narrowly interpret the application of the decision, since Section 4 (d) of the *CAA* provides the Pubic Guardian and Trustee of Ontario with the ability to bring an application to enforce compliance with "donor directions", whether or not such directions constitute a donor restricted charitable purpose trust in the more formal context contemplated by the Ontario courts in the *Christian Brothers* case.

B. Instances of Breach of Trust Involving Donor Restricted Charitable Gifts

The case law concerning breach of trust involving donor restricted charitable gifts has been well established in England,[65] as well as in Canada.[66] Some examples of fact situations where the courts have found that there has been breach of trust involving donor restricted charitable gifts are summarized below as follow:[67]

[62] *Christian Brothers of Ireland in Canada (Re)*, (2000), 47 O.R. (3d) 674 (Ont. C.A.), rev'g (1998), 37 O.R. (3d) 367, application for leave to appeal to the Supreme Court of Canada dismissed, November 16, 2000 [hereinafter *Christian Brothers Ont. C.A.*].

[63] *Rowland v. Vancouver College Ltd.* (2000), 78 B.C.L.R. (3d) 87 (S.C.), 34 E.T.R. (2d) 60, aff'd (2001), 94 B.C.L.R. (3d) 249 (C.A.) [hereinafter *Christian Brothers B.C.S.C.*].

[64] *Rowland v. Vancouver college Ltd.* (2001), 94 B.C.L.R. (3d) 249 (C.A.), aff'g 78 B.C.L.R. (3d) 87 (S.C.), application for leave to appeal to the Supreme Court of Canada dismissed, May 23, 2002 [hereinafter *Christian Brothers B.C.C.A.*].

[65] See Tudor, *supra* note 42 at 245 for list of applicable case law.

[66] See also *Young Women's Christian Association Extension Campaign Fund* [1934] 3 W.W.R. 49 (Sask. K.B.); *R. v. Baker* (1984), 11 D.L.R. (4th) 430, 47 O.R. (2d) 415, 17 E.T.R. 168 (Ont. S.C. (HCJ)).

[67] For an extensive list of case citations, see Tudor, *supra* note 42 at 245; and Hubert Picarda, *The Law and Practice Relating to Charities,* 2nd ed. (London: Butterworths, 1995), at p. 367.

- A charity diverting a fund intended for one charitable program for use in another charitable program. For example, a charity using monies from an estate that was intended by the testator to help the poor in one parish by diverting those monies to help the poor in another parish.

- A charity withholding a fund and not having it applied to the purpose for which it was intended by the donor.

- The trustees of a charity concealing the existence of a charitable trust fund by not communicating its existence to the persons or groups intended to benefit from it.

- A charity placing funds into a perpetual endowment fund when all of the funds were intended by the donor to be expended in the short term in support of a particular operational program of the charity.

- A charity mixing its funds with another charity and then applying the combined funds for the purposes of the other charity.

- A charity encroaching upon the capital of an endowment fund that was intended by the donor to be held in perpetuity.

- A church that had received land in trust to further a particular doctrinal statement subsequently using the land for the benefit of individuals adhering to a different doctrinal statement.

- The members of a church unilaterally attempting to alter the terms of a trust deed for church property without first obtaining court authorization.

- A charity borrowing monies from a donor restricted charitable trust fund notwithstanding that there was a bona fide intent to repay those monies together with interest.

- A charity using surplus funds from a public fundraising appeal for different charitable purposes from those communicated in the public appeal without first obtaining court authorization.

- The directors of a charity altering the terms of a donor’s restriction without first obtaining court authorization.

C. Can a Donor Restriction be Unilaterally Varied

Notwithstanding well-established law to the contrary, the boards of many charities believe that a charity somehow has an inherent right to unilaterally vary the terms of a donor restriction or to liberally interpret what the applicable restriction means. Alternatively, many charities that receive a testamentary gift which is subject to restrictions believe that the executor of the estate also has an inherent ability to unilaterally vary or liberally interpret the donor's restrictions. Neither of these assumptions, though, is correct. Only the courts can vary the terms of a restricted special purpose charitable trust based on the court's inherent scheme-making power.

> It is not for the trustees [of a charity] to deal with the funds on their own authority, even by the direction or approval of the original subscriber of the charitable funds...[68]

This means that to vary a donor restricted charitable gift, an application must be made for a *cy-près* order. Any attempt to unilaterally vary a donor restricted charitable gift based upon the consent of only the donor, with the charity acting on its own, without first obtaining the necessary court approval, would likely constitute a breach of trust and must therefore be carefully avoided notwithstanding the time and expense of making the necessary court application.

There are two situations, however, in which court approval to vary a donor restricted charitable gift may not be necessary. The first situation is where a *cy-près* court application is not successful and the gift reverts back to the donor in circumstances where there is no gift over to another charity. The second situation results in the same effect, but is due to the failure of either a condition precedent or a condition subsequent where there is a reversion back to the donor.[69] In both situations, the donor would be able to unilaterally re-issue the gift to the intended charity once the donor had received the gift back and at that point establish either new restrictions or re-issue the gift without any restrictions being imposed.

[68] *Ibid* at 245.

[69] See Carter *supra*, note 23 at p. 44-48; 63-67 for a more detailed explanation of conditional gifts and the consequences flowing from non-fulfillment of conditions.

D. How Should Donor Restricted Gifts be Managed once Received?

Often, a charity will run into difficulties in dealing with donor-restricted charitable gifts due to either a lack of understanding of the legal consequences arising from such gifts or a failure by the charity to implement appropriate policies to effectively manage donor-restricted charitable gifts once received. The following provides a brief summary of some of the practical considerations that should be addressed by a charity, its board of directors, management, and fundraisers in effectively managing donor-restricted charitable gifts:

(1) Identifying the Nature of the Charitable Gift

Since the legal consequences in dealing with donor restricted charitable gifts are very serious, it is important for a charity to retain the assistance of legal counsel in drafting guidelines to identify the legal distinctions in relation to gifts received. These guidelines should provide examples of gifts that are subject to terms, restrictions, or conditions that will need to be scrutinized to determine whether or not they may constitute donor-restricted charitable trusts, as well as providing examples of gifts that are clearly unrestricted.

In the event that there were any questions concerning the nature of the gift, then the instrument creating the gift should be forwarded to legal counsel for the charity so that an appropriate legal opinion can be obtained. If a determination is made that the gift constitutes a donor-restricted charitable gift, then the gift would need to be identified as such and subsequently treated as a special purpose charitable trust.

(2) Reviewing and Approving Donor Restrictions

Whenever a gift is received that is identified as a donor-restricted charitable gift, it is important that the management of the charity carefully review the terms of the donor restrictions to ensure that the following questions are addressed:

- Are the restrictions charitable?

- If so, are the restrictions within the charitable purposes of the charity?

- Are the restrictions both possible and practicable?

- If they are, then are the restrictions acceptable to the charity?

- If any of these questions is answered in the negative, then the charity should not accept the gift, the gift should be returned to the donor, and no charitable tax receipt should be issued.

- Alternatively, if the gift is subject to restrictions that the charity wishes to accept but such restrictions are either impossible or impractical, then the charity would need to apply to a court to have the court exercise its *cy-près* scheme-making power to vary the terms of the donor-restricted charitable trust "as near as possible" to the original restrictions imposed by the donor.

(3) Effective Ongoing Management of Donor Restricted Charitable Gifts

Once a decision is made to accept a donor-restricted charitable gift, then the charity and its management must be careful to ensure that the funds in question are managed as charitable trust funds. Appropriate management in this regard would involve looking at the following considerations:[70]

- Since a donor-restricted charitable gift is by its very nature given to a specific charity or trustee, the gift must be deposited into the bank account of that charity and used by that charity for the stated charitable purposes, unless the objects and power clauses of the named charity permit the funds to be subsequently transferred to another charity.

- Donor-restricted charitable funds must be invested in accordance with the specific investment powers set out in the document creating the restricted charitable trust or, if there is no special investment clause, in accordance with the general investment powers of the charity.

- The charity must never borrow against donor-restricted charitable funds, whether to further other charitable purposes of the charity or to underwrite the general operations of

[70] *Ibid* at 186.

the charity, notwithstanding that the board may intend to repay the monies at a later time with interest.

- At common law, each donor-restricted trust fund is required to be held separately from other restricted trust funds and cannot be co-mingled together though very few charities, though, comply with this common law prohibition against co-mingling. As such, it is anticipated that pending regulations under s.5.1 of the *CAA* will permit co-mingling of restricted funds by a charity; however, it is likely that such regulations will impose some restrictions on the ability to co-mingle.

- Since donor-restricted charitable gifts are often testamentary gifts, it is important for the charity to maintain ongoing communication with family members of the testator to provide information and confirmation of compliance by the charity with the applicable restrictions. Good communication in this regard can help to avoid misunderstandings in the future between family members of the testator and the charity that might otherwise lead to legal action.

- A transfer of a donor restricted charitable trust from one charity to another will require, at the very least, a written appointment in accordance with s.3 of the *Trustee Act* to document a change in trustees. A transfer may also require court authorization pursuant to a consent order obtained under s.13(1) of the *CAA* in the event that the nature of the donor restriction contemplated that the role of the named charity as the trustee of the fund was a fundamental term of the donor-restricted charitable trust.

- The proceeds realized from the sale of charitable property that is subject to a special purpose charitable trust, such as a trust deed for church property, will remain impressed with the terms of that trust and may have to be accounted for as a special purpose charitable trust fund on a perpetual basis, unless court approval is first received to vary the terms in accordance with a *cy-près* application.

E. How Can Donor Restricted Charitable Gifts be Avoided in the First Instance?

Since donor-restricted charitable gifts involve considerable legal responsibility and exposure to liability, an important question that a charity should ask is what can be done on a practical basis to encourage donors to give unrestricted gifts rather than restricted charitable gifts. This is not to suggest that there is not a place for donor-restricted gifts; however, a program of good legal risk management in avoiding breach of trust should involve taking positive steps to avoid situations that might otherwise give rise to a breach of trust before it occurs instead of trying to remedy the problem after the fact.

Some practical suggestions include:

- The simplest approach is to encourage donors to give unrestricted gifts, wherever possible. This could be done by providing sample bequest clauses that make reference to the general purposes of the charity without suggesting the option of giving a restricted gift, e.g.,*"to ABC charity for its general charitable purposes*."

- If a donor wanted to give directions concerning how a gift was to be used, then the donor could be encouraged to use wording that constitutes "suggestions" only as opposed to a binding restrictions, e.g., "*to ABC charity, with the request, but not the legal obligation, that the gift be used for _______*."

- Fundraisers should be understand and be able to identify the difference between unrestricted charitable gifts and donor-restricted charitable gifts, so that they can encourage donors to focus on the flexibility of an unrestricted gift.

- As a precautionary measure, fundraising materials should include a statement to explain that all gifts will be considered to have been given to further the general charitable purposes of the charity in accordance with its needs from time to time, unless the donor has specifically stated that the gift is to be subject to binding restrictions, in which event the donor would be encouraged to contact the charity to discuss the specific terms of the restriction before making such a gift.

F. Preventative Steps to Reduce Liability Involving Donor Restricted Charitable Gifts

Since it is not realistic to expect that all future gifts that a charity will receive will be of an unrestricted nature, it is important for a charity also to develop and implement a policy to reduce the risks associated with receiving donor-restricted charitable gifts. Considerations should include:

- Public fundraising appeals for a specific program, such as monies required for a building program, should contain a clear statement that any surplus monies remaining after the necessary funds have been raised for the designated project or program will be used to further the general charitable purposes of the charity. This would avoid the charity having to make a *cy-près* court application to obtain judicial direction.

- Suggested wording given to a prospective donor and the donor's solicitor concerning an estate legacy where a donor wants to include a restricted charitable gift should include a standard *cy-près* clause in the will so that the charity will be able to unilaterally modify the restrictions imposed by the donor in the event that such restrictions become impossible or impracticable in the future.

- To avoid a donor restricted charitable gift subsequently failing and the gift reverting back to either the donor or to the beneficiaries of the testator, it is important that the wording used in the document creating the restricted gift, such as the will, use clear language to identify the specific charitable purpose for which the monies are to be used and who the beneficiary is to be; otherwise, the gift may fail altogether for lack of certainty.[71] In this regard, and in accordance with *Christian Brothers Gen. Div.*, it would be prudent to include language that shows clearly that a charitable trust has been created, e.g., using the phrase "in trust," and to ensure that the formalities of the three certainties of a trust are met, i.e., who is the trustee? what is the trust property? and what is the charitable purpose?

- In the event that the donor intends to give endowment funds where the capital is to be held in perpetuity and the interest income is to be used for operational purposes of the charity, then the donor should be encouraged to place only general restrictions on how the income can be used. In any event, the donor should include a *cy-près* clause so that the restriction can be unilaterally varied. The inclusion of such a clause would ensure that the charity would have the ability to redirect the income earned from the endowment fund in the event that the restrictions concerning how the income is to be used became impossible or impracticable to honour.

G. Protecting Donor Restricted Charitable Gifts

(1) Background

The Ontario Court of Appeal decision in *Christian Brothers of Ireland in Canada (Re)*[72] (hereinafter "*Christian Brothers Ontario C.A.*") arose out of an appeal from a lower court judgment[73] concerning the issue of the exigibility of charitable property. The lower court decision involved an application to determine the issue of whether property held in trust by the Christian Brothers of Ireland in Canada ("CBIC") was available to compensate tort creditors of CBIC, which was being wound-up under the *Winding-Up and Restructuring Act*

[71] See *Muir* v. *Muir* (1995), 7 E.T.R. (2d) 58 Ont. Ct. (Gen. Div.); *O'Neill Community Ratepayers Association* v. *Oshawa (City)* (1995), 22 O.R. (3d) 648 Ont. Ct. (Gen. Div.).

[72] *Supra note 62*.

[73] *Supra* note 61.

R.S.C. 1985 c. W. 11. The matter had arisen because the CBIC had general corporate assets totaling four million dollars ($4,000,000.00) but judgments by tort victims from the Mount Cashel Orphanage in Newfoundland totaling in excess of thirty-six million dollars ($36,000,000.00). The primary issue in the case was whether two schools located in British Columbia that the CBIC purportedly owned in trust were exigible to satisfy claims by tort victims. The lower court in Ontario was only required to deal with the general legal principles involving the exigibility of charitable property. The specific issue of whether the two schools in British Columbia were owned in trust by the CBIC had been referred to the jurisdiction of the B.C. Courts.

(2) Exigibility of Special Purpose Charitable Trusts

The decision of Feldman J.A. in *Christian Brothers Ont. C.A.* concerning the exigibility of special purpose charitable trusts is arguably one of the most significant cases involving charities in Canada. Since leave to appeal the decision to the Supreme Court of Canada has been denied, it is now important to consider the full impact of the pronouncement by the Ontario Court of Appeal. In this regard, it is expected that the decision of Feldman J.A. will create serious problems for charities in protecting their special purpose charitable trusts from tort creditors of the charity. The decision is also expected to have a serious impact upon the ability of charities to raise monies from donors, particularly monies for endowment funds in situations where donors presume that their gifts will be protected from creditors of the recipient charity.

As explained earlier in this article, Blair J. in the *Christian Brothers Gen. Div.* decision held that although the general corporate property of a charity is not immune from exigibility by tort creditors, property that is held as a special purpose charitable trust would not be available to compensate creditors of a charity unless the claim of the tort creditor arose from a wrong perpetrated within the framework of the particular special purpose charitable trust in question.

In the Ontario Court of Appeal decision, Feldman J.A. agreed with Blair J. that there was no general doctrine of charitable immunity applicable in Canada. However, Feldman J.A. stated that once Blair J. had determined that there was no doctrine of charitable immunity, it then became redundant for him to analyze whether the special purpose charitable trusts of a charity were exigible to pay the claims of tort creditors. Feldman J.A. concluded that:

> For the purposes of this winding-up procedure, all assets of the [Christian Brothers], whether owned beneficially or on trust for one or more charitable purposes, are exigible and may be used by the Liquidator to pay the claims of the tort victims.

Unfortunately the result in the British Columbia decisions does little if anything to temper the impact of *Christian Brothers Ont. C.A.* Both B.C. courts declined to deal with the issue of the exigibility of special purpose trust funds for the benefit of a charity's tort creditors. Rather, they stated that the case as it was stated before them was restricted to determining the ownership of the assets and did not allow them to address the issue of exigibility. The courts accepted that while they were to determine ownership, the implications of that determination would depend on the decision of the Ontario courts. As mentioned earlier, Braidwood J.A. dissented, stating that it was open to the B.C. court to determine the legal ramifications of the determination of ownership. He agreed with Blair J. (in *Christian Brothers Gen. Div.*) that special purpose charitable trusts could only be available to tort creditors claiming for a wrong perpetrated within the framework of the particular special purpose trust. However, since leave to appeal to the Supreme Court of Canada was denied, Braidwood J.A.'s dissent has little impact on the practical result. Granted, the affirmation by the B.C. courts that special purpose charitable trusts do indeed exist in Canadian law may give donors some comfort in knowing that the charity recipient is legally, and not just morally, bound to use the donations for the donor's stated purposes. However, donors will have no assurance that their funds will not be used for completely unrelated purposes in the event that the charity becomes subject to tort claims which it is unable to satisfy from its other assets.

(3) Commentary on the *Christian Brothers* Ont. C.A. Decision

What follows is only a brief commentary concerning some aspects of the Ontario Court of Appeal decision:[74]

- The decision that all assets held by a charity pursuant to special purpose charitable trusts are exigible by tort claimants of the charity, even if the wrongdoing was only with respect to one particular trust and not to the others, is in direct conflict with the long-standing principle at law that trust property held by a trustee is not exigible to satisfy a judgment against that trustee personally.[75]

- Although not specifically expressed in the decision of Feldman J.A., the basis on which the Ontario Court of Appeal could conclude that special purpose charitable trusts were exigible and not run contrary to the established principles of trust law in relation to protection of trust property, is to draw a distinction between private trusts and charitable trusts. In this regard, there appears to be an underlying presumption by the Ontario Court of Appeal that special purpose charitable trusts held by a charity as the trustee are tantamount to an individual holding property in trust for the trustee personally, which would preclude a trust in the first place. This line of reasoning comes from a perception that special purpose charitable trusts do not have identifiable beneficiaries to enforce the trust and therefore it is as if the charity is holding the property in question for itself, subject only to a trustee-like fiduciary obligation to comply with the expectations of the donor.

- What Feldman J.A. and, for that matter, counsel for the liquidator, failed to recognize, was that a basic attribute of a charitable purpose trust is that it is exempt from the requirement that there be identifiable beneficiaries.[76] The reason why special status is given at law to a charitable purpose trust is that the public-at-large receives the benefit of the charitable purpose and as such, collectively, members of the public are considered to constitute the beneficiaries of the trust. Since it would be impossible for all members of the public to enforce the trust, it falls upon the Attorney General on behalf of the Crown to enforce the terms of the charitable purpose in accordance with its *parens patriae* role in overseeing charitable property. Given that a charitable purpose trust is as much a valid trust as a private trust, it follows that the ability of tort creditors to seize property held by a charity pursuant to a special purpose charitable trust could mean that any trust property held by a trustee, including property held pursuant to a private trust, might arguably be

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[74] For a thorough analysis of this decision see David Stevens, "An Analysis of the Christian Brothers Decisions". (Paper Presented at the First Annual Charity Law Symposium, *Fundamental New Developments in the Law of Charity*, Canadian Bar Association of Ontario, Toronto, 2000.) [unpublished].

[75] *Jellett v. Wilkie* (1896), 26 S.C.R. 282, at 288.

[76] *Supra* note 12 at 395.

subject to claims against the trustee personally. This is clearly not the law in Canada. It is therefore unfortunate that leave to appeal to the Supreme Court of Canada was not granted so that the uncertainty resulting from the *Christian Brothers Ont. C.A.* decision on this issue could have been resolved.

- Feldman J.A., in an attempt to limit the impact of the decision, was careful to note that the Court of Appeal decision was limited to a very specific fact situation, i.e., only in instances where:

  - there are claims by tort victims against the charity;
  - the general assets of the charity are insufficient to satisfy the resulting judgments;
  - the charity is no longer operating; and
  - the charity has been wound up pursuant to a winding-up order under the *Winding-Up and Restructuring Act*.

These limitations, though, are arbitrary in nature and provide little comfort to charities and their legal counsel who may be concerned that the decision could become the "thin edge of the wedge" that could lead to future court decisions exposing special purpose trusts' property, such as endowment funds, to claims by tort victims in a broader context instead of only in the limited fact situation involving the *Christian Brothers* case.

(4) Impact of the *Christian Brothers* Ont. C.A. Decision

The *Christian Brothers Ont. C.A.* decision will probably have a negative impact on the operations of charities across Canada in at least six crucial ways:

- Tort victims will now be encouraged to pursue claims against charities, particularly larger charities, knowing that there may be "deep pockets" that were previously untouchable but can now be readily accessed.

- Property and/or funds held as special purpose charitable trusts, particularly endowment funds, that many charities depend upon for their continued existence, will now be susceptible to claims by tort victims. This in turn may prejudice the ability of some charities to continue operating and could result in either the bankruptcy or forced distribution of funds for some charities that are particularly vulnerable, such as religious denominations, local churches and educational institutions.

- The ability of donors to create enforceable special purpose trusts will be thwarted where claims by tort creditors cause those special purpose charitable trusts to be applied in ways totally different from that which was originally contemplated by the donors. Such a result ignores the overriding jurisdiction and mandate of the court to apply a special purpose charitable trust *cy-près* where the original charitable purpose has become either impossible or impracticable.

- Donors will be reluctant to give large gifts (such as endowment funds) directly to charities that otherwise had been thought to be protected from creditors as special purpose charitable trusts when no assurance can be given to donors that the special purpose charitable trusts will be immune from present or future creditors of the charity.

- International charities may be reluctant to set up operations in Canada for fear that they might arguably be exposing their global assets to claims by tort creditors in Canada.

- Lawyers might be found liable if they fail to advise clients, either charities or donors, that special purpose charitable trusts are no longer protected from the claims of tort creditors and that alternatives should be canvassed in an attempt to "credit-proof" special purpose charitable trusts as much as possible.[141]

The combined overall "chill effect" that will likely result from the negative impact of *Christian Brothers Ont. C.A.* may very well prejudice the financial stability of a large segment of the charitable sector in Canada and could even affect its long-term viability. This in turn may require that various levels of government may need to fill the void that could result in the loss of social services currently being provided by charities that could be seriously affected by the decision.

(5) Developing a Strategy in Response

Since it is uncertain whether anything effective can be done to "credit-proof" existing special purpose charitable trusts, the task for lawyers in advising charities and donors will be to focus on how to structure future special purpose charitable gifts so that they will not become exigible by tort creditors of the charity. Some strategies that legal counsel may want to consider in advising charities and donors on this issue include:

- Creating a special purpose charitable trust by the donor giving the intended gift to an arm's-length parallel foundation established to advance only the purposes of the intended charity;

- Creating a special purpose charitable trust by the donor giving the intended gift to a community foundation or trust company to be held in trust for the benefit of a specific named charity; or

- Structuring a donation as a determinable gift to be determined upon the winding-up, dissolution or bankruptcy of the charity, accompanied by a "gift over" to another charity that had similar charitable purposes or, alternatively, providing that the gift revert to the donor.[77]

All of these options and, in particular, the use of conditional gifts, would require addressing a number of important legal issues, including determining the income tax consequences to the donor in making the gift. (Some of these have been addressed earlier in this article and elsewhere.)[78]

7. AVOIDING LIABILITY IN GIFT AND FUNDRAISING PROGRAMS

This section of the paper provides a summary overview of some of the legal risks associated with the more commonly used gift and fundraising programs. However, it is important to emphasize that what follows is not intended to be a thorough analysis of the fundraising programs that are described nor are the comments concerning legal liability intended to be of a comprehensive nature. The reader will need to conduct further research as necessary.

A. Gift of Shares or Interests in a Business

In addition to restrictions imposed under the anti-avoidance amendments to the *ITA* in 1997 concerning the gifting of shares and debt of a private corporation, a charity will need to be aware that provincial legislation in Ontario limits the extent of ownership that a charity can have in a business. Specifically, Section 2(1) of the *Charitable Gifts Act* restricts a charity (other than

[77] Although a condition subsequent against forfeiture on bankruptcy would be void, a limitation in the form of a determinable interest until bankruptcy has been held to be valid. See John McGhee, ed., *Snell's Equity*, 30th ed. (London: Sweet & Maxwell, 2000), pp. 160-161. See also Jill E. Martin, ed., *Hanbury & Martin: Modern Equity,* 15th ed., (London: Sweet & Maxwell, 1997), pp. 186-187.

[78] For further information concerning the limit of donor restrictions providing a benefit back to the donor, see *Charity Newsletter No*. 9 (December 2000).

organizations of religious denominations) from owning, either directly or indirectly, more than a 10% interest in a business. Section 3(1) and (2) of the said Act states that if a charity obtains an interest in a business that represents more than a 10% interest in the business, the charity must dispose of the interest in excess of 10% within 7 years after the death of the testator in the case of a bequest under will, or within 7 years after the date of the instrument where the gift is received other than by a will. This time frame, however, may be extended by an order of the court if the court is satisfied that the extension will benefit the applicable charitable purposes.

An often overlooked provision of the *Charitable Gifts Act* is Section 6 which states that the proceeds of such disposition <u>must</u> be invested only in accordance with authorized investments under the *Insurance Act*. Some commentators have suggested that this mandatory investment power would take precedent over a broader general investment power contained within the letters patent of a charity.[79]

<u>B. Valuing and Receipting Shares in Publicly Traded Companies</u>

For charities and gift planners alike, the fair market value of publicly traded shares is vitally important, as it determines (a) the actual amount of the donation that the charitable organization receives, (b) the amount that must be entered on the charitable donation receipt for the donor; and finally, (c) the tax credit that the donor can claim on their annual income tax return. Valuation of publicly traded shares can often be difficult, but is a crucial element of charitable fundraising.

The CRA policies regarding valuation of publicly traded securities are based on a number of documents which have been posted to the CRA website to explain CRA's method of valuating the fair market value of items. In Information Letter CIL – 1999 -04 and Information Circular IC-89-3 entitled "Policy Statement on Business Equity Valuators", "fair market value" was defined as:

> "… the <u>highest price</u>, expressed in terms of money or money's worth, obtainable in an <u>open and unrestricted market</u> between <u>knowledgeable,</u>

[79] See Francis K. Boyle, *Legal Aspects of Charitable Gifts: Issues Relating to Community Foundations* (Ottawa: Community Foundations of Canada, 1998) at 36.

> informed and prudent parties acting at arm's length, neither party being under any compulsion to transact."

In *Registered Charity Newsletter* No. 12, CRA sets out its general rule with respect to valuating publicly traded securities:

> General rule - "closing bid price of the shares on the date it is received or the mid-point between the high and the low trading prices for the day, whichever provides the best indicator, given the circumstances, of fair market value on normal and active market trading."

In addition to its general rule, CRA also considers other factors when valuating publicly traded securities, including:

- the size of the block of shares in relation to the whole
- the volume traded
- the attributes of the shares
- whether the donor had control or was a minority shareholder
- whether there were any restrictions on the transferability of the shares
- whether the shares were thinly traded, requiring a look at trades over a longer period of time

For reference purposes, Information Circular IC-89-3 noted above also includes additional factors used by CRA:

- The nature of the business, and history of the business from its inception.
- The general outlook, the specific outlook and condition of the particular industry and the company's position in the industry.
- The balance sheet, the financial condition and the capital structure of the particular company.
- The company's earnings record and its earnings power.
- The dividend-paying capacity of the specific company.
- The existence of goodwill and/or other intangible assets.
- Sales of the company's stock.
- The size of the specific shareholding to be valued.
- The stock market prices of comparable stocks of reasonably similar corporations in the same line of business, where these shares are actively traded in an open, unrestricted and public market.

- The value of the corporate assets underlying the shares.

Other factors relevant to the valuation of specific shareholdings include:

- options, other buy-sell agreements or other contractual rights or obligations;
- control or minority shareholder interests;
- the rights and privileges of the various classes of shares under the company's letters patent, bylaws, or memorandum of association; and
- corporate-owned life insurance.

C. Gifts of Real Estate

A fundraising program adopted by some charities involves encouraging donors to give different types of gifts in kind. However, since such programs may result in a gift of real estate, there are a number of risk factors that the charity should take into account before accepting a gift of real property. Those factors are set out below as follows:

(1) Restrictions on Property Investments Under the Charities Accounting Act

The Public Guardian and Trustee of Ontario, in its *Not-For-Profit Incorporators Handbook,* summarizes the provisions of the *CAA* that restricts the ability of a charity to own real property as an investment for longer than three years as follows:

> A charity, unless special legislation specifically provides otherwise, can hold land only for the purpose of actual use or occupation for the charitable purposes of the charity. A charity, therefore, cannot hold land for purposes of leasing or investment.[80]

Section 8(2) of the *CAA* specifically provides as follows:

> Section 8(2) - Where in the opinion of the Public Guardian and Trustee, land held for a charitable purpose,

[80] *Supra* note 21 at 60.

> (a) has not been actually used or occupied for the charitable purpose for a period of three years;
>
> (b) is not required for actual use or occupation for the charitable purpose; and
>
> (c) will not be required for actual use or occupation for the charitable purpose in the immediate future,
>
> the Public Guardian and Trustee may vest the land in himself or herself...

Thereafter the Public Guardian and Trustee may sell the lands and apply the proceeds of sale for the applicable charitable purpose. This restriction, though, does not apply to surplus land owned by an unincorporated religious organization, since under the *Religious Organization Land Act*, a religious organization is able to lease surplus land for up to 40 years.

(2) Liability for Toxic Property

A charity and its board of directors need to be aware of the liability that could result in the event that the land being acquired was contaminated. Contamination could occur through something as innocuous as a slow leak from an abandoned underground oil tank, or from more overt contamination caused by current or former owners or tenants of the property.

No matter how the contamination may have been caused, the provisions of the *Environmental Protection Act*[81] mean that not only would the charity be responsible for the cost of cleaning up the contamination, but the directors of the charity would also be exposed to personal liability for such costs, as well as being exposed to fines and penalties as was the case with the board of directors in *R. v. Bata Industries Ltd*.[82]

[81] R.S.O. 1990, c. E-19.

[82] *R. v. Bata Industries Ltd.,* (1993), 14 O.R. (3d) 354(Ont. Crt. of Jus. (Gen. Div.)), reversed on appeal on the matter of terms of a probation order, (1995), 127 D.L.R. (4th) 438 (Ont. C.A.), also see Arthur Drache, "Solid Ground? Real Estate Donations", *Canadian Not-For-Profit News* ,December 2002, at p. 95.

(3) Lack of Due Diligence Searches

The fact that a charity is to receive ownership of real property as a gift should not stop the charity from conducting all of the regular due diligence searches that would normally be done if the charity were purchasing property from a third party for fair market value. The usual searches that are conducted in a normal real estate transaction should be completed, including a full search of title and inquires about zoning, work orders, taxes, insurance, as well as having a building inspection conducted.

(4) Inability to Manage Real Property

Even if there are no overt risks in a charity owning a particular piece of real estate, not every charity will have the ability to adequately manage a real property portfolio, even over the short term of three years as prescribed by the *CAA*. A charity would therefore need to determine whether the risks associated with managing real property compared to the income to be earned is reasonable in the circumstances. If not, the charity should consider not accepting a gift of real property in the first place or suggesting that the donor dispose of it and then subsequently gift the sale proceeds to the charity. The board of directors of the charity must be able to satisfy themselves that owning real property will not result in an unreasonable risk or a loss to the charity, otherwise the directors could be found personally liable for the losses resulting with owning real estate.

D. Receiving Used “Gifts in Kind”

Some charities have embarked on a fundraising program of seeking donations of used “gifts in kind”, such as used motor vehicles, and either sell such items to a wholesaler or to the public directly. This type of fundraising program would require that the charitable receipt being issued to the donor be for no more than the fair market value of the item as determined by an appraisal if the value exceeds $1,000.00.

However, the more serious issue associated with receiving used "gifts in kind", particularly when they involve used automobiles, is potential liability to third parties who are end users of such items, particularly where the charity has itself sold the item itself to a third party. The board of directors of a charity should be aware of the potential for legal action that could occur if a third party purchaser of a used item was to become injured and was to sue the charity and/or its board of directors based on allegations that the charity failed to ensure that the used item was properly checked for defects which the charity knew or should have known might cause injury. In approving this type of fundraising program, it is likely that the directors of the charity will have primarily focused on the revenue that would be earned without first identifying and considering the potential legal liability associated with such program.

Even with the sale of lesser "gifts in kind", such as used furniture, equipment or recreational items, i.e. bicycles, the charity and its board of directors could be at risk from potential legal action unless they have implemented appropriate due diligence procedures to ensure the reasonable safety of the items being sold, or alternatively have properly warned third party purchasers of the risks involved in buying used items as evidenced by a signed acknowledgment and possibly even a release by the purchaser. The fact that the Government of Ontario has had to adopt legislation in the form of the *Donation of Food Act*[83] to protect charities, their directors and employees from liability with regard to donated food that is distributed by food banks and other charities underscores the extent of the risk that charities may be exposed to in reselling used items.

E. Self Insured Gift Annuities

(1) The Difference Between Self Insured and Reinsured Gift Annuities

One of the more controversial methods of fundraising, although not widely in use, involves the issuance of self insured gift annuities. In its most basic terms, a gift annuity involves a donor who makes a payment to a charity in return for a contract whereby the charity agrees to pay the donor a certain amount of money on a regular basis during the lifetime of the donor and/or a surviving spouse, with any residue on death being kept by the charity as a

[83] S.O. 1994, c. 19.

gift. Gift annuities are issued either as self insured annuities or as reinsured annuities. The difference between the two is summarized below as follows:

(a) Self Insured Gift Annuity

A self insured gift annuity is an annuity that is issued by the charity where the charity itself is responsible to make all payments to the donor/annuitant. In the event that the donor/annuitant dies before the capital of the original payment is expended, the balance of the capital and any accrued interest will be retained by the charity as a charitable gift. On the other hand, if the original capital payment is expended before the donor/annuitant dies, then the charity must use its own funds to meet the obligations of the annuity contract until the death of the donor/annuity or his or her surviving spouse dies if there is a "second to die" provision in the annuity contract. As such, it is the charity's responsibility to underwrite the risk associated with the annuity contract.

(b) Reinsured Gift Annuity

A reinsured gift annuity, on the other hand, involves a charity arranging for a donor/annuitant being able to purchase an annuity contract through an insurance company that works in conjunction with the charity. The difference between the payment made by the donor/annuitant and the cost of purchasing the annuity will be kept by the charity as a charitable gift.

(2) Legal Risks Associated with Self Insured Annuities

Since reinsured gift annuities are issued by licensed insurance companies, the legal risks associated with such contracts are assumed by the insurance company. However, where there are fundraising programs that involve self insured gift annuities, there are a number of serious legal concerns that arise. Those concerns are summarized below as follows:

(a) Lack of Corporate Authority

With the exception of a few religious denominations and other charities created by federal and/or provincial incorporating legislation that provide for specific corporate authorization to issue annuities, no other charities have the necessary corporate power to issue self insured annuities. If a charity without corporate authority were to issue self insured annuities and the charity was to suffer a loss from the sale of such annuities, it is possible that the directors could be held personally liable for such loss in having allowed the charity to undertake an *ultra vires* fundraising and/or investment program.

It should be noted as well that charitable foundations are unable to issue annuities at all as a result of the restrictions imposed upon foundations not to incur debt other than a few limited instances described in subsections 149.1(3) and (4) of the *ITA*.

(b) Violation of the Insurance Act

Whether or not a charity has the corporate power to issue an annuity, there is the separate issue of whether or not the selling of an annuity contract constitutes the issuance of insurance requiring licensing under the *Insurance Act* of Ontario. There has been an ongoing debate for over ten (10) years concerning whether a self insured annuity constitutes an insurance product that is regulated by the *Insurance Act.* The Canadian Charitable Annuity Association (formerly known as the 'Canadian Association on Charitable Gift Annuities') suggested in its submission to the Ontario Law Reform Commission on the Law of Charities [84] that self insured gift annuities were not subject to any explicit or implicit provincial government regulation in Ontario. They supported their position by the fact that many religious denominations have been issuing annuities for decades and no one at the Superintendent of Financial Services for Ontario (formally the Superintendent of Insurance for Ontario)

[84] See submission made by the Canadian Association on Charitable Gift Annuities to the Ontario Law Reform Commission on the Law of Charities, *supra* note 12 at 589.

has challenged the ability of those charities to issue annuities, nor has the Superintendent asserted any jurisdiction over those charities that do issue annuities.

However, the Public Guardian and Trustee of Ontario takes the position that an annuity contract does involve the issuance of insurance that requires a charity to be licensed under the *Insurance Act*.

> "...the term "insurance" is defined under the Insurance Act as, "to pay a sum of money upon the happening of a certain event...". The corresponding term "insurer" includes reference to any party who distributes or publishes any proposal in Ontario that makes or causes to be made any written or oral solicitation for insurance and deems such person to be carrying on business in Ontario within the meaning of that Act. Accordingly, it appears that a vendor (including a charity) of annuities in Ontario would come within the purview of the Act and therefore would be required to obtain a license from the Superintendent of Insurance and comply with the requirements of that legislation, including maintenance and appropriate investment of adequate reserves for the liability for the annuities."[85]

The Public Guardian and Trustee of Ontario does not distinguish between charities that have the corporate power under special legislation to issue annuities and those that do not. Clearly, a charity that does not have the corporate authority to issue annuities would be unable to obtain a license to issue annuities, since it would not have the corporate power to issue annuities even if it was licensed. However, it would appear that simply because a charity has the corporate authority under special legislation to issue annuities, such statutory corporate authority does not exempt the charity from having to be licensed under the *Insurance Act* or otherwise comply with the requirements of that Act. "*A charity, in order to apply for a license, must be able to demonstrate that it has the corporate power to undertake such activities under its Letters Patent.*"[86] *[Emphasis Added]*

[85] *Supra* note 21 at 65.
[86] *Ibid* at 66.

With regard to the applicability of insurance legislation in other provinces, Frank Minton and Lorna Summers in the second edition of their book on fundraising entitled "*Charitable Giving in Canada*", summarized the general situation in other provinces as follows:

> "Since gift annuities are similar to commercial annuities, they come under the jurisdiction of provincial insurance commissioners. Some of the insurance commissioners, who have addressed the subject, have taken the position that only licensed insurance companies can issue gift annuities and that they must be acquired through licensed insurance agents. Thus, they conclude that charities self-insuring gift annuities are in contravention of the insurance acts." [87]

In 1999, the Superintendent and Chief Executive Officer of Financial Institutions in British Columbia confirmed that the definition of "insurance business" found in Section 1 of the *Financial Institutions Act*[88] of British Columbia ("*FIA*") included the issuance of a contract of insurance, and that under section 75 of the *FIA*, only those companies with authorization to carry on insurance business could do so. Section 76 of the *FIA* enumerates certain exemptions from the above requirement. However, charitable organizations did not fall within the purview of any of these exemptions.

However, effective July 26, 2002, British Columbia addressed the exemption of charitable organizations statutorily through *FIA* Regulation 219/2002, entitled "Insurance Company Exemption Regulation", which provides for the issuance of "charitable gift annuities" as set out in section 13 of the Regulation:

Charitable gift annuities

13 (1) In this section:

"charitable gift annuity**"** means an annuity

[87] Minton & Somers *supra*, note 1 at 167.
[88] R.S.B.C. 1996, c. 41.

(a) provided by a charitable organization in return for a transfer of cash or other property by a donor to the charitable organization, and

(b) with a value that is less than the value of the cash or other property transferred and the difference in value is a charitable deduction under the *Income Tax Act* (Canada);

"charitable organization" means a charitable organization that is a registered charity, as defined in section 248 of the *Income Tax Act* (Canada).

(2) Section 75 of the Act does not apply to a charitable organization providing a charitable gift annuity to a donor, on the condition that the charitable organization discloses in writing to the donor, when entering into an agreement with the donor, that

(a) the charitable gift annuity is not insured by an insurance company regulated under the Act, and

(b) the charitable organization is exempt from the regulatory requirements of the Act.

As such, charitable organizations that comply with section 13 of *FIA* Regulation 219/2002 are exempted from the requirements under section 75 of the *FIA*, and are therefore authorized to conduct insurance business in British Columbia with respect to the issuance of charitable gift annuities.

It would therefore appear that charities are not required to be licensed as an insurance company, at least in British Columbia, to issue self insured annuities. However, for other provincial jurisdictions, like Ontario, charitable organizations should be aware that there are not similar exemptions. As such, charities must determine whether exemptions for charitable organizations to issue self-insured annuities exist under the applicable provincial legislation in each jurisdiction, notwithstanding that the charity may have corporate authority to issue annuities in their incorporating legislation.

(c) Operational Financial Risks

Even if self insured annuities did not fall within the parameters of provincial insurance legislation, since an annuity is a sophisticated financial product, there are considerable financial risks that a charity would be exposed to in issuing self insured annuities. It is beyond the scope of this paper to discuss those risks in any detail. However, one risk that a charity would need to review would be the expectation that a charity will have sufficient assets in reserves to cover the outstanding obligations under all annuity contracts that have been issued, together with an appropriate reserve for unforeseen contingencies. In addition, the size and sophistication of the charity would need to be reviewed to determine whether an annuity program was a reasonable and prudent investment for a charity to be involved with, given the potential personal liability of the board of directors in the event that the charity was to suffer a loss from the annuity program.

(3) U.S. Experience with Self Insured Annuities

The issuance of self insured annuities has generally been a more common practice in the U.S. than in Canada. However, in many U.S. states, the issuance of self insured annuities has become regulated by state legislation. As of 1998, at least 23 states had imposed some type of regulatory limitations on the issuance of gift annuities by a charity.[89] Most of the regulatory restrictions have taken the form of amendments to existing insurance legislation and establish minimum disclosure requirements to the public, annual reviews of the annuity programs, and mandatory requirements concerning the establishment of reserve funds.

In addition to being subject to general insurance legislation in some states and specific legislative restrictions in other states, the issuance of self insured annuities resulted in a large class action law suit being brought against the American Council on Gift Annuities and

[89] "Annuity Payouts Should Decline Slightly, Council Suggests" *Nonprofit Alert* (June 1998) Gammon & Grange, Washington D.C. at 6.2.

several Lutheran charities, as well as numerous other charities that were subsequently added. The class action was based on allegations of price fixing.[90] The threat to the financial viability of the charities affected by the class action was such that Congress had to intervene to protect charities by adopting remedial legislation in 1995 and 1997 that exempted charitable gift annuities from most federal anti-trust and securities law.[91]

The highly regulated nature of the self insured annuity field in the United States, as well as the spectre of litigation experienced by many charities involved in self insured annuities in the U.S. serves as a warning of possible development that might happen in Canada in relation to self insured annuities.

(4) General Observation on Self Insured Annuities

Given the considerable risks involved with self insured annuities, particularly as they relate to non compliance with applicable provincial insurance legislation, and in consideration of the difficulties that have been experienced in the United States, any charity that is considering embarking on a self insured annuity program should carefully consider the legal consequences before doing so. Even charities that have specific corporate authority by special legislation to issue annuities, presumably under both federal and provincial parallel legislation, may want to consider whether they are required to be licensed under applicable provincial insurance legislation. Simply because legal challenges have not been encountered in the past on this issue should not be interpreted as an assurance that challenges will not occur in the future.

For those charities that do find gift annuities an attractive fundraising program, there is the option of the charities working in conjunction with an insurance company with regards to a

[90] *Ozee v. American Council on Gift Annuities*, 110 F.3d 1082 (5th Cir. 1997). The antitrust suit was filed in 1994, "Court Battle Over Annuity Rates Continues, Despite Federal Law" *Nonprofit Alert* (Mar. 1996) Gammon & Grange, Washington D.C. at 1.1.

[91] "States Amend Laws Following Gift Annuities Case" *Nonprofit Alert* (Sept. 1996) Gammon & Grange, Washington D.C. at 6.1. See also "Congress Passes New Relief Bill for Charitable Annuities" *Nonprofit Alert* (Aug. 1997) Gammon & Grange, Washington D.C. at 1.2.

reinsured gift annuity program. Although this option is not completely devoid of liability exposure, the utilization of a reinsured annuity program would be fundamentally less risky than the charity issuing the annuities itself.

F. Debt Instruments Forgivable on Death

Another type of fundraising vehicle that is frequently used as part of an estate planning program is the issuance of a debt instrument that state on its face that it is forgivable on death of the holder. The debt instrument is normally in the form of a promissory note, bond, or certificate of deposit. The debt instrument will carry a low or zero interest rate, allowing the charity to reinvest the monies and earn income on the "interest spread", or alternatively to use the loan for operational purposes of the charity at an interest rate considerably less than what the charity would otherwise have to pay to a financial institution to borrow monies.

The charity, though, will generally not consider the debt instrument to be a "real" debt. This is because the charity will have the donor co-sign the debt instrument stating that the outstanding indebtedness is to be forgiven upon the death of the donor or the spouse of the donor if there is a "last to die" provision included in the instrument.

What the charity and its board of directors may fail to understand is that the forgiveness of the debt on death can only be accomplished by a testamentary instrument properly signed and witnessed by two witnesses who are not beneficiaries. When the donor dies, the debt instrument would constitute one of the assets of the estate. However, since the intent to forgive the debt on death by the testator would not have been properly executed by a testamentary instrument, the debt would not be forgiven on death and would remain as an asset of the estate instead of becoming a gift to the charity.[92] In addition, the estate would have an obligation to recover the debt from the charity notwithstanding what the testator had wanted. Even if an estate trustee of a testator's estate were

[92] See *Carson v. Wilson* [1961] O.R. 113, 26 D.L.R. (2d) 307 (Ont. C.A.) for a discussion of when a document will constitute a testamentary disposition and will need to meet the execution requirements for a will.

insured to honour the wishes of the trustee and forgive the debt owned by the charity, the estate trustee could not do so without court authorization.[93]

Where a promissory note remained outstanding on death, the directors of the charity who had authorized the incurring of the debt in the first place on the mistaken belief that the debt would be forgiven on death could be exposed to personally liability for allowing the charity to incur an improvident indebtedness that lacked the legal mechanism required to have it self liquidate on death. Without the assurance that the debt would be forgivable on death, it is unlikely that the directors would have incurred the debt in the first place. However, such misunderstanding of the law would not exempt the directors from liability, although it might cause the directors to look for indemnification from legal counsel for the charity if the circumstances of the advice sought from the lawyer was such that the lawyer should have brought the risk to the attention of the board of directors.

A separate but equally serious issue is whether a debt instrument forgivable on death would constitute a contract of insurance under the *Insurance Act,* since such debt instrument would appear to involve the payment of monies dependent upon the life of an individual. Whether a debt instrument constitutes a contract of insurance depends upon the circumstances and wording of the debt instrument in question. If it did, the charity would be required to become licensed as an insurance company under applicable insurance legislation.

G. Soliciting Investments from the Public

(1) Situations Where Charities May Decide to Seek Investments from the Public

Normally fundraising programs undertaken by charities seek gifts of monies and/or property. However, there are situations were a charity may decide to embark upon a program of raising monies by seeking investments from the public, whether they be from supporters of the charity or from unrelated members of the public. Some common situations where a charity may decide to seek investments from the public are listed below:

[93] *Re Snowden*, *supra*, note 58.

- when donations from the current donor base has been exhausted in attempting to meet the current operating expenses of the charity;

- when it is impractical to raise monies through a gift program alone and a charity is reluctant or unable to pay the cost associated with borrowing from a regular financial institution;

- when there is a need by the charity for a “quick fix” of cash because of an unexpected shortfall of funds or increase in expenses;

- when the charity borrows money with a long term expectation that such loans will become forgivable loans on death, as discussed previously;

- when a large sum of money is required for a capital program, such as a building project;

- when difficulties are encountered in securing and maintaining a reliable flow of funds to meet the expenses of the charity;

- when traditional sources of borrowing from financial institutions are no longer available; and

- when there is an intentional reliance by the charity upon its exempt status under the *Securities Act* from the registration and prospectus requirement normally required to issue securities to the public.

(2) Different Types of Investments offered by Charities to the Public

Some of the investments that are generally offered to the public by charities include the following:

- unsecured instruments of debt, such as promissory notes, including those that are forgivable on death;

- unsecured loan certificates;

- guaranteed loan certificates, often secured against the assets of the charity or by the personal guarantee of certain named individuals;
- bonds, both secured and unsecured, normally issued by churches and other religious institutions;
- debentures, both secured and unsecured; and
- mortgage certificates issued pursuant to a mortgage back certificate program.

(3) Application of the Securities Act

All of the above forms of investments would likely constitute the issuance of a "security" under the *Securities Act* (Ontario). However, charities are normally exempt from the registration and prospectus requirement of the *Securities Act* (Ontario). Section 35 subsection (2), paragraph 7 of the *Securities Act* (Ontario) states that:

> Section 35(2): Subject to the regulations, registration is not required to trade in the following securities:
> ...
> Par. 7 - securities issued by an issuer organized exclusively for educational, benevolent, fraternal, charitable, religious or recreational purposes and not for profit, where no commission or other remuneration is paid in connection with the sale thereof.

Although it is generally presumed that a charity is exempt under the *Securities Act* (Ontario), what is not always understood is that the exemption is subject to the requirement that "*no commission or the remuneration is paid in connection with the sale thereof"*. As such, a charity that issues securities would need to ensure that no commission, either directly or indirectly, was paid to any individual or business, such as a professional fundraiser, with regards to the issuance of any type of securities, i.e., promissory notes, bonds, certificates, or debentures.

This requirement, though, would not necessarily preclude a charity from paying a professional fundraiser for general fundraising services. However, if the work provided by the fundraiser was associated in any way with the sale or issuance of any type of investment security, the sale of those securities would likely no longer be exempt under the *Securities Act* (Ontario). Instead, the charity may need to become registered as an issuer of securities under the *Securities Act* (Ontario), a requirement that obviously no charity would want to do or would realistically be able to undertake.

Since there are serious financial penalties, as well as the possibility of even imprisonment that can result from violations of the *Securities Act* (Ontario), it is essential that a charity and its board of directors take appropriate steps to ensure that any proposed sale of securities to the public is exempt from the requirements of the *Securities Act* (Ontario) before proceeding with issuing the securities.

British Columbia is generally considered another charity-friendly jurisdiction with regards to securities legislation. Under the *Securities Act* (British Columbia), section 46(g) provides that organizations operating exclusively for charitable purposes are permitted to trade securities without registration if they meet specific requirements:

Exemption when trading in certain securities

46 Subject to the regulations, a person may trade in the following securities without being registered under section 34 (1) (a):

> (g) securities issued by an issuer organized exclusively for educational, benevolent, fraternal, charitable, religious or recreational purposes and not for profit, if
>
> > (i) no part of the net earnings of the issuer accrue to the benefit of a security holder,
> >
> > (ii) no commission or other remuneration is paid in connection with the sale of the securities,
> >
> > (iii) in the case of a trade made by the issuer, an information statement in the required form is delivered to the purchaser before an agreement of purchase and sale is entered into, and

> (iv) in the case of a trade made by the issuer, the information statement is filed not later than 10 days after the trade;

It is anticipated that a new *Securities Act* (British Columbia) will be proclaimed in force in November 2004. The new securities framework will retain an exemption for charitable organizations under section 53 of the new *Securities Rules,* which largely reiterates the exemption in place under the current legislation, and reads as follows:

> Trade of security of not-for-profit issuer
>
> 53 A person is not required to register to trade a security of an issuer organized for educational, charitable, religious or recreational purposes and not for profit, if
>
> (a) no part of the net earnings of the issuer accrue to the benefit of a security holder,
> (b) no commission or other remuneration is paid in connection with the trade, and
> (c) for a trade by the issuer, an information statement that complies with section 104 is delivered to a person before the person agrees in writing to purchase the security.

Despite the fact that the securities legislation of many provinces allows charitable and non-profit organizations to issue securities, such organizations must still be very careful when doing so. In an article entitled “Charities must exercise caution when issuing securities”, authors Robert Stewart and Walter Wagnleithner advised that, although Canadian charities and non-profit organizations have been able to issue securities without a prospectus and without complying with securities legislation in the past, “the exemption will be unavailable if that entity adopts even a single purpose that is not benevolent in nature…[as] Ontario Securities Commission rulings have taken the same stance”.[94]

Furthermore, the authors warn that charities and non-profit organizations should not believe that compliance with tax legislation is synonymous with compliance with securities legislation, even though trust and tax laws are similar in their requirements for charities. Good standing with CRA is not a defence for non-compliance with securities legislation.

[94] Robert Stewart, and Walter Wagnleithner. “Charities must exercise caution when issuing securities”, *The Lawyers Weekly*, February 14, 2003, p. 14.

(4) Liability Exposure to the Charity and its Directors

(a) Situations Where Investors May Become Antagonistic

In the event that a charity runs into financial difficulties and is unable to fully repay the investment and/or accrued interest owing thereon, the investors and/or their surviving families may become antagonistic, either because the investor now needs the monies invested for his or her own use or because the investor feels that he or she may have been mislead by the charity when the investment was made. Alternatively, an attorney for an investor under a power of attorney or an estate trustee for the estate of a testator may decide to commence legal action against the charity to challenge the legality of the investment fundraising program in an effort to establish the personal liability of the board of directors of the charity in a situation where the charity has insufficient assets to satisfy all investor claims.

(b) Allegations of Negligent Misrepresentation

If an investor, or the attorney or estate trustee on behalf of an investor, was to commence legal action against the charity and its board of directors, it would likely be based upon an allegation of negligent misrepresentation by the charity and its directors as a result of the investor not fully understanding the nature of the investment that was being offered by the charity. In this regard, the Supreme Court of Canada in *Queen v. Cognos Inc*[95] has held that negligent misrepresentation will be found where:

- there is a duty of care based upon the existence of a "special relationship";
- there is a representation that is untrue, inaccurate or misleading;
- the representation is made negligently;
- reliance is placed upon the representation; and
- damages result.

[95] *Queen v. Cognos Inc.* [1993] 1 S.C.R. 87, 99 D.L.R. (4th) 626 (SCC).

(c) Examples of Possible Negligent Misrepresentation

Examples of situations were a court might find that the charity and/or its board of directors liable for negligent misrepresentation involving the sale of investment securities to the public are listed below:

- failure by a charity to adequately inform investors of the unregulated nature of securities being offered for sale to the public pursuant to the general exemption available to charities from disclosure requirements under the *Securities Act;*

- failure by the charity to provide reasonable disclosure information concerning the details of the investments being offered, such as;

  - providing a full explanation of the purpose of the investment monies being raised by the charity;
  - explaining what security for the investment, if any, is being offered to the investor;
  - explaining the nature of the risks associated with the investment; or
  - explaining the actual investment returns that the investor can expect to receive from the investment as opposed to a "guesstimate" only;

- making false or misleading statements about the financial strength or vulnerability of the charity;

- suggesting that investments may be secure when they are not, i.e., calling unsecured promissory notes "debentures", "bonds", or "certificates", when no security is being provided;

- failure to provide the specific type of security that an investor might reasonably presume would be in place, such as a collateral mortgage against church property to secure the holders of church bonds issued to construct a new sanctuary;

- making false or misleading statements about the true nature of the securities being offered for investment, i.e., suggesting that a security is in the form of a first mortgage when the mortgage security can at the option of the charity be postponed into a second mortgage without notice or the approval of the investors;

- failure by the charity to establish a realistic sinking fund to retire the debt being incurred by the charity in issuing securities to the public in the first place;

- making unsubstantiated predictions concerning the income to be produced from the securities being offered, i.e., statements such as "better than market investment";

- failure by the charity to recommend that a potential investor should first obtain independent legal advice before proceeding with the investment;

- listing the names and occupations of directors and/or officers of the charity in sales brochures in an attempt to add credibility to the securities being offered for sale; and

- failure to disclose an actual or pending financial crisis that the charity is attempting to address by the infusion of monies through a public offering of investments.

(d) Legal Avenues Available to an Antagonistic Investor

If an investment issued by a charity did go sour, an antagonistic investor, or the estate of a deceased investor, might seek recovery of the lost investment through a number of legal avenues, including:

- commencing legal action against the charity and its board of directors based upon negligent misrepresentation;

- seeking an order for a public inquiry of the fundraising practices of the charity under Section 6 of the *CAA*;

- filing a complaint with the Public Guardian and Trustee of Ontario and requesting that their office investigate the charity under Section 3 of the *CAA*; or

- filing a complaint with the Ontario Securities Commission in the event that the pre-conditions for the charitable exemption under Section 35 subsection (2) paragraph 7 of the *Securities Act* is not complied with, i.e., where there has been a direct or indirect payment to a fundraiser involved in the issuance of securities by the charity.

H. Implications of Bill C-45 (Westray Mines) on Fundraising[96]

Fundraising initiatives are more than likely to be supervised, administered, or at least acquiesced by senior officers, as well as even the directors of a charity. The Federal Government has recently introduced amendments to the *Criminal Code of Canada,* R.S.C. 1985 c.C-46 (the "Criminal Code"), which will affect when organizations and their representatives may face criminal liability for negligent conduct. Bill C-45, "*An Act to Amend the Criminal Code (Criminal Liability of Organizations)*", received Royal Assent on November 7, 2003, but has not yet been proclaimed into force at the time of this article's publication. The amendments are normally identified as the "Westray Mines" Amendments. It is anticipated that the amendments will come into force and effect shortly. Fundraising activities as well as activities in support of charitable programs that may be impacted by Bill C-45 could possibly include marathons, volunteer building projects in Canada and abroad, county fairs, children's carnivals, festivals, sporting events and other like events.

When the amendments are proclaimed into force, Bill C-45 will impose a Criminal Code duty on organizations and their representatives to protect their workers, volunteers and the public by creating a Criminal Code duty similar to the duty already found in the *Occupational Health and Safety Act* (Ontario), which requires that employers take "*every precaution reasonable in the circumstances for the protection a worker*".[97]

The amendments contemplated by Bill C-45 will apply not only to corporations, but to all types of organizations, including non-share capital corporations, profit-making corporations, partnerships, and unincorporated organizations. "Organization" is defined in Bill C-45 to mean:

> (a) a public body, body corporate, society, company, firm, partnership, trade union or municipality, or
> (b) an association of persons that
> (i) is created for a common purpose,

[96] Excerpts of this section were previously published in "Bill C-45 and Its Effect on Criminal Liability and Insurance Coverage for Charities.", by Mervyn F. White, Bruce W. Long, and U. Shen Goh Also found at www.charitylaw.ca under *Charity Law Bulletin* No. 35.

[97] *Occupational Health and Safety Act*, R.S.O. 1990, c. 0.1, s. 25 (2)(h).

(ii) has an operational structure, and
(iii) holds itself out to the public as an association of persons.

The key reforms to the Criminal Code proposed by Bill C-45 include, but are not limited to:

1. Imposing criminal liability on organizations will no longer require that the criminal conduct or act of the organization be committed by a directing mind of the organization. Traditionally, to impose criminal liability on corporations in Canada, the Crown, applying the "identification theory", had to establish that the directing minds of the organization and the organization itself were effectively one and the same in committing the offence. Establishing this will no longer be necessary to obtain a conviction under Bill C-45.

2. The Crown will now be able to "cobble together" the essential elements of a criminal offence, such that the *actus reus* (the "Physical Element") and the *mens rea* (the "Mental Element") can be attributed to separate individuals within the offending organization in order to establish criminal liability.

3. The class of representatives of the offending organization who can commit or contribute to the Physical Element of the offence has been expanded from directors and officers to all representatives who act on behalf of the organization, such as directors, partners, employees, members, agents or contractors of the organization.

4. For crimes of criminal negligence, the Mental Element of the offence will be proven against offending organizations from the collective fault of the senior officers of the organization. In other words, a reckless corporate culture, which is tolerated by senior management, may be sufficient to establish the Mental Element of the criminal offence.

5. Where the criminal offence is based on allegations of criminal intent or recklessness, the Crown will establish the Mental Element where a senior officer is a party to the criminal

offence, or where a senior officer had knowledge of the offence but failed to take all reasonable steps to prevent or stop the offence.

6. Finally, a specific and explicit legal duty will be imposed on those who direct the work or task of others, to ensure that such individuals take all reasonable steps to prevent bodily harm at work.

By introducing the possibility of bringing criminal negligence charges against those who direct the work of others, Bill C-45 will seriously affect insurance coverage for directors and officers, where such insurance coverage was previously available. For example, many Directors and Officers liability insurance policies provide for a duty to defend against civil lawsuits founded in negligence, or against allegations laid under regulatory legislations, such as the *Occupational Health and Safety Act* (Ontario). This duty to defend would impose on the insurer a duty to provide and pay for reasonable legal expenses incurred in defending a claim. Normally, such a duty to defend would not extend to allegations of criminal conduct. This is based, in part at least, on the public policy principle that one cannot buy insurance to cover criminal activities. As such, it is possible that a director or officer could be charged under the new provisions of the *Criminal Code* for conduct that would have traditionally been considered a regulatory offence (and for which a duty to defend would have been imposed upon the insurer) and not be covered for legal defence costs.

What is striking about this is that activities which previously resulted in civil liability based on negligence may now be adjudged criminal in nature. This, in turn, will detrimentally affect insurance coverage. It must be remembered that insurance policies usually impose two obligations on insurers: the duty to defend (discussed above) and the duty to indemnify (i.e., the duty to pay for the damages sustained). Most insurance policies, either through specific exclusionary clauses, or caselaw based on public policy, generally do not cover conduct that is designed to cause a loss or for which the loss is predictable. Criminal conduct, by its very nature, is predicated in the predictability of the outcome or loss sustained. This is the Mental Element of the criminal offence. A criminal act requires that a perpetrator turns his or her mind to committing the act, or, in the certain limited cases, wilfully turn his or her mind away from the dangers posed by his or her activities (wilful blindness or recklessness).

As such, the distinction between insurance coverage for non-intentional torts versus intentional torts is very important in light of the amendments introduced through Bill C-45. By its very nature as a criminal charge (which contemplates either a form of criminal intent or a recklessly negligent mind), Bill C-45, and specifically section 217.1, may have the effect of creating a form of "intentional" or "criminal" negligence. While this may seem illogical and contradictory at first glance, it would appear that the intent of the legislation is to create a new level or type of negligence, which is based on the recklessness of an organization, but for which the penalties imposed are more stringent. It would seem appropriate to anyone that, while a "new" form of criminal negligence has been created by the legislation, the underlying negligence – based on the foreseeability of the event – has not changed, and as such insurance coverage should be provided. It should, however, be anticipated that insurers will attempt to limit their obligations to cover losses arising from such criminal negligence and will argue that it is an excluded risk. Although there are reasonable arguments to be made that insurance should be extended to cover such losses, such arguments may be resisted by the insurers, and will probably require judicial review and determination.

The end result is that charities that carry on activities and programs that expose employees, volunteers or the public to harm, whether that be in relation to its primary charitable programs or with regard to a fundraising program like a walkathon may now be faced with the possibility of criminal liability as a result of Bill C-45.

I. Transferring Capital Funds Between Charities

Another fundraising program that is becoming more common involves one charity, normally an umbrella organization, receiving transfers of capital from a smaller charity that is no longer able to manage such capital funds as an endowment portfolio or wishes to wind up its operations altogether.

In addition to having to comply with the provisions of the *ITA* concerning the transfer of assets from one charity to another charity, i.e, designating the transfer as a "specified gift" under Section 149.1(1) of the *ITA* to avoid including the transfer of capital in the disbursement quota of the recipient charity, there are a number of due diligence steps that the board of both charities should consider. A brief summary of those considerations is set out below as follows:

- A determination should be made concerning whether or not the funds being transferred include donor restricted charitable gifts. It is the obligation of both charities to "look behind the transfer" and determine if there are restrictions that apply, either in the form of a specific donor restricted charitable gift, or by implication, by the terms of the charitable purposes contained in the letters patent of the transferring charity. In either situation, a transfer agreement should be entered into between the two charities to ensure that any applicable donor restricted funds will continue to be complied with by the recipient charity, as well as ensuring that any unrestricted funds are used only in accordance with general charitable purposes of the transferring charity.

- In the event that the charitable funds being transferred include donor restricted charitable gifts where those restrictions are either impossible or impractical to carry out, the recipient charity would need to apply to a court for a *cy-près* order to vary the terms of those restrictions.[98]

- Where donor restricted charitable funds are being transferred, such transfer will involve a change of trustees over such funds from the transferring charity to the recipient charity. This would involve the appointment of the recipient charity as the new trustee pursuant to Section 3 (1) of the *Trustee Act* permitting a "surviving trustee" to appoint a new trustee. However, there may be circumstances where it is necessary to obtain a court order to authorize the transfer of such restricted funds, presumably pursuant to a consent order from the Public Guardian and Trustee under Section 13.(1) of the *CAA*.

(1) Flow Through Funds and Personal Benefit Programs

Often umbrella organizations, like religious denominations or community foundations, may receive gifts that are intended for another party, whether such other party is another charity, an individual, or an organization that is not a registered charity or other form of "*qualified*

[98] Louise J.A. Greig & M. Elena Hoffstein, "Issues Arising from Mergers and Fusions of Charitable Organizations" (1997) 15 *The Philanthropist* 40.

donee" under Section 149.1(1) of the *ITA*. The general rule is that a gift to the charity can only be accepted if the gift is intended to be used by the charity for its own charitable purposes. A charity cannot act as a "conduit" for gifts intended either for another charity or for a non "*qualified donee*" that is not acting as either an agent or joint venture participant pursuant to a written agreement with the charity.[99]

In addition, where the gift is ultimately intended to benefit a named individual or individuals, IT-Bulletin 110-R3, paragraph 15(f) prohibits a donor from receiving a charitable receipt where the gift is directed for the personal benefit of a specified person or family, or where a direct or indirect benefit is received back by the donor or by someone not dealing at arms length with the donor. The position of CRA in IT-110R3 was confirmed in the decision of *R. v. Woolner* in the Federal Court of Appeal[100] discussed later in this paper.

J. Investment Issues in Fundraising

(1) General Comments on Investment Powers

The issues involving the investment of charitable funds have become considerably more complicated as a result of the amendments to the *Trustee Act* establishing a "prudent investor"[101] standard that came into force on July 1st, 1999.[102] In the provinces of Alberta, Newfoundland, Ontario, Prince Edward Island and Saskatchewan, the respective *Trustee*

[99] *Beaudry v. R.*, *supra,* note 56. For an explanation of what is required to transfer monies outside of Canada see an article by Terrance S. Carter entitled "*U.S. Tax Exempt Organizations Commencing Charitable Operations in Canada and International Structuring*" available on the Internet at www.chartiylaw.ca. For a U.S. version of the same article see T. Carter, "How to Structure and Begin Charitable Operations in Canada" (1999) 11:3 *Journal of Taxation of Exempt Organizations,* 128.

[100] See *Woolner v. R*, [1999] F.C.J. No. 1615, (1999) N.R. 129 (F.C.A.). .

[101] See Linda J. Godel, "Investment Powers for Charities across Canada", Toronto: Gowlings, September 2003, at p. 8 Linda J. Godel, "Inter-Provincial Investments Powers for Charities", "*What's New and What's Coming",* Second National Symposium on Charity Law, Canadian Bar Association, Toronto, April 14, 2004, and Carter, Terrance S. ""Pro-Active Protection of Charitable Assets" A Selective Discussion of Liability Risks and Pro-Active Responses". November 20, 2001, also found at www.charitylaw.ca. .

[102] For a general discussion of the issues involving investment of charitable funds, see Timothy Youdan, "Investment by Charities" *Fit to be Tithed II* (Toronto: The Law Society of Upper Canada, Department of Continuing Legal Education, 1998) and in particular the issue of delegation.

Acts each set out a list that governs the elements of a trustee's investment review.[103] Amendments to the *Trustee Act* in 2001, amended certain provisions of *Trustee Act* (Ontario) and *Charities Accounting Act* (Ontario). Under those amendments, a charity in Ontario is able to delegate investment decision making to qualified investment managers subject to certain due diligence requirements. Although it is beyond the scope of this paper to discuss the relevant issues involving investment powers for charities, a brief summary of some of the more important background issues are set out in *Charity Law Bulletin No. 8*[104], and *Legal Issues in Investments of Charitable Funds* available at www.charitylaw.ca.

(2) Variable Investment Powers

What is relevant to a discussion of liability in fundraising is that different fundraising programs and the timing of when those programs are implemented may result in different investment powers having to be complied with. Some situations where variable investment powers might arise are summarized below as follows:

- If the letters patent or special legislation incorporating a charity are silent on investment powers, then the Public Guardian and Trustee takes the position that the applicable investment powers are those set out under the *Trustee Act,* as amended [105].

- If the letters patent or special legislation of a charity establishes a specific investment power for the charity, then that investment power will normally take precedence over the provisions of the *Trustee Act*.

- Where a charity is applying for supplementary letters patent to materially change the objects or powers of the Ontario charity, the Public Guardian and Trustee of Ontario requires that a provision be included in the supplementary letters patent to ensure that any property that was acquired before the supplementary letters patent became effective can only be used in accordance with the charitable purposes and powers as they were immediately before they were varied. This means that the old investment powers in

[103] *Supra* Godel, note 101 at p. 9

[104] For a more detailed discussion see an article by the author *at Charity Law Bulletin* No. 8, at www.charitylaw.ca

[105] *Supra*, note 21 at 58. See also "Duties, Responsibilities, Powers of Directors and Trustees of Charities" *Charities Bulletin No. 3: Information from the Public Guardian and Trustee's Charitable Property Program* (Toronto: Office of the Public Guardian and Trustee of Ontario, July 1999) at 3.

place prior to the issuance of supplementary letters patent would appear to continue to apply to any funds held by the charity at the time of the issuance of supplementary letters patent.

- Funds received by a charity through an endowment agreement, whether by means of an *inter vivos* endowment or a testamentary endowment, may include specific investment powers, in which event such investment authority would take precedence over the general investment powers of the charity.

- In the event that a charity was to receive a transfer of restricted funds from another charity, then the investment powers of the transferring charity would generally constitute the investment parameters for the funds being received by the recipient charity.

- As noted earlier, in the event that an interest greater than 10% in a business is sold within 7 years pursuant to the requirements of the *Charitable Gift Act,* then the proceeds from such sale can only be invested in accordance with the investment powers set out in the *Insurance Act* of Ontario.

From the above examples, it is possible for a single charity to have a number of different investment powers that may apply to various funds held by the charity. It is therefore essential that a charity, its board of directors, management, as well as its fundraisers, become cognizant of the various investment powers that may apply and then ensure that the terms of such investment powers are complied with in relation to the funds in question, failing which the directors of the charity could be exposed to personal liability for breach of trust.

K. Managed or Pooled Investment of Charitable Funds

A number of umbrella charitable organizations, such as religious denominations and community foundations, have initiated or are considering programs whereby the umbrella charity receives monies from other charities, often but not necessarily members of its umbrella group of charities, and then manage those monies as one pooled investment fund in order to maximize returns and reduce administration expenses by investing such funds as a pooled fund. The umbrella organization will normally be entitled to deduct a fee for administrating the pooled fund, but such fee will usually be considerably less than if each participating charity were to invest its funds on its own.

Although the benefit of pooling charitable funds has been recognized in other jurisdictions as charitable, there are a number of legal issues that should be addressed before a charity embarks on such a program. Some of the legal issues that need to be considered are set out below as follows:

- Does the recipient charity operating the pooled fund have the corporate power to operate a pooled fund on behalf of other charities? If not, the recipient charity may need to apply for supplementary letters patent to expand its objects and/or power clauses, subject to obtaining pre-approval from the Charities Directorate of CRA and the Public Guardian and Trustee of Ontario if the charity is incorporated in Ontario.

- Does the investment power of each participating charity permit it to invest charitable monies by pooling those monies through the intermediary of another charity? If not, such arrangement might arguably constitute an unauthorized delegation of investment decision making power.

- Does the investment of monies on a pooled basis for other charities that are not necessarily members of the umbrella charity constitute the business of operating a trust corporation that would require registration under the *Loan and Trust Corporations Act*? In this regard, a letter that the author received in 1984 from the then senior legal counsel for the Public Trustee of Ontario, Crown Estates Department, in his personal capacity rather than in any official capacity, sent in response to a similar question suggested that the *Loan and Trust Corporations Act* might have application:

  > "The definitions in the Loan and Trust Corporations Act of a "loan corporation" and "trust company" would seem to catch any organization that is accepting by way of deposit, sums of money and acting either as agent or as principal in the investment of the money. Section 174 would appear to require a person in Ontario to be registered if he is caught by the definitions and Section 174 is not exempt from Section 2 of the Act".

- Does the placement of funds by a charity with an umbrella charity in a pooled investment fund constitute a "deposit" that may require registration under the *Bank Act*[106] or under the *Loan and Trust Corporations Act* as a regulated deposit? This question has been raised by others:

[106] R.S.C. (1991) c. 46.

> "Another area to consider is whether the transfer of the fund [into a pooled fund] could be considered a "deposit" for investment purposes (i.e., where the [community] foundation is acting like a bank) under provincial law (such as the Ontario Trust and Loans Companies Act) [sic].[107]

- Does the issuance of an acknowledgment that the participating charity can recover its investment funds from a recipient umbrella charity constitute the issuance of a "security" that may require registration under the *Securities Act* if the exemption for charities under Section 35 subsection (2) paragraph 7 is not complied with?

- Since there is no common law right to co-mingle trust funds of different charities, and since the new regulation under the *CAA* does not extend to permitting the co-mingling of charitable funds of different charities, the recipient charity of such funds might be required to obtain court authorization before it can pool funds received from other charities.

In consideration of the numerous legal issues that should be addressed, a charity contemplating establishing and managing a managed or pooled fund should first retain legal counsel to provide a considered legal opinion concerning whether the specific circumstances of that charity and the details of the proposed managed or pooled fund with regard to applicable legislation would permit the charity to proceed with the program. A note of caution in this regard was suggested in the materials prepared by Francis K. Boyle for the Community Foundations of Canada in December 1998, in which she stated that:

> An overriding consideration, of course, is whether the community foundation and its goals are being sufficiently enhanced by taking on managed funds to justify the inconveniences. In many cases, there will be no such benefit[108]

L. Charity Acting as Trustee of Property for a Fee

On occasion, charities may agree to act as a trustee of property for a donor in return for an administrative fee. The trust document may be in the form of either a revocable or irrevocable trust,

[107] *Supra*, note 79 at 21.
[108] *Ibid.*

with the charity often being designated as the residual beneficiary in the event of the death of the donor/beneficiary.

The benefit to the charity in acting as the trustee would the management fee earned in caring for the trust property, as well as an expectation that either at the outset or at sometime in the future, the donor may be inclined to designate the charity as the beneficiary of the property on the death of the donor.

There are a number of problems, though, associated with this form of fundraising, the more important of which are summarized below:

- The charity may not have the corporate power to act as a trustee for a third party, instead of acting only as a trustee for its own charitable purposes.

- Acting as a trustee for third parties who are not "qualified donees" would not only not be an acceptable charitable activity, but it would unlikely be either a related business activity or a "deemed related business" activity under subsection 149.1(1)(J) of the *ITA*.

- Acting as a trustee for a third party, particularly when a charity receives a fee for doing so, albeit small, and offers to provide such service to the public, may require that the charity become registered as a trust corporation under the *Loan and Trust Corporations Act* similar to the situation where a charity undertakes to manage a pooled investment fund on behalf of other charities that are not necessarily members of the umbrella organization.

- In addition, if the trust agreement provides for disposition on death, such disposition clause would face the same requirements as a debt instrument that is forgivable on death, i.e., requiring that it be structured as a testamentary instrument and possibly having to comply with the provisions of the *Insurance Act* of Ontario.

- Finally, the charity and its board of directors run the risk of being exposed to liability for environmental contamination if the real property being held in trust is found to be contaminated.

M. Legal Issues Involving Fundraising on the Internet

The Internet can provide charities with a powerful tool to use in fundraising. It provides instant international reach on a medium whose global popularity continues to rapidly increase. Online philanthropy in the United States is now estimated at .6 percent of all charitable giving, a small amount percentage-wise, but representing $1 billion in online donations.[109] Online giving has grown rapidly, and the trend appears to be solidifying as part of larger fundraising campaign tool set. Charity.ca, a web portal that facilitates online giving to a number of charitable organizations, reported that in 2002, the average online gift was $125, significantly higher than donations made via direct mail.[110] However, the Internet is still in many respects uncharted water when it comes to the law, and charities must stay aware of the burgeoning legal issues that they face in order to use the Internet effectively. The following is intended as a brief discussion of some of these issues and should be used only as a broad framework to start considering the issues involved with fundraising on the Internet:

(1) Territorial Jurisdiction

The Internet is international in scope. However, some countries attempt to impose jurisdiction over its use. For example, nations will impose tax, privacy, censorship and even criminal laws upon Internet usage. The manner in which a charity uses its website can potentially expose it to the laws of any jurisdiction in the world. A charity must therefore be aware of the laws of all nations in which it is actively soliciting funds, as opposed to places where its website is only passively available to be viewed.

Generally speaking, where a "substantial connection" can be established between a web site and a jurisdictional locale, that locale will claim some sort of legal jurisdiction over the site. "Substantial connection" is generally established where a site solicits commercial activity from those in the jurisdiction in which the site is being viewed. The use of active "push and

[109] Joyce R. O' Brien, "How to make the most out of technology in fundraising", *Advancing Philanthropy*, July/August 2003, at p. 13.
[110] Edward Trapunski, "Philanthropy and the Internet", *Front & Centre*, March 2003, Vol. 10, No. 2, at p. 1.

pull" mechanisms of doing "business" with web site users is distinguished from sites that are non-commercial and only exist passively with no interactive commercial potential with viewers.

The difficulty for charities is differentiating on the web site regarding those jurisdictions in which the charity wishes its site to exist as an active fundraising mechanism, and those in which it merely wishes to appear as a passive site. Some as of yet unproven suggestions in this regard might be to limit access to certain users in various jurisdiction to part or all of the charity's site; or, to post disclaimers on the site stating that the charity only intends to raise money through its site in certain jurisdictions and, in fact, will only accept funds from those jurisdictions, and will not accept funds from any jurisdictions foreign to those listed. A charity should also ensure that it is familiar with the applicable laws of all jurisdictions in which its web site appears, or at least of those jurisdictions in which it is actively soliciting funds. It should be noted that many countries have specific fundraising regulations of which the charity should be aware.

(2) Intellectual Property Law

Charities need to be aware that all trade mark and copyright laws are applicable to web sites and Internet usage. In fact, it is very easy to infringe copyright on the Internet by, for example, downloading without proper authorization information such as music, software, images, or video. If unauthorized downloading were to occur on a charity's computers, even if such were conducted by an employee, then the charity could potentially be exposed to liability for copyright infringement.

Charities should also be aware that the person whom the charity hires to design its website, unless an employee of the charity, will own the copyright in that site. A charity should therefore ensure that it obtains an assignment of the copyright and a waiver of the designer's moral rights prior to contracting with the designer. Alternatively, if the charity is purchasing the website from another organization that has been using it, it should ensure that the organization from which it is purchasing the site itself owns the copyright, and is willing to assign such to the charity.

Confusion can arise from multiple domain names that are similar in nature but which are not being used by the same organization. A charity should consider purchasing all domain names that are similar to that of its main web site to guard against both confusion and against someone creating an unsavoury or directly defamatory site with a name similar to that of the charity's. Briefly, a charity also needs to consider other trade mark issues involving:

(a) Posting others' trade marks on its site;
(b) hyper-linking;
(c) meta-tags;
(d) dilution (of cause of action); and
(e) passing off.

(3) Civil Actions and the Internet

Charities need to be aware of the many different areas where potential civil liability can arise through involvement with the Internet, which can include the following:

- Defamation (libel and slander): It is very easy for defamation to appear on the Internet. Bulletin boards and chat-rooms easily facilitate the posting of defamatory material by Internet users. A charity should ensure that its web site is monitored frequently for posted messages by users that could be defamatory in nature. E-mails should also not be considered as private or privileged communication, and therefore need to be scrutinized closely.

- Interference with economic interests: Civil liability can arise where a web site is used to criticize the business practises, wares or services of others, and such criticism promotes or leads to contracts with those others being breached.

- Passing off.

- Breach of trade secrets: Breach of trade secrets can easily occur through inappropriate use of e-mail or improper security measures.

- Misrepresentation of personality: Misrepresentation of personality can occur through the use of a person's image or personality without authorization.

- Negligence: Negligence can arise where misleading statements are posted on a web site which are relied upon by others to their detriment where it should have been expected that such reliance would potentially occur. This situation could easily happen where information on a web site were not properly updated on a regular basis.

- Privacy: The online philanthropy trend discussed often uses software which will enable a donor to donate funds directly online. Privacy legislation creates an onus on a charity to keep this information confidential and protected.

(4) Domain Names, Trade Marks and the Internet

A matter involving fundraising on the Internet that should be emphasized to a charity is the importance of ensuring that the charity has an Internet domain name (URL) that is as close as possible to the corporate or primary operating name of the charity and protecting the domain name as a registered trade mark. This would help to ensure that if a potential donor is looking for the charity on the Internet, either for informational purposes or to make a donation, the donor will not be directed to the website of another charity where the other charity has a similar or confusing domain name to the corporate or operating name of the charity that the donor is wanting to contact. More information in this regard can be found in the summary entitled *"Checklist and Reference Guide: Avoiding Wasting Assets II – Trade-mark and Domain Name Protection for Charities"* attached as Appendix 7 to this paper.

(5) Marketing and Advertising on the Internet

Charities should be aware that all existing laws regarding marketing and advertising also apply to such practises on the Internet. There are numerous laws aimed at protecting consumers from false or misleading advertising and inappropriate business practises. In addition to fundraising legislation discussed later in this paper, charities should be aware of a number of general acts that apply, including the *Trade Mark Act*; the *Business Practises Act* (Ontario); and the *Competition Act,* Section 52(1) of the latter states that:

> No person shall, for the purpose of promoting, directly or indirectly, the supply or use of a product or for the purpose of promoting, directly or indirectly, any business interest, by any means whatever, knowingly or recklessly make a representation to the public that is false or misleading in a material respect.

(a) Contests and Sweepstakes:

These types of promotions are governed by the *Criminal Code* as well as the *Competition Act.* Under both Canadian and U.S. law, unless a contest requires some skill for the selection of winners, there must be no consideration (or price) paid to enter (*Criminal Code s.206(1)).*

(b) E-Mail Marketing and Spamming

Before considering using bulk e-mail marketing, a charity should be aware that such methods have led to litigation in the United States and remain a controversial issue in Canada. In general, it is considered a breach of "netiquette" to send "bulk" e-mails. Such email marketing may constitute a violation of the *Criminal Code* provisions regarding tampering with computer equipment and software and mischief against data and computer systems. In addition, charities must consider the new Bill C-6 *Personal Information Protection and Electronic Documents Act.* This new privacy legislation provides rules governing the usage of individuals' personal information gathered through the Internet. Bill C-6 is discussed in greater detail later in this paper. In an article entitled "Should we use e-mail for fundraising?"[111], Marilyn Gross agrees with the possibility of using e-mail as <u>one</u> tool in a fundraising kit, but there are many other issues to be considered before embarking on an e-fundraising campaign. Gross encourages fundraisers to possible drawbacks of e-mail

[111] Marilyn Gross, "Should we use e-mail for fundraising?", *Front & Centre* (Toronto: Canadian Centre for Philanthropy, May 2002), at p. 18.

solicitation, including the perceived invasion of a potential donor's privacy, and also the perceived illegality of asking for money via the Internet, whether or not this is true. Public perception of a charity's fundraising practices can either bolster or damage its overall reputation. As such, Gross encourages fundraisers to develop an open, information relationship with potential donors before asking for funds via e-mail, including the respect of donor privacy.[112]

(c) Quebec Language Laws

Charities that wish to advertise and fundraise in Quebec must be aware of that province's language laws which specify that all specific advertising in Quebec must be in French.

(6) Rules of Thumb

A charity wishing to use the Internet for fundraising purposes must consider a myriad of issues and laws and should obtain legal advice before doing so. The following are a few "rules of thumb" that a charity may consider when thinking about fundraising on the Internet:

- Never use the work, good will, or intellectual property of another organization or individual on the site without first obtaining formal authorization from that organization

- Maintain control over the site and closely monitor the site to ensure that any content that appears on or is posted to it is not defamatory or does not infringe any intellectual property laws. This would apply to information on any linked sites.

- Consider limiting access to the site to a controlled number of trusted employees.

- Maintain confidentiality over information obtained and used on web site.

[112] *Ibid* at 18.

- Operate the web site with an eye for the effect that it will have on a global scale, not just in Canada and the U.S.

N. Legal Issues in Sponsorship Arrangements

One of the most significant areas of growth for fundraising is the utilization of the names, trade-marks and goodwill of a charity in various sponsorship arrangements. A summary of the legal issues is set out in the article attached at Appendix 7 to this paper. Some charities in the United States have entered into extensive sponsorship arrangements with businesses, including the endorsement of products. For instance, Ducks Unlimited in the United States has licensed its trade-marks in conjunction with "Ducks Unlimited Home Furnishings" and "Ducks Unlimited Official Clothing."[113] In addition, the American Cancer Society two years ago entered into an exclusive licensing arrangement of its logo with NicoDerm, a smoking cessation patch, although the exclusive rights to use the name of the American Cancer Society was subsequently dropped from the business arrangement.[114] Another example is a program that was undertaken by Save the Children in the United States to license its name and trade-marks in conjunction with "the Save the Children Pet Furnishings Collection."[115]

In Canada, there are a numerous charities which are actively involved in sponsorship arrangements, such as the Canadian Olympic Association. Another example is, Save the Children Fund of Canada which started to license its name and logo in November 1998 to manufacturers which sell through traditional retail outlets. Participating manufacturers will now have access to Save the Children's names, trade-marks and reputation in return for the charity receiving licensing fees, ranging anywhere from five to ten percent of the sale price, depending upon the nature of the product being sold.[116]

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[113] Susan Gray and Holly Hall, "Cashing in on Charity's Good Name" *Chronicle of Philanthropy* (July 30, 1998) 25 at 29.
[114] *Ibid,* at 29.
[115] *Ibid.*
[116] "Save the Children Turns to its Good Name to Generate Extra Income" (1998) 8:20 *Canadian Fundraiser* at 2.

Although it is beyond the scope of this paper to provide a thorough discussion of the legal issues involved in sponsorship arrangements by charities, the following is given as a brief outline of some of the more important legal issues that should be considered by charities and their legal counsel before embarking on a sponsorship program.

(1) Distinguishing Between Receiptable Donations and Non-Receiptable Sponsorship Payments

CRA in its publication entitled "*Tax Advantages of Donating to Charity"* issued on October 3rd, 1999 and available from CRA's website at www.ccra-adrc.gc.ca, states at page 16 that:

> When a business gives cash or other property to a charity, it may not necessarily be making a gift to the charity. For example, a business may make a payment, or give merchandise to a charity and receive a business advantage in return, such as promotional or advertising services. In this situation, the business has not made a gift to the charity and the charity cannot issue an official tax receipt. The business can usually claim the payment or the value of the merchandise as a business expense.

Although the receipt of a business sponsorship payment by a charity will require the charity to collect and remit G.S.T., the business will be able to claim an input tax credit for such payment. More importantly, the charity will not need to include the sponsorship payment in its disbursement quota for the following year, since no charitable receipt will have been issued for the said payment.

If the business transfers property or money to a charity but does not receive any meaningful consideration in return, then the transfer would likely be a gift for which a receipt could be issued, although it would still be preferable from the standpoint of the charity that a receipt not be issued that would result in an increase in its disbursement quota.

Whether or not a business has received a benefit from the payment made to the charity will depend upon the facts of each situation. For instance, a simple acknowledgment in a newsletter of a charity at the end of the year that a business has given a gift would not likely constitute sufficient consideration by the business that would preclude a charitable receipt being issued. On the other hand, if a business receives advertising space in a charity's magazine or newsletter that was intended to promote the goodwill of the business for its products or service, then such arrangement would, in the opinion of CRA, not be considered to be a gift for which a receipt could be issued. The same result would also occur with more obvious sponsorship arrangements, such as licensing fees where the name or trade-marks of a charity are used to promote the goodwill products or seminars of a business.

(2) The Importance of Documenting Sponsorship Arrangements

Charities are often lax in entering into appropriate sponsorship agreements that adequately protect their interest. A charity and its board of directors need to understand that it is essential that a carefully crafted sponsorship agreement be utilized to protect the name and goodwill of the charity, which is often the most important asset of a charity.

The sponsorship agreement should address matters such as controlling the use of the charity's name, establishing time parameters for the sponsorship arrangement, providing for appropriate releases and indemnities, as well as determining the calculation of fees to be paid to the charity. Failure by the directors of the charity to ensure that the name and goodwill of a charity is properly protected and that fair market value consideration is being received could leave the directors personally exposed to liability for not having adequately preserved and managed the charitable property that has been entrusted to them.

(3) Protecting and Licensing Trade-Marks in Sponsorship Arrangements

Fundamental to entering into a sponsorship agreement is the identification, protection and licensing of the trade-marks of the charity. To obtain an overview of some of the more important issues involving trade-marks for charities, reference can be made to the summary outline attached to this paper at Appendix 7, as well as to a longer article by the author on the same subject found at www.charitylaw.ca.[117]

As is evident from reviewing the attached summary, a charity that is considering entering into a sponsorship arrangement should take the following steps to protect its trade-marks:

- The charity should identify what are its trade-marks, including possibly its corporate name, business names, logos, and even slogans.
- The charity should highlight those trade-marks that are in everyday use by utilizing the *"™"* marking for an unregistered trade-mark and the *"®"* marking once the trade-mark is registered.
- The charity should take steps to apply for registered trade-marks for all of its trade-marks under the *Trade-Marks Act*[118]
- A charity should obtain domain names on the Internet utilizing its trade-marks and variations of its trade-marks that otherwise might be either intentionally or unintentionally misappropriated by other charities or businesses.
- The charity should ensure that no sponsor is able to utilize the trade-marks of the charity without first entering into a trade-mark license agreement in accordance with requirements of Section 50 of the *Trade-Marks Act*.
- The charity should ensure that it diligently monitors the way in which it uses its trade-marks, as well as how the trade-marks are used by businesses and other third parties as licensees of the trade-marks, failing which the trade-marks could become "wasting assets" through misuse or lack of attention.
- Finally, the charity should be vigilant in ensuring that unlicensed third parties are not able to misuse or misappropriate any of the trade-marks of the charity through failure of the charity to adequately protect its trade-marks, including commencing legal action if necessary.

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117 Terrance S. Carter, "Avoiding Wasting Assets II: Intellectual Property Protection for Charities", "*What's New and What's Coming",* Second National Symposium on Charity Law, Canadian Bar Association, Toronto, April 14, 2004. (Also found at www.charitylaw.ca)

118 R.S.C. (1999) c. T-13.

(4) Liability Exposure from Sponsorship Arrangements

Some examples of liability exposure that a charity and possibly its directors may face arising out of a sponsorship arrangement are outlined below as follows:

- The Public Guardian and Trustee of Ontario, in "*Charities Bulletin No. 4*",[119] indicated that the Public Guardian and Trustee of Ontario will investigate complaints about the misuse of charitable property, and that such property would include *"money, real estate, food, clothing, trade-marks or goodwill"* [Emphasis added]. An investigation into the misuse of the trade-mark of a charity in a sponsorship arrangement could result in a demand for a formal passing of accounts under Section 3 of the *CAA*.

- A charity could also face liability exposure if the sponsorship arrangement constituted a form of business partnership or joint venture. The charity and its legal counsel would need to carefully scrutinize the facts surrounding any sponsorship arrangement to determine the real nature of the relationship and the extent of liability exposure to the charity so that either the sponsorship program was modified to reduce the exposure to liability or alternatively, appropriate releases and indemnities are obtained from the business sponsor.

- Where a charity is involved in either directly or indirectly endorsing the products or services of a business sponsor, the charity, and potentially its board of directors, could become exposed to liability in the event that a purchaser of the endorsed products or services become injured or otherwise suffered damages. The purchaser might allege that the charity is liable either because of negligent misrepresentation by the charity or because of detrimental reliance placed by the purchaser upon the endorsement of the charity.

- A charity will want to consider, and ultimately, participate in, a sponsorship arrangement that generate funds and promote the charity's goodwill reputation. Some keys in this regard are outlined in the article "Sponsorship, Partnership, Strategic Investment" including:

  - asking the key question, which is, "How do we use our organization and the power of our brand equity to advance a business and how, in return, does the business help us do the work that we're here to do?"
  - listening;

[119] "Complaining About Charities" *Charities Bulletin No. 4: Information from the Public Guardian and Trustee's Charitable Property Program* (Toronto: Office of the Public Guardian and Trustee of Ontario, July 1999) at 1.

- understanding the business prospect;
- avoiding forcing a bad fit;
- thinking beyond cash;
- negotiating;
- never sell the organization short; and
- never compromise the organization's own brand to promote another. [120]

(5) Reducing Liability from Sponsorship Arrangements

In consideration of the potential exposure to liability from sponsorship arrangements, charities should become diligent in reducing legal risks as much as possible. In this regard, the May 27th, 1999 issue of *Canadian Fundraiser* included a summary of a Preliminary Report issued by the Attorney Generals of sixteen American states and the District of Columbia in April1999 entitled "*What's in a Non-Profits Name? Public Trust, Profit and the Potential for Public Deception*".[121]

The report identified the potential for false and misleading messages to the public where the name of a charity is utilized by a business. The report developed a set of key principals for public protection in this area, which have been summarized below as follows:

- Both the commercial sponsor and the charity should satisfy all applicable legal standards, including compliance with consumer laws prohibiting false advertising, unfair and/or deceptive trade practices and consumer fraud.

- Advertisement for commercial products should not represent that the charity has endorsed the advertised product. If the name or the trade-marks of a charity are utilized by a business and the charity has not in fact endorsed the advertised product, then the advertising must clearly and conspicuously disclose that the charity has not endorsed or recommended the product in question.

- Advertisements for commercial products using the name or trade-marks of a charity must avoid making express or implied claims that the advertised product is superior to

[120] Norah McClintock, "Sponsorship, Partnership, Strategic Investment", *Front & Centre* (Toronto: Canadian Centre for Philanthropy, March 2002), Vol. 9, No. 2, at pp. 2-3.
[121] "What's in a Name, When it Belongs to a Non-Profit?"(1999) 9:10 *Canadian Fundraiser* at 6.

others in the same product category unless the claim is true and substantiated and the charity has determined that the advertised product is in fact superior to others in the same product category.

- Advertisement for commercial products and services using the name or trade-mark of a charity should disclose clearly and conspicuously that the corporate sponsor has paid for the use of the charity's name or trade-mark when that is the case.

- Product advertisement arising from a commercial/charity relationship should not mislead, deceive or confuse the public about the effect of the consumer's purchase of such products or services on charitable contributions by the commercial sponsor.

- Advertising sponsorships between commercial and charitable entities should avoid exclusive product or service sponsorships. However, in the case where an exclusive relationship does exist, product or service advertisement using the name or trade-marks of a charity should clearly and conspicuously disclose such fact.

These principles provide a practical guideline to follow for Canadian charities in avoiding some of the problems and liability exposure involved in sponsorship arrangements.

O. Legal Issues Involving Third Party Fundraisers

More charities than ever are entering into arrangements with third party fundraisers to assist with the fundraising programs of a charity, such as special fundraising projects, telemarketing campaigns, and large advertising campaigns, to name but a few. The legal issues involved in working with a third party fundraiser requires that a carefully worded contract be prepared and that the charity be aware of the various statutes that have a direct bearing in governing the actions of fundraisers in various jurisdictions. What follows is a brief outline of some of the more important issues that should be addressed in working with a professional fundraiser.

(1) CRA Policy on Third Party Fundraisers

CRA has published a position with regard to the way in which charities can fundraise in order to support its charitable activities, methods of which often include the assistance of a third party fundraiser. A charity can use a third party organization or fundraiser as an agent to organize a fundraising event, but the charity must retain control over all monies earned and all receipts issued in relation to the event. CRA's *Policy Commentary* entitled, "Third Party Fundraisers",[122] set outs the parameters under which registered charities can use fundraising events as a means of furthering their charitable purposes. Key to charitable fundraising is the issue of control, in that charities may use agents for their fundraising efforts, but must ultimately direct all fundraising activities. If control is not maintained, a charity puts itself at risk of losing it charitable registration.

Where a charity is not directly involved in the management of a fundraising event, CRA advises the charity to do the following:

- create a written agreement stipulating all facets of the fundraising arrangement;
- ensure that official donation receipts are only issued to donors for the eligible amount of the donation as defined above;
- ensure that an authorized official duly signs all receipts in accordance with the *Income Tax Regulations* 3501(1)(i), 3501(2), 3501(3);
- be prepared to show CRA a full accounting of all donated fundraising monies and issued receipts; and
- be able to report the amount of advantage received by the fundraising event's participants to CRA.

Gift planners and charities can try to avoid valuation penalties by ensuring that, "particularly where the property is unusual and difficult to value, that independent reputable valuations are obtained and can be supported" [123]. In addition, "it is particularly important for charities to be careful when obtaining valuations not to be persuaded by the donor to simply accept the donor's valuation.

[122] "Third Party Fundraisers" *Policy Commentary,* dated February 26, 2003, *available at* http://www.ccra-adrc.gc.ca/tax/charities/policy/cpc/cpc-026-e.html.

[123] Susan Manwaring. "Third Party Civil Penalties: What Every Gift Planner Should Know". *Gift Planning in Canada* (Edmonds, WA: G. Roger Schoenhals, 2004), Vol. 9, No.2 at p.1.

(2) Considerations When Contracting with a Third Party Fundraiser

The following are some of the terms that should be included in a contract with a third party fundraiser.[124]

- The fundraiser, its employees and agents should be prohibited from misleading the public by stating or implying, either in writing, or verbally, that there are charity employees. The court in *The Aids Society for Children (Ontario)*[125] held that all fundraising contractors and subcontractors are agents of the charity. As the principal, the charity is liable for misrepresentation and/or misleading information committed by the contractors or subcontractors as its agents in the course of the fundraising.

- The charity's name and trade-marks must only be used within the specific parameters identified in the contract and only as approved in writing by the charity.

- The charity must retain full ownership and control of its donor lists.

- The charity must maintain full control of the receipts and deposits of charitable contributions received from the fundraising program.

- The charity must maintain full control over the content and method of fundraising initiatives presented to the public.

- The charity must retain the right to inspect the premises of the fundraiser and be able to verify the methods of solicitation and calculations being employed by the fundraisers, as well as being able to examine all documents and financial records of the fundraiser relating to the fundraising programs in question.

- The fundraiser must work in compliance with a strict written code of ethics for fundraising, such as that recommended by the Canadian Centre for Philanthropy, the Canadian Association of Gift Planners or the Association of Fundraising Professionals. The AFP's *Code of Ethical Principles and Standards of Professional Practice*, for example, provides guidelines for when to help a donor, and how far to go when a donor asks for assistance, a situation which is not uncommon in the sphere of fundraising.

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[124] Some of the considerations enumerated above can be found in a helpful list of recommendations of inclusions in a fundraising contract recommended by the Public Guardian and Trustee of Ontario in the *Not-for-Profit Incorporators Handbook*, *supra* note 21 at 64.

[125] *Supra,* footnote 14

- The fundraiser must comply with the new deceptive telemarketing and false or misleading representation provisions in the *Competitions Act* as discussed latter in this paper.

- The cost, expenses and profits of the fundraiser must be kept within the 20% limit allowed by Canada Customs and Revenue for administrative and non charitable activities. *The Aids Society for Children (Ontario)* reemphasized this principle.

- The fundraiser must disclose to donors what proportion of the monies being donated will be retained by, or paid to, the professional fundraiser for the expenses, administrative costs, profit of the fundraiser, and the estimated amount of money which will finally follow to the charity.

- The charity has a fiduciary obligation to account for all funds collected fully to the public. It cannot derogate this obligation to its agents, namely third party fundraisers or their subcontractors.

- As an agent of the charity, a third party fundraiser has a duty to account to the charity for all monies that it receives from fundraising programs.

- The charity must be entitled to terminate the contract if the fundraiser employs false or misleading solicitation practices as determined in the sole opinion of the charity.

- A fundraising agreement with a third party fundraiser is void or voidable if the compensations paid to the third party fundraisers are disproportionate to the total amount of funds raised.

P. Fundraising and Related Legislation[126]

Although there is presently no specific fundraising legislation in Ontario (except for the complaint and investigation procedure under Section 6 of the *CAA*), there are a number of statutes in other provinces and at the federal level that impact upon fundraising activities that are carried both within and outside Ontario.A few provinces have legislation governing charitable fund-raising activities,

[126] Excerpts of this section have been previously published in "Extra-Provincial Corporate and Fundraising Compliance for Charities", by Jacqueline M. Connor and Esther S. J. Oh, assisted by U. Shen Goh, presented at the 2nd National Symposium on Charity Law, "*What's New and What's Coming*", hosted by the Ontario Bar Association, Canadian Bar Association, and Canadian Association of Gift Planners, Toronto, Ontario, April 14, 2004.

which require registration by extra-provincial entities with a charitable purpose. A charitable purpose includes any philanthropic, benevolent, educational, health, humane, recreational, religious, cultural or artistic purpose. The various provincial charitable fund-raising statutes vary in their content and application and each should be carefully reviewed for any potential implications for a particular charity's activities. A brief summary of those statutes is set out below.

(1) Ontario

In Ontario, charities and others receiving or holding property for charitable purposes must report such information to the Office of the Public Guardian and Trustee of Ontario ("PGT") pursuant to the *Charities Accounting Act*. As there is no prescribed form required, this notice can be provided by writing a letter to the Ministry of the Attorney General, Office of the Public Guardian and Trustee. The letter should be accompanied by a copy of the Letters Patent governing the charity; street and mailing addresses of the charity; names and street and mailing addresses of its directors and officers; all legal and popular or common names or acronyms by which the charity is known or identified; and registration and business identification numbers assigned by CRA for charitable donation tax-credit purposes. There is no fee for an Ontario charitable fund-raising registration.

(2) Alberta

Charities using a fund-raising business, intending to raise more than $25,000 in gross contributions in its financial year from solicitations to individuals in Alberta, or raising more than $25,000 during or after a campaign, must register under the Alberta *Charitable Fund-raising Act*. Alberta has the most comprehensive legislation governing charities in Canada.

Registration can be effected by filing an Application for Charitable Organizations with an authorized service provider. In the specific case where a charity raises more than $25,000 during or after a campaign, the charitable fund-raising registration is required within 45 days after the contributions reach $25,000 in Alberta. The fee for an Alberta charitable fund-raising registration also depends on with which authorized service provider the corporation chooses to file. The fee charged by authorized service providers is usually around $81.40 (including G.S.T.). Of this fee, $60.00 is the government fee. The Alberta charitable fund-raising registration is valid for 1 year.

(3) Saskatchewan

There is currently no Saskatchewan legislation requiring charitable fund-raising registration. However, there is legislation governing charitable fund-raising activities. The Province of Saskatchewan recently passed the Saskatchewan *Charitable Fund-raising Businesses Act,* effective January 1, 2003. The legislation imposes additional restrictions on the activities of charities, especially in respect of the hours during which telephone or door-to-door solicitations may be conducted, contracts with fundraising companies, disclosure requirements owed to donors and the general public and a strict requirement to refrain from making solicitations when requested by an individual to do so. The Act will also require fund-raising businesses that work for profit to obtain a license and otherwise comply with the provisions of the Act.

(4) Manitoba

In Manitoba, charities canvassing for, soliciting, or collecting money, goods, or financial assistance of any kind must register pursuant to the Manitoba *Charities Endorsement Act*. Registration entails the completion of an Application for Authorization to Solicit Funds with Consumer and Corporate Affairs, Consumers' Bureau. There is no fee for a Manitoba charitable fund-raising registration.

(5) Quebec

Charities, whether or not incorporated, that receive donations or income in Quebec must register pursuant to the Quebec *Taxation Act.* This can be done by filing the following documents with the Government of Quebec, Minister of Revenue: Application for Registration as a Canadian Charitable Organization; Certified copy of the incorporating document; Statement of Activities; Copy of Statement of Assets and Liabilities; List of names, addresses and position or title for all directors and officers; and Copy of the Canada Customs Revenue Agency registration. There is no fee for a Quebec charitable fund-raising registration.

(6) Prince Edward Island

Prince Edward Island requires that charities that directly or indirectly solicit or make any appeal to the public for donations must register pursuant to the *Charities Act* (Prince Edward Island). However, the *Charities Act* does not apply to an organization or foundation that is a registered charity under the *ITA*.

(7) Other Provinces

There is currently no legislation governing charitable fund-raising activities and requiring registration by extra-provincial entities in British Columbia, New Brunswick, Nova Scotia, Newfoundland, the Yukon Territory, the Northwest Territories, and Nunavut.

(8) *Federal Competition Act*: Deceptive Telemarketing & False or Misleading Representation

On March 11th, 1999, the 1999 Amendments to the *Competition Act*, *An Act to Amend the Competition Act* received Royal Assent. On March 18th, 1999, the provisions relating to deceptive telemarketing and false or misleading representation were proclaimed in force. These provisions have important application to charities in relation to telemarketing and Internet fundraising, as well as door to door and other forms of fundraising solicitation. In particular, the amendments to the *Competitions Act* contained in the 1999 Amendments to the *Competition Act* creates a serious source of liability for both fund-raisers as well as charities, their boards of directors, and their officers if the fundraising activities of the charity violate the new provisions of the *Competitions Act*.

The amendments contained in the 1999 Amendments to the *Competition Act* that have direct impact upon fundraising practices are summarized below as follows:

- The definition of "business" under Section 2(1) of the *Competition Act* now specifically includes "*the raising of funds for charitable or other non-profit purposes"*.

- The Competition Bureau Publication entitled "Misleading Advertising Guidelines," published in 2001,[127] clarifies that, notwithstanding the above, the provisions of the *Competition Act* do not apply to representations that are solely charitable in purpose, as indicated below:

  > In general, these provisions apply to anyone promoting, directly or indirectly, the supply or use of a product or service, or any business interest, by any means. This does not include advertisements or representations made solely for a political or charitable purpose; [emphasis added]

- However, if part of the purpose of the fundraising is promoting a product or service, or there is evidence of a non-charitable purpose such as a personal benefit, the fundraising could be subject to the provisions of the *Competition Act*.

- The inclusion of more restrictive telemarketing provisions were made in response to the public perception that there is a growing problem of deceptive telephone sales and contracts that target vulnerable groups in society, like the elderly. As a result, the definition of telemarketing has been expanded under Section 52.1(1) of the *Competition Act* to now mean:

  > "...the practice of using interactive telephone communications for the purpose of promoting, directly or indirectly, the supply or use of a product or for the purpose of promoting directly or indirectly, any business interest [Emphasis added]

- Guidelines issued by the Competition Bureau of Industry Canada regarding the 1999 Amendments to the *Competition Act* have defined "*interactive telephone communications*" as follows:

  > "Interactive telephone communications will be interpreted as live voice communications between two or more persons. The Director will not consider "interactive telephone communications" to have occurred with regard to:

[127] *Available* on the Competition Bureau website at http://strategis.ic.gc.ca/epic/internet/incb-bc.nsf/en/ct01299e.html.

- fax communications,
- Internet communications, or
- a customers interaction with automated prerecorded messages."[128]

The exclusion of Internet communications from the telemarketing provisions is an important and welcome concession, since more and more fundraising is being conducted on the Internet. However, the telemarketing provision will apply to telephone follow up calls resulting from initial contact via the Internet.

- Section 52.1(2) prohibits anyone from being involved in telemarketing unless there has been disclosure;

> ...in a fair and reasonable manner at the beginning of each telephone communication, of the identity of the person on behalf of whom the communication is made, the nature of the product or business interest being promoted and the purposes of that communication... [as well as] disclosure in a fair, reasonable and timely manner of the price of any product whose supply or use is being promoted and any material restrictions, terms or conditions applicable to its delivery...

- A violation of the telemarketing provisions in the *Competitions Act* constitutes a criminal offence with punishment that may include fines at the discretion of the court, and/or imprisonment for up to five years.

- Section 52.1(6) provides for a due diligence defense for corporations or individuals with respect to alleged violations of the telemarketing provisions where the person is able to establish that there was appropriate due diligence taken to prevent the commission of an offence. However, under Section 52.1(7), a corporation may be convicted of the offence if it is shown that an employee or agent committed the offence, whether or not the employee or agent had been identified, unless due diligence has been established.[129]
- Of more concern, though, is the potential for personal liability of directors and officers in relation to telemarketing. In this regard, Section 52.1(8) of the 1999 Amendments to the *Competition Act* states that:

> Where a corporation commits an offence... any officer or director of the corporation who is in a position to direct or influence the policies of the

[128] Guidelines by Industry Canada, Competition Bureau, *available at* http://strategis.ic.gc.ca/epic/internet/incb-bc.nsf/en/ct01180e.html.

[129] H. James Blake, "New Developments in Corporate law" *Operation Update* (Continuing Legal Education of the Canadian Bar Association, Toronto, 1999) at 9. See also James B. Mausgrove, "*Sorry Wrong Number: The New Criminal Telemarketing Provisions of the Competitions Act"* (Business Law Section of the Canadian Bar Association, Toronto, May 26th, 1999).

> corporation in respect of conduct prohibited by the Section is a party to and guilty of the offence and is liable to punishment... whether or not the corporation has been prosecuted or convicted, unless the officer or director establishes that the officer or director exercised due diligence to prevent the commission of the offence. [Emphasis added]

The possibility that directors and officers of a charity may become personally liable for criminal prosecution from deceptive telemarketing will necessitate that the board of a charity, as well its officers and senior management, become actively involved in reviewing and approving procedures involved in telemarketing and thereafter to regularly ensure that those procedures are being carefully followed.

- The 1999 Amendments to the *Competition Act*, amending the *Competition Act* also amends the description of what constitutes "false or misleading representation involving a "business interest." The new provision will now have a direct impact on charitable fundraising because of the expanded definition of "business interest". In this regard, Section 52.(1) of the *Competitions Act* now provides for the following offence:

> 52.(1) No person shall, for the purpose of promoting, directly or indirectly, the supply or use of a product or for the purpose of promoting, directly or indirectly, any business interest, by any means whatever, knowingly or recklessly make a representation to the public that is false or misleading in a material respect. [Emphasis added]

- 52.(2) states that a representation referred to in Section 52.(1) is deemed to have been made to the public where it is:

> (a) expressed in an article offered or displayed for sale or on its wrap or containers,
> (b) expressed in anything attached to, inserted in or accompanied an article offered or displayed for sale, its wrapper or container, or anything on which the article is mounted for display or sale,
> (c) expressed on an in-store or other point-of purchase display,
> (d) made in a course of in-store, door-to-door or telephone selling to a person as ultimate user, or
> (e) contained in or on anything that is sold, sent, delivered, transmitted, or made available in any other manner to a member of the public.. [Emphasis added]

The false or misleading representation provisions therefore apply not only to telemarketing but also to door-to-door solicitation and with regard to any materials accompanying items that are offered for sale by the charity, such as a candy-donation box that are often placed by charities on the counters of retail stores.

- A disconcerting aspect of the new provisions dealing with false or misleading representation is that Section 52(1.1) states that to establish a false or misleading representation, it is *"not necessary to prove that any person was deceived or mislead"*. This means that if the solicitation complained of was made in a reckless manner that was false or misleading in a material respect, whether or not anyone was actually mislead or deceived, then the charity and the fundraisers would be guilty of an offence.

- Where there has been a violation of either the new deceptive telemarketing provisions or the false or misleading representation provisions, individuals can receive penalties up to $50,000.00 for a first offence and $100,000.00 for each subsequent offence. A charity itself can be subject to penalties of up to $100,000.00 for a first time offence and up to $200,000.00 for subsequent offences.

In light of the increased exposure to liability for both charities and individuals under the new provisions of the *Competition Act*, it is essential that preventative steps be implemented to reduce the exposure to liability as much as possible. In this regard, Section 74 (5) of the *Competition Act* states that if the offending organization can demonstrate a history of compliance with the *Competition Act* and it has formal fundraising policies in place and follows them, penalties may be reduced or waived altogether. As a result, it is essential for charities to adopt fundraising practices to guard against improper telemarketing and misrepresentation in fundraising, such as those contained in the recommendations made by the CCP.[130] A summary of those recommendations are set out below:

- Ensure that the fundraising materials (including scripts) accurately describe the charity, its activities, and the purposes for which those donations will be used.

- Consider providing written instructions to telephone solicitors, as well as door to door canvassers advising them that any misrepresentation could result in a severe penalty for them personally and for the charity that they are acting on behalf of.

- Ensure that the telephone fundraising scripts used by employees, volunteers and contract fundraisers disclose at the outset both the identity of the organization and the purpose for the call.

[130] Len Wolstenholne, "Charities now to be Covered by the Competitions Act" (1999) 9:7 *Canadian Fundraiser* at 1.

- Ensure that the contract with telephone solicitors includes a provision requiring adherence to the disclosure and misrepresentation provisions of the *Competitions Act*.

- Ensure that any promotional materials concerning lotteries, etc., includes the required disclosures, i.e., the number and value of the prizes, and any available information that materially effects that chances of "winning". Winners should be chosen either randomly or on the basis of their skill and then ensure that the prizes are distributed properly.

- Advise the governing board of the charity concerning the measures that have been taken and the procedures that are in place to ensure compliance with the new provisions of the *Competition Act*.

- Finally, have the board of a charity adopt a policy committing the organization, its directors, officers employees, and volunteers to, at all times, avoid making "false or misleading representations" on behalf of the charity. Then ensure that such policy is provided to everyone in the charity, including volunteers as well as employees.

In consideration of the heightened public anxiety that has resulted from numerous publicized telemarketing scams, it is probable that the Competitions Bureau will be under pressure to be very diligent in enforcing compliance with the new provisions under the *Competitions Act*. In this regard, it should be noted that the Competition Bureau is now able to apply for judicial authorization to intercept private communications without consent (i.e., a wire tap) to investigate more serious cases.[131]

The 1999 Amendments to the *Competition Act* amending the *Competition Act* constitutes a substantive change in the law with regard to fundraising across Canada and will need to be carefully studied by charities and their legal counsel given the substantive penalties that may result and the possibility of criminal charges being laid.

(9) Federal - Personal Information Protection and Electronic Documents Act

The *Personal Information Protection and Electronic Documents Act* ("*PIPEDA*") was passed on April 4th, 2000, and Part I came into effect on January 01, 2001. It is the first

[131] W. Laird Hunter, "Can I Take a Few Minutes of Your Time?" *Not-For-Profit News* (April, 1999) 26 at 27.

privacy legislation dealing with the private sector in Canada. The following is a brief introduction to the legislation, and an illustration of some of the ways that it will impact upon charities. In this regard, the *Personal Information Protection and Electronic Document Act,* “PIPEDA” became fully functional on January 1, 2004, when its provisions applied to every organization that collects, uses or discloses personal information, including personal health information, in the course of commercial activities. PIPEDA is the first comprehensive privacy legislation dealing with the private sector in Canada, and has as its purpose the protection of personal information gathered through electronic commerce. PIPEDA, will have a significant impact upon the ability of a charity to buy or sell donor lists, as well as carrying out any type of commercial activities. Charities should therefore determine whether their activities fall within the scope of the PIPEDA and, if so, that they are complying with the legislation. For a more detailed discussion of PIPEDA, an article entitled "Impact of the *Personal Information Protection And Electronic Documents Act* (PIPEDA) on Charitable And Non-Profit Organizations" by Mark J. Wong has been included as Appendix 5 to this paper.

(10) Provincial Business Name Registration Requirements

Most provinces and territories have business name legislation, such as the Ontario *Business Name Act,* which require a corporation, partnership or individual carrying on “business” in a name other than its legal name to register such business names in accordance with the terms of the applicable provincial legislation. There is normally no exception from registration requirements for a charity. As such, a charity that utilizes a shortened name from that of its full corporate name in its operation, such as “the ABC Fund” by the “ABC Fund Foundation of Canada Inc.,” will normally be required to register such operating name under the applicable business name legislation in each province that the charity operates in.

Failure to comply with applicable business name legislation may not only result in serious penalties, but it could preclude the charity from either commencing or defending legal action in the offending operating name of the charity.

(11) Extra Provincial Registration Requirements

As with business name legislation, each province or territory will normally have legislation requiring the registration by an extra provincial corporation that operates in a particular province or territories, such as the Ontario *Extra Provincial Corporation Act.*[132] The terms of the applicable legislation in each province or territory needs to be carefully reviewed to determine whether or not the fundraising activities of a charity are such that the charity would be considered to be "carrying on business" in that province or territory that would require the charity to register under the applicable extra provincial legislation.

In the Province of Quebec, there are additional restrictions that preclude residents in that province from utilizing a tax receipt issued by a charity for provincial income taxation purposes unless that charity has become a registered charity under Quebec provincial legislation. As such, registered charities that fundraise in the Province of Quebec will need to apply to the Quebec Ministry of Revenue to obtain charitable status in that province.

Q. Fundraising Liability and Anti-Terrorism[133]

(1) Overview of Legislation

Since the occurrence of September 11th, 2001, charitable fundraising and activities which until recently were thought to be commonplace and uneventful may now lead to a charity becoming susceptible to criminal charges for having facilitated "terrorist activities" or supported "terrorist groups" under new anti-terrorism legislation. This in turn could result in the charity possibly losing its charitable status and the corresponding exposure of its directors to personal liability. In addition, financial transactions, such as fundraising, involving charities may also lead to the possibility of allegations of terrorist financing or the

[132] R.S.O. (1990), c. E-27.

[133] Excerpts of this section were previously published in "Charities and Compliance with Anti-Terrorism Legislation: The Shadow Of The Law" presented by Terrance S. Carter at the ONTARIO JUSTICE EDUCATION NETWORK: SUMMER LAW INSTITUTE in Toronto, August 27 - 28, 2003, *available at* www.charitylaw.ca. .

surveillance and monitoring of a charity's financial activities. Lawyers handling transactions on behalf of charitable clients or on behalf of estates dealing with charities may also find themselves in situations involving a legal duty to report under new money laundering legislation in Canada.

The four main anti-terrorism initiatives include Bill C-36, *An Act to amend the Criminal Code, the Official Secrets Act, the Canada Evidence Act, the Proceeds of Crime (Money Laundering) Act and other Acts, and to Enact Measures Respecting the Registration of Charities, In Order to Combat Terrorism* [hereinafter "Bill C-36" or Anti-terrorism Act];[134] Bill C-35, *An Act to Amend the Foreign Missions and International Organizations Act* [hereinafter Foreign Missions Act];[135] the proposed Bill C-17, *An Act to amend certain Acts of Canada, and to Enact Measures for Implementing the Biological and Toxin Weapons Convention, In Order to Enhance Public Safety* [hereinafter "Bill C-17" or Public Safety Act][136], as well as the proposed Bill C-45, *An Act to amend the Criminal Code (Criminal Liability of Organizations)* [hereinafter "Bill C-45" or Criminal Liability of Organizations Act].[137] Although other statutes deal with issues related to terrorism, for the purposes of this paper, the above four pieces of legislation are collectively referred to as Canada's anti-terrorism legislation ("Anti-terrorism Legislation").

Bill C-36, i.e., the omnibus *Anti-terrorism Act* that was proclaimed in force on December 24, 2001, is an extremely complicated piece of legislation that involves co-ordinating the provisions of many federal Acts, including the *Criminal Code*, *Canadian Human Rights Act*, and the *Proceeds of Crime (Money Laundering) Act* [hereinafter *Proceeds of Crime Act*][138] (including regulations that were issued on May 9, 2002). Part 6 of the *Anti-terrorism Act*

[134] 1st sess., 37th Parl., 2002 (assented to 18 December 2001, S.C. 2001, c. 41; proclaimed in force 24 December 2001).
[135] 1st Sess., 37th Parl., 2001 (assented to 30 April 2002, S.C. 2002, c. 12; proclaimed in force).
[136] 2nd Sess., 37th Parl., 2002 (1st reading 31 October 2002;as amended by the Legislative committee on Bill C-17 on 7 May 2003).
[137] 2nd Sess., 37th Parl., 2003 (1st reading 12 June 2003).
[138] Now renamed the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act*, S.C. 2000, c. 17. This Act is discussed in greater detail in Part D of this paper.

also creates the new *Charities Registration (Security Information) Act*. The *Anti-terrorism Act* raises several concerns that innocent charities may be unwittingly caught within its provisions, which include the enactment of new criminal offences that are contingent on sweeping definitions of terms, such as “terrorist activities”, “terrorist group” and “facilitation of terrorist activities”; the establishment of a de-registration process for charities suspected of involvement in “terrorist activities”; and the development of broad new legislation to curtail “terrorist financing”.

(2) Specific Criminal Code Offences That May Impact Charities

The amendments to the *Criminal Code* implemented by the *Anti-terrorism Act*, and to a certain extent by the *Foreign Missions Act*, constitute the creation of a new type of criminal offence under the heading of terrorism. The assumption underlying these amendments to the *Criminal Code* is that certain offences, specifically terrorism offences, including the threat of or attempt to commit such offences, warrant an extraordinary approach in the methods of investigation, incarceration and punishment due to the very nature of those offences. The amendments implemented by the *Anti-terrorism Act* arguably amount to the creation of a “Super *Criminal Code*” within Canada’s existing *Criminal Code*.

Whether or not a particular charity will be subject to prosecution under the “Super *Criminal Code*” provisions provided for under the *Anti-terrorism Act* remains conjecture at this time. However, the immediate practical concern for charities is not that they will be prosecuted under the *Criminal Code* provisions. Rather, it is that a charity may be vulnerable to de-registration as a charity under the *Charities Registration (Security Information) Act* where a charity may have become unwittingly involved in activities or with groups that meet the definition of “terrorist activity” or “terrorist group” under the *Criminal Code*, even if no criminal charges are brought against the charity. At the same time, a charity may find to its surprise that it meets the broad and inclusive definition of “facilitating” a “terrorist activity” or “terrorist group” under the *Anti-Terrorist Act,* that could result in the seizure or freezing of its assets. Considering the stigma, suspicion, and loss of goodwill that such actions would have on a charity, the implications are both disturbing in theory and devastating in practice.

In recognition of the complexities of the Anti-terrorism Legislation, the co-ordination of several federal Acts and the lack of evidence to date concerning how the legislation may be implemented because of its relative novelty and the fact that much of the enforcement of these Acts is and will be conducted in secrecy, it is difficult to speculate concerning what sections of the Amended *Criminal Code* will in fact affect charities. The most that can be done is to draw a few examples from the applicable *Criminal Code* provisions as amended by the *Anti-terrorism Act* where charities might be caught under those provisions. In this regard, some of the relevant *Criminal Code* provisions that may impact charities include the following:

s. 83.02: Directly or indirectly providing or collecting property that is intended to be used or knowing that it will be used in whole or in part in a terrorist activity;

s. 83.03: Directly or indirectly providing or inviting the provision of property, financial or other related services that facilitate or carry out a terrorist activity or benefits a terrorist group;

s. 83.04: Directly or indirectly using or possessing property to facilitate a terrorist activity;

s. 83.08: Dealing with property owned or controlled by or on behalf of a terrorist group, facilitating, directly or indirectly, transactions or financial or related services for the benefit or at the direction of a terrorist group;

s. 83.18: Directly or indirectly participating or contributing to any actions that enhance the facilitation of a terrorist activity;

s. 83.21: Directly or indirectly instructing a person to carry out activities for the benefit of a terrorist group;

s. 83.22: Directly or indirectly instructing a person to carry out a terrorist activity; and,

s. 83.14: The Attorney General may apply for an order of forfeiture of property of a terrorist group if property had or will be used, in whole or in part, to facilitate or carry out a terrorist activity.

(3) The Need for Due Diligence

Unfortunately, due diligence is not a defence for violations of the new terrorism provisions of the *Criminal Code* as amended by the *Anti-terrorism Act* or against revocation of charitable status under these new laws. While due diligence is not a defence against the Anti-terrorism charges, the Anti-terrorism laws do not relieve directors of their fiduciary duties to the charity and its donors. As such, due diligence is still important to protect directors from allegations of failures to comply specifically with their common law duties with regards to the *Anti-terrorism Act.* If a charity's assets are frozen or seized, the directors and officers of a charity could be exposed to civil liability for breaching their fiduciary duty to protect the charitable assets of the charity. If they are found to have been negligent, this could be a significant liability quite apart from any possible criminal sanctions. By evidencing their effort to comply through exercising due diligence, directors and officers will be better equipped to protect themselves against a finding of negligence.

(a) In-House Due Diligence

A due diligence checklist should be developed in keeping with the unique characteristics of each charity. The checklist should identify and eliminate potential risk areas for the particular charity, taking into consideration how the new legislation will apply to its unique programs. At the same time, it must be designed in order to give guidance to the charity on how to continue to be effective in meeting its charitable objects and avoid unnecessary limitations on its activities. The due diligence checklist should be designed to enable the charity to assess the level of compliance of its charitable programs with Anti-terrorism Legislation and the level of risk that each of its programs might pose. All relevant aspects of Anti-terrorism Legislation and of the charity's Anti-terrorism policy that apply to its charitable programs should be incorporated into the due diligence compliance checklist. The checklist should reflect the "Super *Criminal Code*", money-laundering and terrorist financing provisions, as well as any relevant provisions in the *Foreign Missions Act* and the *Public Safety Act*.

(b) Due Diligence Concerning Third Parties

Due Diligence Concerning Affiliated Charities

Charities should also conduct a comprehensive Anti-terrorism audit of the organizations, individuals, and institutions they are affiliated with. This would include (as mentioned above) umbrella associations to which the charity belongs or, if the charity itself is an umbrella organization, other organizations that are members of the charity. It would also include other registered charities in conjunction with which the charity works, whether through informal cooperation or by formal joint venture or partnership agreements. Affiliated charities that either receive funds from the charity or give funds to the charity can create put the charity at risk if they are not complying with Bill C-36.

Due Diligence with Regard to Third Party Agents

All third party agents of a charity, including agents that act on behalf of a third party agent for a charity, can expose the charity to liability by directly or indirectly being involved in the facilitation of a "terrorist activity". In addition to reviewing third parties for potential risks, charities should encourage their agents to take their own steps to ensure compliance with the law by establishing Anti-terrorism policies and regular audits, due diligence check-lists, etc. Agents should be required to provide releases and indemnities to the charity in the event of non-compliance with Anti-terrorism Legislation.

Due Diligence Concerning Donors

Charities should exercise vigilance in monitoring incoming donations with respect to the identity of the donor, and the manner in which the donor obtained the funds, as well as with regard to any donor restrictions on donated funds that could put the charity in contravention of Anti-terrorism Legislation. Charities must regularly review their donor-lists for "listed entities" or organizations that may be terrorist groups, affiliated with terrorist groups, or inadvertently facilitating terrorist activity. They must also ensure that a donor would not be able to use any of the charity's programs to permit the flow-through of funds directly or indirectly to a terrorist activity.

All third parties with whom the charity is associated, including donors, agents, and affiliated charities among others, should be required to provide appropriate disclosure statements, as well as releases and indemnities in the event of non-compliance with Anti-terrorism Legislation.

(c) Documenting Due Diligence

Anti-terrorism Policy Statements

An Anti-terrorism policy statement is a charity's obvious first line of defence to show that it has addressed the possible risks to the charity and is making every effort to comply with applicable legislation. Along with the due diligence checklist, it is also a very effective tool to educate a charity's directors and officers about the charity's potential risks and liabilities. An Anti-terrorism policy statement must be carefully thought out with the guidance of legal counsel. The full cooperation of the charity's board and officers is necessary in order to make the policy statement reflect the individual needs and risks of each charity and to enable it to continue to meet its charitable objectives with the least possible interference. The process of preparing such a statement will, of course, require a comprehensive review of the charity's operations in order to identify the charity's risks and objectives. In fact, a charity's Anti-terrorism policy statement should include a requirement to complete a comprehensive audit of the charity's existing programs on a regular basis and of all new program proposals as part of the initial review to decide whether to undertake a new program. These audits should be executed in accordance with the due diligence checklist which reflects the unique characteristics of each charity.

Reporting Requirements under the Proceeds of Crime Act

The reporting requirements under the *Anti-terrorism Act* may also have an impact on charitable fundraising involving any large cash donations or the funding of international projects. This may unduly deter *bona fide* donors from making significant donations to Canadian charities, especially organizations that the donors are not intimately familiar with, or discourage Canadian charities from transferring much-needed funds to support projects in foreign jurisdictions. A Canadian charity which transfers charitable funds to a foreign charity under an agency or joint-venture agreement may find itself becoming the subject of a reported transaction to the Financial Transactions and Reports Analysis Centre of Canada ("FINTRAC").

8. CIVIL PENALTIES FOR MISREPRESENTATIONS OF TAX MATTERS BY THIRD PARTIES UNDER THE *INCOME TAX ACT*

As part of the Federal Budget of February 1999, the Federal Government proposed civil penalties for misrepresentation of tax matters by third parties. The proposed amendment was the subject matter of much debate amongst tax professionals[139]. On June 29, 2000, section 163.2 of the *ITA* was introduced to provide for a new civil penalty for third parties, which was intended to include tax preparers, advisors, tax shelter promoters and valuators who cause others to

[139] For a detailed discussion of problems inherent in the proposed new s. 163.2, reference should be made to (Sept. 23) *Tax Topics* #1437 (CCH Canadian Ltd., 1999) and (Sept. 30) *Tax Topics* #1438 (CCH Canadian Ltd., 1999).

misrepresent their tax owing. There are two separate penalties, which are explained by CRA in Information Circular IC 01-1 as follows:

> Both section 163.2 of the ITA and section 285.1 of the ETA provide for two penalties, one directed primarily at those who prepare (or participate in), sell or promote a tax shelter or tax shelter-like arrangement, and the other directed at those who provide tax-related services to a taxpayer. The first of these two penalties will be referred to as the "planner penalty" and the latter will be referred to as the "preparer penalty" throughout the rest of this circular.

CRA's Fact Sheet dated November 2002 concerning art-donation or art-flipping schemes indicates that third party penalty can include charities that receive the donation if "it knows – or if it can reasonably be expected to have known – that the appraised value were incorrect." This position of CRA is confirmed in CRA's *Registered Charities Newsletter* No. 16 issued on October 9, 2003.

In this regard, Information Circular IC 01-1 specifically indicates the following:

> If the charity knew, or would have reasonably been expected to know but for circumstances amounting to culpable conduct, that the valuations were incorrect, it would be liable for the penalties for issuing false receipts.

Even though subsection 163.2 of the *ITA* imposes penalties on tax advisors who become involved in making false statements or submissions in relation to tax matters has been softened somewhat by replacing a "gross negligence" standard in the proposed legislation with a more moderate "culpable conduct test", the extent of the resulting liability is not limited to tax professionals or tax advisors only. It also encompasses professional fundraisers as well as any individuals who are involved directly or indirectly in giving tax advice. This would include individuals who advise on the tax implication of giving a donation to a charity, which in many situations will include fundraisers. It could also include volunteers of a charity who may have suggested that there is a tax advantage involved in a particular type of gift by a donor when there is not.

Subsection 163.2 also applies to advice given on the Internet through the website of a charity, whether the advice is in a "static" written form or involves an exchange back and forth between a representative of the charity and the donor, whether the representative is a professional fundraiser, employee of the charity, or a volunteer of the charity. As a result, Subsection 163.2 of the *ITA* will need to be carefully studied by fundraisers, charities, and their board of directors to ensure that there is compliance with this recent change to the *ITA*.[140]

9. CHARITABLE GAMING AND LOTTERIES

Not surprisingly, there are numerous legal risks that a charity would encounter in embarking upon charitable gaming and lotteries. However, since it is beyond the scope of this paper to address the issues involved in charitable giving and lotteries, the reader should refer to the reference text on the law of charitable gaming in Canada, *The Law of Charitable and Casino Gaming,*[141] by Donald Bourgeois.

10. THE EFFECT OF NEW REGULATIONS UNDER THE *CHARITIES ACCOUNTING ACT*

A. Background to Regulation

Regulation 04/01 adopted under Section 5.1 of the *CAA* was filed by the Public Guardian Trustee of Ontario ("PGT") on behalf of the Ministry of the Attorney General on January 17, 2001 and was published in the Ontario Gazette on February 3rd, 2001 ("the Regulation").

The Regulation had been anticipated ever since Section 5.1 of the *CAA* was passed in 1996. Section 5.1 authorized the adoption of regulations by the Attorney General to permit certain prescribed activity involving charitable property that would otherwise have required the approval of the Superior Court of Justice. This involved the following:

[140] See Manwaring, *supra* note 123 at p.1.
[141] Donald J. Bourgeois, *The Law of Charitable and Casino Gaming* (Toronto: Buttersworth, 1999).

- permitting directors to receive remuneration from charities on whose boards of directors they sit;

- permitting charities to indemnify trustees, executors, directors and officers for personal liability arising out of their offices, as well as to purchase directors and officers liability insurance; and

- allowing charities to co-mingle multiple restricted funds held by the charity into a single account or investment portfolio.

B. No Relief to the Common Law Rule Prohibiting Directors from Receiving Remuneration

Unfortunately, the current Regulation does not deal with (a) above, i.e., authorizing directors and trustees to receive any remuneration from the charity. Therefore, the common law rule in Ontario still applies, i.e. that directors of a charity, in their quasi trustee role, have a fiduciary obligation not to put themselves into a conflict of interest by receiving remuneration, either directly or indirectly, from the charity on which they serve as a director. The Public Guardian and Trustee has indicated that further regulations dealing with this issue may be passed in the future but, for now, the current common law in Ontario continues to apply. Consequently, it will continue to be necessary for the board of a charity and its legal counsel to ensure that the charity's by-laws and other constating documents do not permit the remuneration of directors other than for reimbursement of out of pocket expenses.

Some of the consequences arising from the new Regulation failing to authorize the remuneration of directors are as follows:

- Charities may continue to find if difficult to attract qualified candidates to its board of directors where those candidates are providing goods and services to the charity either at or below market value, such as inexpensive or pro-bono services by a lawyer or accountant.

- Some religious charities for doctrinal reasons may find it theologically unacceptable that their minister cannot be a member of the controlling board of the church simply because the minister receives remuneration from the church. In those situations, it may be necessary for churches or other religious organizations to make an application for a consent order from The *PGT* under section 13 of the *CAA* to permit such payment.

- For those charities that do not want to go to the trouble or expense in obtaining a consent order from the *PGT*, an alternative would be to structure the by-law and other constating documents of the charity so that the employee in question, such as an executive director, will not be a member of the Board of Directors but will be given substantive rights over the day to day operations of the charity, including the right to receive notification of all board meetings, be present at all board meetings, and participate at all board meetings (save and except when such board meetings are dealing with the position of the Executive Director) but without such person being a member of the board of directors. For a more detailed discussion concerning issues involving remuneration of directors, see articles by the author entitled "*Remuneration of Directors in Ontario*" and "*Update on Remuneration of Directors in Ontario*" found at www.*charitylaw.ca*.

C. Indemnification of Directors and Officers and Liability Insurance

Under the Regulation, a charity may indemnify a trustee or executor or, where the executor or trustee is a corporation, indemnify the directors or officers of the corporation, for personal liability arising from an act or omission in performing his or her duties. However, a charity may not indemnify for liability arising from a failure to act honestly and in good faith in performing these duties.

The ability of a charitable corporation to adopt an indemnity by-law had been in question as a result of an error in the wording in recent amendments to the *Corporations Act*. However, this omission has recently been corrected through a further amendment to the *Corporations Act* which now ensures that Ontario non-share capital corporations can indemnify their directors and officers, provided that the terms and conditions of the Regulation adopted under the *CAA* have been followed.

The Regulation also provides that insurance may be purchased to cover personal liability arising from the act or omissions of the executors, trustees, directors or officers of a charity in performing their duties. However, the terms of the insurance or indemnification must not impair a person's right to bring legal action against the executor, trustee, director or officer. In addition, the Regulation states that the purchase of the insurance policy must not unduly impair the carrying out of the religious, educational, charitable or public purposes for which the charity holds property. The Regulation further states that the executor or trustee, and if the executive director is a corporation, the board of directors of the corporation, must consider the following before giving an indemnity or purchasing insurance:

- The degree of risk to which the executor, trustee, director or officer is or may be exposed.
- Whether, in practice, the risk cannot be eliminated or significantly reduced by means other than the indemnity or insurance.
- Whether the amount or cost of the insurance is reasonable in relation to the risk.
- Whether the cost of the insurance is reasonable in relation to the revenue available to the charity.
- Whether it advances the administration and management of the charitable property to give the indemnity or purchase the insurance.

The Regulation states that no indemnity may be paid or insurance purchased if to do so would result in the amount of debts and liabilities exceeding the value of the charitable property, or, if the executor or trustee is a corporation, render the corporation insolvent. Another limitation is that the indemnity may only be paid or the insurance purchased from the charitable property to which the personal liability relates and not from any other charitable property. This would appear to mean that the income from segregated funds, such as endowment funds, that would otherwise not normally attract potential liability for a director or officer should not be used to purchase directors and officers liability insurance or to pay an indemnity.

The consequences of the Regulation permitting indemnification of directors and officers of a charity and the purchase of liability insurance can be summarized as follows:

- It will be important for the directors of a charity to carefully review all of the Regulation to ensure that the director complies with its terms before proceeding with the adoption of an indemnification by-law or the purchase of directors and officers liability insurance.

- If the charity complies with the Regulation, it is important to determine whether the indemnification by-law have been passed and/or insurance has been purchased prior to the publication of the Regulation on February 3rd, 2001. Since the Regulation is not stated to be retro-active, it is possible that an indemnification by-law adopted prior to the publication of Regulation 04/01 may need to be passed as a new by-law or may require the adoption of a current resolution that the board of directors has reviewed the conditions and terms of Regulation 04/01 and are satisfied that the indemnification in question and/or the purchase of liability insurance complies with the terms and conditions of the Regulation.

- Since charities will in most circumstances now be able to purchase directors and officers liability insurance from the funds of the charity, it will become less problematic to recruit qualified volunteers as directors to its board of directors.

D. Charities May Co-Mingle Restricted and Special Purpose Funds

Under the Regulation, a charity may now co-mingle property funds received for a restricted or special purpose with other properties similarly received into a single account or investment portfolio. However, a number of restrictions and obligations are imposed by the Regulation which may make the option of co-mingling funds difficult or impractical. In this regard, a charity that is intending to co-mingle property or funds held or restricted or special purposes:

- may only do so if it advances the administration and management of each of the individual restricted funds;

- must allocate all gains, losses, income and expenses rateably on a fair and reasonable basis to the individual funds; and

- must maintain detailed records relating to each individual fund, including:
  - the value of the individual fund immediately before it becomes part of the combined fund, and the date on which it becomes part of the combined fund;
  - the value of any portion of the individual fund that does not become part of the combined fund;
  - the source and the value of contributed fund (i.e. additional fund that is added to and forms part of a pre-existing individual fund) relating to an individual fund, and the date on which the contributed fund is received;
  - the value of the contributed fund immediately before it becomes part of the combined fund, and the date on which it becomes part of the combined fund;

- the amount of the revenue received by the combined fund that is allocated to the individual fund, and the date of each allocation;
- the amount of the expenses paid from the combined fund that are allocated to the individual fund, and the date of each allocation; and
- the value of all distributions from the combined fund made for the purposes of the individual fund, and the purpose and date of each distribution.

- Must maintain detailed records relating to the combined fund, including the following:
  - the value of each individual fund that becomes part of the combined fund, and the date on which it becomes part of the combined fund;
  - the value of contributed funds that become part of the combined fund, the date on which it becomes part of the combined fund, and the details of the individual fund to which the contributed fund relates;
  - the amount of the revenue received by the combined fund, the amount allocated to each individual fund, and the date of each allocation;
  - the amount of expenses paid from the combined fund, the amount allocated to each individual fund and the date of each allocation; and
  - the value of all distributions from the combined fund made for the purposes of an individual fund and the purpose and date of each distribution.

In light of the double records that must be maintained and the detail of those records, a charity may very well decide that it would be simpler and less problematic to maintain each restricted or special purpose trust fund in a separate account for investment purposes notwithstanding the likely lower rate of return for the over all portfolio investment of the charity. It is therefore important for the board of directors of a charity to weigh the benefits to be gained from combining restricted and special purpose funds against the significant administrative costs and aggravation of keeping the necessary records in order to co-mingle restricted and special purpose funds. It is also important for the board of a charity to realize that co-mingling restricted or special purpose funds in contravention of the Regulation will expose the directors to allegations of breach of trust and resulting personal liability.

11. IMPROPER ISSUANCE OF CHARITABLE RECEIPTS

A. General Comments

No discussion of legal liability involving fundraising would be complete without a review of situations where charitable receipts under the *ITA* are improperly issued. However, the tax issues that are involved under the *ITA* are so many and are so detailed that it would be both impractical and a disservice to the reader to attempt to summarize all of the applicable rules. The impracticality of doing so is evidenced by the fact that there is already a voluminous loose leaf service available on the topic.[142]

What would be of assistance for the purposes of this paper is to outline some of the recent resource materials made available from CRA and to provide a brief summary of some of the more common instances when a charity may become involved in improperly issuing charitable receipts.

B. Recent Resource Materials from CRA[143]

Given the virtual avalanche of materials that has been released by CRA almost every few months[144] over the last two years, it would be impossible to discuss in any detail or even mention all of the additions and changes to the CRA website which affect charities. Instead, what is attached as Appendix 8 to this paper is a synopsis, current to March 22, 2004, of all publications that have been published by CRA with regards to charities from 2002 to 2004. The summary at Appendix 8 organizes the material from CRA in a practical fashion for the fundraiser and practitioner. The reader is advised, though, that the compendium of documents attached as Appendix 8 is *not* an official CRA publication, and as such the reader should refer to the actual documents on the CRA website for official identification and texts of the materials. What follows in this part of the paper is

[142] See Drache, *supra* note 3.

[143] See "Recent Changes to the Income Tax Act and Policies Relating to Charities and Charitable Gifts", by Terrance S. Carter and Theresa L.M. Man, March 1, 2004, presented to the Society of Trust and Estate Practitioners, March 4, 2004. Also available at www.charitylaw.ca.

[144] In the period between September 1, 2003 and March 22, 2004, CRA issued and posted two Policy Statements, over 100 Summary Policies, *Registered Charities Newsletter* No. 16, and over 100 Information Letters on the CRA website. See http://www.ccra-adrc.gc.ca/tax/charities/menu-e.html for CRA's Charities Directorate website.

a brief commentary of the CRA material on its website as reflected in the detail contained in Appendix 8.

Legislative amendments currently include the December 20, 2002 draft technical amendments ("December 2002 Amendments"),[145] the February 18, 2003 Federal Budget 2003 ("February 2003 Budget")[146], the December 5, 2003 draft amendments (the "December 2003 Amendments")[147], and the February 27, 2004 revised draft amendments (the "February 2004 Amendments")[148] issued by the Department of Finance. While these legislative amendments were initiated by the Department of Finance, they were created in consultation with CRA. The changes resulting from these pieces of legislation will have a fundamental impact on the regulation and operation of charities and therefore have been included by CRA on its website.

C. Selected Examples of Improper Issuance of Charitable Receipts

The following is intended as a brief synopsis gleaned from the above mentioned CRA resource Materials of some of the more common situations involving fundraising where a charity may either knowingly or unknowingly have become involved in the improper issuance of charitable receipts. The situations that are listed are of a selective nature and do not purport to cover every situation where a charity may otherwise be improperly issuing charitable receipts. The impact of recent changes to the *ITA* concerning receipting is discussed in the next part of this paper.

- Contributions of services may not be acknowledged by the issuance of a charitable receipt. A gift must involve the gift of property. A contribution of services, that is,

[145] The December 2002 Amendments issued by the Department of Finance have yet to come into effect as of March 22, 2004. The December 2002 Amendments were available for comment until March 23, 2003. In the meantime, both the Department of Finance and CRA, have advised that charities ought to handle gifts and receipting "as if" the legislation was passed.

[146] The February 2003 Budget was passed into law pursuant to *An Act to implement certain provisions of the budget tabled in Parliament on February 18, 2003*, Bill C-28, Assented to June 19, 2003.

[147] The December 5 2003 Amendments to the *ITA* issued by the Department of Finance have yet to come into effect. The amendments largely restrict and limit the tax benefits previously enjoyed by donors under charitable donation tax shelter donation arrangements.

[148] The February 27, 2004 Amendments to the *ITA* issued by the Department of Finance have yet to come into effect. The Amendments largely consolidate earlier tax legislation amendments, and also introduce and modify other provisions of the *ITA*.

time, skill, or effort, is not considered to be a gift of property and therefore will not qualify for a charitable receipt.

- A charity may not issue an official receipt where the donor has directed the charity to give the funds to a specified person or family.

- Donations that are subject to a general direction from the donor that the gift be used in a particular program operated by the charity are acceptable, provided that no benefit accrues to the donor, the directed gift does not benefit any person not dealing at arms length with the donor, and the decisions regarding utilization of the donation within a program rests with the charity.

- A charity cannot issue receipts for 100% of a student's tuition fees paid to a privately funded secular or religious school by having the tuition fees paid by the parents indirectly through a scholarship fund operated by the school or by another charity associated with the school that purports to grant "scholarships" for tuition fees to children attending the school.[149]

- A charity may not issue a charitable receipt if the donor has directed the charity to give the funds to a non "qualified donee" as defined under subsection 149.1(1) of the *ITA*. Most foreign charities or foreign affiliates of a Canadian charity, with the exception of a "prescribed university", would not meet the definition of a "qualified donees" and as such gifts directed to them would not be eligible for an official charitable receipt.150

- A charitable receipt cannot be issued for the payment of a lottery ticket or other chance to win a prize.

- A charity that receives a gift in kind can only issue receipts for the fair market value of the gift as of the date that it was donated. When a gift in kind has a fair market value of $1,000.00 or more, a qualified written appraisal is required to justify the amount shown on the receipt.

- If an individual gives a security to a charity that is a "non qualifying security" as defined under subsection 118.1(18) of the *ITA*, a credit for the donation will be denied at the time that the gift is made and the donor will only be entitled to receive a charitable receipt if the charity subsequently disposes of the "non qualified security" within a period of sixty (60) months from the date of the gift. A "non qualifying security" is defined as including shares, obligations or securities of a corporation or person with

[149] Woolner, *supra*, note 100.

[150] Beaudry, *supra* note 56.

whom the donor does not deal "at arms length". Specifically excluded, though, from the definition of "non qualifying securities" are shares, obligations and other securities listed on prescribed stock exchanges and amounts deposited with financial institutions. Excluded as well from "non qualifying securities" are "excepted gifts" as defined under subsection 118.1 (19) of the *ITA* as gifts that meet the following requirements:

- they are limited to shares of a corporation as opposed to debt;
- the donee charity must not be a "private foundation";
- the donor must deal at arms length with the donee charity; and
- the donor must deal at arms length with each director, trustee, officer and like official of the donee charity.

The practical effect of the definition of "excepted gift" and "non qualifying security" is that no charitable receipt can be issued by a charitable organization or a public foundation for the gift of shares or securities of a corporation that are not the shares or securities of a publicly traded company on a "prescribed stock exchange" as defined or where such gift is made by a director, trustee, officer or other like official of the charitable organization or public foundation or by anyone related to or otherwise not dealing at arms length with such person.

- In accordance with Resolution 21 in the 1997 Federal Budget intended to stop "loanbacks", subsection 118.(16) provides that the amount of a charitable tax credit that a donor can claim will be reduced in a situation where a gift is made to a charity, other than a gift of a *"non-qualifying security*", and within 5 years thereafter if;

  - **-** charity holds a "*non-qualifying security*" of the donor where the charity acquired the security no earlier than 5 years before the gift was made; or

  - the charity allows the donor to use the property so gifted within 5 years of the original gift, the use of such property was pursuant to an agreement made or modified no earlier than 5 years before the making of the gift, and the use of the property was not in the course of the charity's charitable activities.

  Pursuant to Section 118.1 (16) and (17) of the *ITA*, and depending upon the applicable circumstances, the amount of the tax credit or deduction that had been claimed for the gift will have to be reduced by the amount the charity gave to acquire the "*non qualifying security*" or by the value of the property the charity allows the donor to use.

- A gift to a charity for the use of vacation property, usually auctioned by a charity at a fundraising event, has now been determined by Canada Customs and Revenue to be ineligible as a receiptable gift. An earlier position by Canada Customs and Revenue setting out circumstances under which a charitable receipt could be issued for the fair market value of a gift of vacation property was explained in a letter by Carl Juneau, Assistant Director of Charities, in the fall of 1998.[151] The letter was considered to be a reasonable interpretation of Department policy at that time. However, the Rulings Directorate, which is responsible for policy at Canada Customs and Revenue, in April 1999, reversed the earlier position and stated that since a receiptable gift requires the voluntary transfer of property without consideration, the mere granting of a right to use property for a limited period of time did not constitute an acceptable "transfer of property". Canada Customs and Revenue notified taxpayers of its change in position in Bulletin ITTN-17 released on April 26th, 1999. As a result, effective as of April 26, 1999, loans of vacation property to a charity will no longer be considered to be a gift of property for which a charitable receipt can be issued.[152] This will no doubt cause problems for charities that have relied upon such gifts as part of a successful charity auction event.

12. RECENT CHANGES TO THE *INCOME TAX ACT* AFFECTING CHARITABLE RECEIPTING[153]

A. New Definition of Gift

The December 2002 Amendments introduced a new concept of "gift" for tax purposes which is different from the traditional concept of "gift" at common law as a result of the insertion of subsections 248(30), (31), (32) and (33) to the *ITA*, which will apply to gifts made after December 20, 2002, once the legislation is finally passed.[154]

At common law, in order to have a valid gift, three elements are required: (1) the donor must have an intention to give, (2) there must be successful delivery of the gift from the donor to the donee, and (3) the gift must be accepted by the donee. The Explanatory Notes to the December 2002 Amendments state that, at common law, property must be transferred voluntarily, without any contractual obligation and with no advantage of a material nature returned to the donor and that, as such, a contract to dispose of a property to a charity at a price below fair market value would not

[151] See (1997) 1:1 *Charity & the Law Update* (Sept. 26th), for a summary of the letter. (Found also at www.charitylaw.ca).
[152] See (1999) 1:3 Charity & the Law Update (April 30th). (Found also at www.charitylaw.ca).
[153] *Supra* note 143.
[154] *Supra* note 145.

generally be considered to include a gift. However, the new subsections 248(30) to (33) of the *ITA* will create a new concept of "gift" for tax purposes, which will permit a donor to have a tax benefit under the *ITA* even though the donor (or a person not dealing at arm's length with the donor) received a benefit, provided that the value of the property exceeds the benefit received by the donor.

It would appear from the Explanatory Notes that the rationale for expanding the definition of "gift" compared to that of the long-established rules at common law is an attempt by CRA to offer a benefit to donors of gifts that are permitted under section 1806 of the *Civil Code of Québec*[155], whereby it is possible to sell property to a charity at a price below fair market value, resulting in a gift of the difference. This is based on the rule that a gift in Quebec is a contract by which ownership of property is transferred by gratuitous title. In order to achieve this result, CRA appears to have accepted a line of caselaw at common law[156] whereby the courts have accepted transfers of property to a charity where the transfer was made partly in consideration for services and partly as a gift.

The new subsection 248(30) of the *ITA* introduced by the December 2002 Amendments defines the "eligible amount of a gift" to be "the amount by which the fair market value of the property that is the subject of the gift exceeds the amount of the advantage, if any, in respect of the gift". The December 2003 Amendments clarified that subsection 248(30) is also applicable to monetary contributions made to registered parties and candidates by including additional references to "monetary contributions" in this subsection, as well as by cross referencing the term "eligible amount" in subsection 127(3) of the *ITA* which provides that monetary contributions to registered parties and candidates may be deducted from tax. This subsection applies to gifts made after December 20, 2002.

The "amount of the advantage" in respect of a gift or political contribution is defined in subsection 248(31). The wording of subsection 248(31) introduced by the December 2002 Amendments has

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[155] S.Q., 1991, c. 64.

[156] See *Gonthier v. The Queen*, Court File No. 2001-2389 (IT)I; *Pennington v. Wain*, [2002] 4 All. E.R. 215; *The Queen v. Freidberg*, 92 DTC 6031 (FCA); *Woolner v. Attorney General of Canada*, 99 DTC 522 (FCA), *The Queen v. Zandstra*, 74 DTC 6416 (FCA).

been substantially amended by the December 2003 Amendments, which was further amended by the February 2004 Amendments and has now become subsection 248(31) (a) by the insertion of a new subsection 248(31) (b), which requires the reduction of the amount of a gift by the limited-recourse debt incurred by the donor

B. Split-Receipting

On December 24, 2002, CRA released *Income Tax Technical News* No. 26 ("Technical News No. 26") to supplement the December 2002 Amendments to the *ITA* concerning the definition of gift. Technical News No. 26 contains proposed new guidelines on split-receipting in order to explain CRA's new administrative policy in relation to "determining whether there is a gift in situations other than where there is an outright transfer of property for no consideration". Technical News No. 26, as well as *Registered Charities Newsletter* No. 17, released in January of 2004, also addresses a number of common gifting situations. Existing interpretation bulletins and publications of CRA will be revised in order to reflect these new administrative guidelines.

Prior to the amendments, the ability of a charity to issue a charitable receipt was subject to strict rules, which reflected an understanding of what a gift was at common law, i.e. that there could be no advantage received back by the donor. The only exception to this rule was in the scenario when a charity gave the donor a gift of "nominal" value – a term defined to mean the lesser of $50 or 10 per cent of the gift. The new rules go much further, however, as they allow charities to issue charitable receipts for the difference between the donor's benefit (now called the 'advantage') and the fair market value of the value of the gift as discussed further below.

C. Tax Shelter Donation Programs

Among measures announced in the February 2003 Budget was an amendment to broaden the definition of "tax shelter" in the *ITA*. A "tax shelter" is defined under subsection 237.1(1) of the *ITA* as any property for which a promoter represents that an investor can claim deductions or receive benefits which equal or exceed the amount invested within four years of its purchase. The definition of tax shelter has now been amended to include gifting arrangements, tax credits, refunds and deductions, since previously only deductions from income or taxable income were accounted for when determining whether or not an arrangement was a tax shelter. The newly amended section was introduced into the House of Commons via Bill-C28: *An Act to Implement Certain Provisions of the Budget Tabled in Parliament on February 18, 2003*, which was passed into law on June 19, 2003.

(1) CRA's Warnings with Respect to Tax Shelter Donation Programs

CRA's warning on tax shelter donation programs, as set out in CRA's FactSheet dated November 2000 entitled "Canada Customs and Revenue Agency Reminds Investors of Risks Associated with Tax Shelters", stated that registration as a tax shelter "does not indicate that the CRA guarantees an investment or authorizes any resulting tax benefits" and that "[the] CRA uses this identification number later to identify unacceptable tax avoidance arrangements". CRA's FactSheet dated November 2002 concerning art-donation or art-flipping schemes indicates that third party penalties can include charities that receive the donation if "it knows – or if it can reasonably be expected to have known – that the appraised values were incorrect." This position was confirmed in CRA's *Registered Charities Newsletter* No. 16 issued on October 9, 2003.

In this regard, Information Circular IC 01-1 specifically states the following:

> If the charity knew, or would have reasonably been expected to know but for circumstances amounting to culpable conduct, that the valuations were incorrect, it would be liable for the penalties for issuing false receipts.

The donation of items of "speculative value" was again brought up in *Registered Charities Newsletter* No. 16 issued on October 9, 2003, by explaining that such situations could involve "trading cards, comic books, and used cars, where a promoter facilitates the donations to the charity." In *Registered Charities Newsletter* No. 16, CRA also warns that the donation of such items could result in the charity not being able to meet its disbursement quota:

> A charity should not lose sight of the fact that it is the amount for which the receipt is issued that is included in its disbursement quota requirement for the following year, even though the charity may in turn sell the property for an amount far below the amount for which the receipt was issued. Failure to meet the disbursement quota is grounds for us to revoke a charity's registered status. In some cases, the charity gambles that the property will be worth at least the receipted amount at some future time.

In *Registered Charity Newsletter* No. 16, CRA pointed out that charities are not obligated to either receive or receipt a gift if they choose not to:

> Charities are reminded that they are not obliged under the *Income Tax Act* to issue official donation receipts for gifts; nor are they required to accept gifts. Before accepting gifts-in-kind, charities should ask themselves how the gift would allow them to further their charitable purposes.

On November 25, 2003, CRA released a factsheet entitled "Tax Shelter Donation Arrangements", which provides numerous additional warnings and guidelines with respect to tax shelter donation schemes. CRA defined these donation arrangements as involving:

> …items sold, often in bulk, through a promoter who donates them to a registered charity which then issues a tax receipt for a considerably higher amount than was paid for the donated items. This type of donation scheme results in an income tax credit for the donor greater than the price paid, and may be disallowed by the Canada Customs and Revenue Agency (CCRA) at a later date.
>
> An example of this – A tax shelter promoter presents an arrangement to you where you can buy – without taking possession of – a quantity of supplies at a bargain basement price. The promoter then arranges for this to be appraised and donated to a registered charity, which will then provide you with a tax receipt based on the appraised value. The tax receipt will be high enough to produce a tax credit greater than the cost of the property plus any capital gains taxes resulting from the arrangement.

Considerable emphasis was given in the factsheet to the possibility of third-party civil penalties. As well, CRA advises that the transactions described below may be challenged by CRA:

- the advertised arrangements promise to sell items (such as art, software, or pharmaceuticals) to taxpayers to be donated immediately to selected charities for tax receipts that are much higher than what the person paid;
- the appraiser is not acting independently of the promoters or sellers of the arrangement or the charities involved;
- the fair market value seems too high;
- where the arrangement involves a loan where it's unlikely the person has to repay the loan because the lender's recourse to collect is limited, or the provision to settle the loan is by way of something other than cash payment from the taxpayer.

(2) December 2003 and February 2004 Amendments Curtailing Tax Shelter Donation Programmes

On December 5, 2003, at 6 p.m., the December 2003 Amendments were announced by the then Deputy Prime Minister and Minister of Finance, having the effect of limiting tax benefits from charitable donations made under tax shelter donation arrangements. The Department of Finance was taking steps to curtail the scope of tax shelter donation arrangements after receiving public complaints and concerns with respect to donation promoters selling the "buy-low, donate-high" schemes that often provide the donor exceptionally high tax-benefits. The Department of Finance, like CRA, was concerned that the government was losing substantial amounts of tax dollars when the taxpayer/donor was able to claim higher tax deductions than he/she was otherwise entitled to.

(a) Limiting Tax Shelter Donation Schemes Involving Donation of Property

The December 2003 Amendments propose to insert a new subsection 248(35) in the *ITA*, of which subparagraph (a) provides that if the taxpayer acquires the property through a "gifting arrangement" as defined in section 237.1 of the *ITA* described above, then the fair market value of the property donated, for purposes of the charitable donation receipt issued by the receipting charities, shall be "deemed" to be the lesser of (i) the "fair market value of the property otherwise determined" and (ii) the cost (or the adjusted cost base in the case of capital property) of the property "to the taxpayer immediately before the gift is made" (the "Deeming Provision"). As such, it is irrelevant when the property was acquired by the donor through the gifting arrangement. Subsection 248 (36) states that the Deeming Provision does not apply to inventory, real property situated in Canada, certified cultural property, publicly traded shares or ecological gifts. Paragraph 248 (35)(a) applies to gifts made on or after 6 p.m. on December 5, 2003. The wording of paragraph 248(a) that was introduced by the December 2003 Amendments were brought forward and included in the February 2004 Amendments.

(b) Other Applications of the Deeming Provision

In introducing the Deeming Provision for donation of property acquired through gifting arrangements, the Department went further than simply curtailing the tax shelter donation schemes addressed by paragraph 248(35)(a). The Department further introduced paragraph 248(35)(b) to provide that the Deeming Provision also applies to donation of property under two other situations, namely, (1) pursuant to subparagraph 248(35)(b)(i), if the property was acquired by the donor less than three years before the day that the gift is made, and (2) pursuant to subparagraph 248(35)(b)(ii), if it is "reasonable to conclude that, at the time the taxpayer acquired the property, the taxpayer expected to make a gift of the property." Under the former scenario, if a donor acquires property and donates the property within three years from the date of acquisition, then the fair market value of the property shall be deemed to be the donor's cost or adjusted cost base. Under the latter scenario, regardless of when the donor acquired the property (even outside of the three-year limitation period), as long as it is "reasonable to conclude" that the donor had the intention to make a gift at the time when the property was acquired, then the Deeming Provision would apply. The burden is on the donor to prove that he or she did not have an intention to make a gift when the property was acquired.

Pursuant to subsection 248(36), paragraph 248(35)(b) does not apply to inventory, real property situated in Canada, certified cultural property, publicly traded shares, or ecological gifts. As well, the opening wording of paragraph 248(35)(b) provides that the Deeming Provision does not apply to situations where the gift is made as a consequence of the donor's death. Paragraph 248(35)(b) applies to gifts made on or after 6 p.m. on December 5, 2003.

(c) Restricting the Use of Tax Shelter Donations Involving Limited Recourse Debt

In addition to the donation of property to charities under the gifting arrangements of tax shelter donation schemes, another type of gifting arrangement which the Department felt the need to restrict involves limited-recourse debts incurred by donors (also known as "leveraged loans" or "leveraged donation shelters"). This usually involves a donor borrowing monies from a lender, followed by the donor donating the borrowed fund together with some of his or her own funds to a charity in return for a charitable donation receipt for the cumulative amount donated. At the same time, the donor pays a fee or other charges to the promoter, which fee or charges would be used to purchase property or to be invested for a return that would, over the term of the loan, be sufficient to pay off the loan borrowed.

The February 2003 Budget, in expanding the definition of "tax shelter" in section 237.1(1) of the *ITA* to include property acquired under a gifting arrangement, also expanded the definition of "tax shelter" to include a gifting arrangement under which it may reasonably be expected, having regard to representations made, that if a taxpayer makes a gift or contribution under the arrangement, a person (whether or not it is the taxpayer himself or herself) will incur an indebtedness in respect of which recourse is limited.

The December 2003 Amendments propose to curtail the use of these arrangements by introducing a series of amendments to the *ITA*, including the insertion of new subsection 143.2(6.1) to the *ITA*, the amendment of the wording of subsection 143.2(13) before paragraph (a), the insertion of new paragraph (b) to subsection

248(31) that was introduced by the December 2002 Amendments[157], as well as the insertion of new subsection 248(34) to the *ITA*. These amendments only apply to donations made after February 18, 2003.

(d) Substantive Gifts

The February 2004 Amendments proposed the insertion of a new subsection 248(38) that applies to gifts made on or after February 27, 2004. The Explanatory Notes to the February 2004 Amendments indicate that subsection 248(38) is intended to prevent a donor from avoiding the application of the Deeming Provision set out in subsection 248(35) by disposing the property to a qualified donee and then donating the proceeds of disposition, rather than the donor donating the property directly to the qualified donee. The property disposed of by the donor is referred to as "substantive gift" in this subsection. The opening wordings of this subsection makes it clear that this subsection only applies to capital property and eligible capital property. This subsection also applies to political contributions. However, this subsection does not apply to the property already exempted under subsection 248(36), e.g. publicly-traded shares, real estate situated in Canada, etc, as described above.

As such, when a person disposes of capital property or eligible capital property to a qualified donee and donates the proceeds of disposition to either that qualified donee or to another qualified donee that does not deal at arm's length with the qualified donee that purchased the property from the donor, then the capital property or eligible capital property will now be referred to as a "substantive gift". Under those situations, the Deeming Provision set out in subsection 248(35) would apply and the fair market value of the gift for purposes of subsection 248(30) is "deemed" under paragraph 248(38)(a) to be "the lesser of the fair market value of the substantive gift and the cost, or if the substantive gift is capital property of the taxpayer, the adjusted

[157] See *Charity Law Bulletin* No. 21 dated April 30, 2003 *available at* www.charitylaw.ca.

cost base, of the substantive gift to the taxpayer immediately before the disposition" of the substantive gift to the qualified donee. Pursuant to paragraphs 248(38)(b) and (c), the proceeds of sale are deemed to be the lesser of the fair market value and the cost, in the case of eligible capital property, or the adjusted cost base, in the case of capital property, immediately before the sale.

(e) Anti-Avoidance Rule

The December 2003 Amendments also introduced an anti-avoidance rule in the new subsection 248(37) of the *ITA* which states that if "one of the reasons for a series of transactions" that includes a disposition or acquisition of property of a donor is to increase the amount that would be deemed to be the fair market value of the gift under subsection 248(35), then the cost of the property for the purpose of subsection 248(35) shall be deemed to be the lowest cost to the donor to acquire the property in question or "an identical property at any time." This subsection applies to gifts made on or after 6 p.m. on December 5, 2003

(f) Practical Implication of Recent Amendments

The application of the proposed Deeming Provision to gifts made outside of tax shelter donation arrangements under paragraph 248(35)(b)(i) of the *ITA*, if the February 2004 Amendments which incorporated changes introduced by the December 2003 Amendments, are passed will have serious practical implications on how charities will need to operate in terms of acceptance of gifts and the issuance of charitable donation receipts.

Firstly, charities will be required to inquire of donors of gifts-in-kind when the property donated was acquired by the donors. Where possible, a written confirmation will need to be obtained from the donors in this regard to evidence the date of acquisition. Where property was acquired by the donors less than three years before the date of donation, the charitable donation receipt will need to reflect the deemed fair market value of the property, being the lesser of the appraised fair market value and the cost of acquisition by the donor. Where property was acquired by the donors more than three years before the date of the donation, then the charitable donation receipt will need to reflect the appraised fair market value of the property.

Secondly, where the Deeming Provision applies, then the charity will need to inquire of the donor to determine the amount of the adjusted cost base of the gifted property, where applicable. From a practical standpoint, this would be a difficult if not impossible task for many charities to undertake, particularly smaller charities.

Thirdly, although the burden is on the donors to prove the lack of intention to make a gift when the property was acquired, it raises a concern whether charities will be required to inquire of donors of gifts-in-kind to determine whether the donor had the intention to make a gift at the time when the donor acquired the property, regardless of when the property was acquired. On the one hand, without charities making the necessary inquiries, it is unclear what value should be reflected in the charitable donation receipt that the charities are required to issue to the donor. On the other hand, since charities are obviously grateful to receive donations, it will be difficult for charities to make such inquiries of its donors regarding whether they had any intention to make a gift when the property was acquired.

Fourthly, there is the possibility that the Deeming Provision could lead to unintended negative results, such as catching the donation of privately held shares where the donor exchanged the original shares for shares of another class for the purpose of donating them to a charity. As such, hopefully the wording of the Deeming Provision will be amended before being passed into law to address the unintended results.

13. UTILIZING TEN YEAR GIFTS IN CHARITABLE FUND RAISING[158]

Although it is beyond the scope of this article to provide a detailed or thorough discussion of the tax considerations involving donor-restricted charitable gifts, it is important to note some of the more important income tax considerations affecting donor-restricted charitable gifts. What follows is intended to be a brief overview of selected tax considerations in this regard.

A. Documenting Ten Year Gifts

As indicated earlier, the purpose of a 10-year gift is to provide an exemption from the 80 per cent disbursement quota under the *ITA* for gifts to a registered charity that are held for a period of at least ten years. To determine what constitutes a 10- year gift and what is required to properly document it, it is necessary to review carefully the definition of a ten year gift under the *ITA*. For ease of reference, the relevant provisions of ss.149.1(1) of the *ITA* is set out below:

> "disbursement quota" for a taxation year of a charitable foundation [also charitable organization] means the amount [which is] 80% of the total of all amounts each of which is the amount of gift for which the foundation [charitable organization] issued a receipt described in subsection 110.1(2) or 118.1(2) in its immediately preceding taxation year, <u>other than</u>;
>
> ...
>
> (b) <u>a gift received subject to a trust or direction to the effect that property given, or property substituted therefor, is to be held by the foundation for a period of not less than ten years</u>... [emphasis added]

The reference to ss.110.1(2) and 118.1(2) above means that the ability to accept a 10-year gift only applies to gifts where a receipt issued by the charity to either an individual or a corporation. The ten year gift exception would not exempt a gift made from one charity to another charity. Such exemption, however, would be available by designating the gift as a "specified gift" under ss.149.1(1) of the *ITA*.

The key elements of a ten year gift under the *ITA* require that there must be a gift that is;

[158] *Supra* note 23 for more details.

(i) received subject to a trust or direction; and

(ii) held for a period of not less than 10 years.

The fact that a 10-year gift can include a donor-directed gift as well as a donor-restricted charitable trust means that many restricted gifts that do not meet the requirements to create a special purpose charitable trust may still constitute ten year gifts where the requirements to document a ten year gift under the *ITA* have been met.

The documentation required as evidence of a 10-year gift must include the following:

- the document must be executed by the donor for each gift that is made;
- the document must clearly identify the donee charity, including its official name and registration number;
- the document must indicate the amount of the gift;
- the document must set out the date the gift is made;
- the document must set out the name and address of the donor; and
- the document must set out the serial number of the official receipt issued to the donor for the gift.[159]

The document should then be attached to the charity's duplicate copy of the receipt and retained with its other books and records.

The requirement that the ten year gift must be by a trust or direction that is "executed by the donor" poses a practical problem where there is a public fund-raising event, such as a dinner or auction where the net proceeds from the event are added to the endowment fund or other type of 10- year gift. It is not realistic to expect that each person attending the dinner would be prepared to sign a direction or declaration of trust. However, possibly the promotion materials for the event could set out the terms required to establish a ten year gift under the *ITA* along with a reply card to buy

[159] Information Circular 80-10R "Registered Charities: Operating a Registered Charity," which discussed the receipting requirements for ten year gifts, has been cancelled and replaced by RC 4108 - "Registered Charities and the *Income Tax Act*." Page 7 of RC 4108 sets out the receipting requirements for all donations, including ten-year gifts.

tickets that includes a statement that the completion and signing of the reply card is deemed to be the execution of a 10-year gift document. Since this is the author's suggestion only, it would be prudent to first obtain the approval of CRA before adopting this practice.

B. Expenditure of Income

A primary factor to remember when dealing with the expenditure of income from ten year gifts is that the 4.5 per cent disbursement quota imposed on private and public foundations each year also applies to a 10-year gift. In this regard, unless the foundation has other monies that it can expend to meet the 4.5 per cent disbursement quota calculated on 10- year gifts that it holds, it is essential that the document creating the ten year gift permit the expenditure of income earned on the 10-year gift during the 10 years and that the income earned each year is at least 4.5 per cent of the original amount of the gift and any resulting capital gains.

In a situation where there was insufficient income earned to meet the 4.5 per cent quota, the definition of a ten year gift under ss.149.1(1) would not permit a partial disbursement of any of the capital to meet the 4.5 per cent disbursement quota. The capital must remain intact, even if the 4.5 per cent disbursement quota cannot be met. In a situation where insufficient income is earned on a ten year gift, a foundation would be put in the impossible situation of either being unable to meet the 4.5 per cent disbursement quota, or if it did try to meet it by disbursing a portion of the original gift or any resulting capital gains, then such disbursement would prove to be futile, since the amount of the gift or any resulting capital gain expended would be added onto the disbursement quota for the charity for that year. This result is further discussed below.

As a result, before a foundation accepts a 10-year gift, it is essential for the board of directors of the foundation to be satisfied that a 4.5 per cent income return on the 10-year gift or overall investment portfolio of the foundation is achievable. If this is not the case, or if the board of the foundation is expecting to be able to expend a portion of the capital of the 10-year gift to meet the 4.5 per cent disbursement quota, then it should not agree to accept a 10-year gift, notwithstanding that the terms of the 10-year gift may contemplate that a portion of the gift or resulting capital gain can be expended to meet the 4.5 per cent disbursement quota. The only alternative would be to apply, under sub-section 149.1(5) of the *ITA*, to have the 4.5 per cent disbursement quota reduced in a particular taxation year in order to advance expenditure of the capital of the 10-year gift.

However, there still remains the question whether the document creating the 10- year gift can authorize the expenditure of any resulting capital gain from the gift by defining "income" earned on the 10-year gift that can be expended to include resulting capital gains. In this regard, Carl Juneau, Director of Policy and Communications for the Charities' Directorate of CRA, has stated that capital gains earned from a gift will be considered to be a portion of the "*property given, or property substituted therefor*" under ss.149.1(1) of the *ITA* and that therefore, no capital gain earned on the 10-year gift can be disbursed during these 10- years. This position was set out in a letter from Carl Juneau addressed to the author dated September 21, 2000, an excerpt of which is set out below:

> ...Our view is that gains accrued to a property subject to a ten-year trust, or property substituted therefor, cannot be distributed without removing the original gift from the exemption to the disbursement quota. If a charitable foundation were to attempt such a distribution, it would appear to be contravening the terms of the trust or direction, as well as the Income Tax Act.
>
> Gifts subject to a trust or direction that they be held for a period of not less than ten years, or property substituted for them, are excluded from the 80% disbursement quota requirement. As you know, charitable foundations typically use such endowments as vehicles for the cumulation of capital to support their long-term charitable activities. Although the terms of a trust may theoretically provide for the exclusion of gain from the ten-year holding period, our view is that in most cases, any gain realized from the original property would be subject to the same ten-year holding period under the statute. Were the foundation to somehow extract and distribute gains realized from the property, it would be contravening the Act by distributing a portion of the property gift.
>
> It is possible for the terms of a trust or direction to permit donated property to be substituted; in other words, to give discretion to the trustees to change the form of the property such that the trust need only hold property possessing value equivalent to the original gift. However, it does not appear that realized gains could be severed from donated property for distribution in this matter because case law would suggest that a "substitute property" is the total proceeds of disposition of the property for which it is substituted. In other words, notwithstanding the terms of the trust or direction, a distribution of any portion of the proceeds realized on the substitution of a

> donated property is, for tax purposes, equivalent to a partial distribution of the gift.[160]

As a result, it is important for charities that currently have 10- year gift documentation which permits the disbursement of resulting capital gains, not to exercise that option. Otherwise, the charity would be in violation of the definition of a 10-year gift under ss.149.1(1) of the *ITA*.

C. Consequences of Expending Capital Prior to the Expiry of Ten Years

In the event that the capital of a ten year gift, i.e., "*property given, or property substituted therefor*" under ss.149.1(1) of the *ITA,* including any resulting capital gains (referred to as "capital"), is expended within the mandatory ten year minimum period, there are certain consequences that would result:

- Since the trust or donor direction creating the ten year gift would require that the capital be held for at least 10 years, then the expenditure of any portion of the capital would constitute a breach of trust where the 10-year gift was created by a trust, or would be a violation of a direction if the gift was created by a donor direction, although CRA does not see a distinction and instead considers any disbursement prior to 10 years with the consent of the donor to be a breach of trust.[161] With regards to the latter, s. 4(d) of the *CAA* would allow the Public Guardian and Trustee of Ontario to seek a court order to force the charity and its directors to comply with the donor's direction.

- The portion of the capital expended prior to 10 years would be added to the disbursement quota of the charity for the year in which the capital was expended in accordance with the definition of the "disbursement quota" under ss.149.1(1) of the *ITA*. This, in effect, would mean that the amount of the capital expended would be added to, and disbursed as part of the disbursement quota in the same year, resulting in a neutral impact upon the disbursement quota of the charity for that year. However, as indicated above, this would not assist in meeting a shortfall in the 4.5 per cent disbursement quota for a 10-year gift of a foundation.

- The more difficult question is whether the full amount of the 10-year gift collapses where only a portion of the capital is expended in any one year. This would not appear to

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[160] Letter of Carl Juneau, Director of Policy and Communications Division Charities' Directorate, Canada Custom and Revenue Agency to Terrence Carter (21 September, 2000).

[161] Canada Revenue Agency, Advance Income Tax Ruling "Disbursement Quote – 10 Year Directions", (11 December 2003).

be the case in accordance with the wording of ss.149.1(1), in that the amount that is added to the disbursement quota is based upon the actual amount that is expended in a particular year. As such, if only 10 percent of a 10-year gift were disbursed in a year prior to the expiry of the 10- years, it would appear that only the ten percent actually expended would be added to the disbursement quota, as opposed to including the full amount of the original 10-year gift.

- Based upon the above, some charities have considered gradually disbursing a 10- year gift over a number of years assuming that in doing so there would be no negative impact on its disbursement quota each year. However, a gradual disbursement of a 10-year gift might be seen by CRA as an intentional misuse of the 10-year gift. This in turn might result in either deregistration of the charity or, alternatively, disallowance of the 10-year gift in the original year in which it was claimed for the full amount of the gift that had been exempted. This is an issue that needs to be canvassed further with CRA.

D. Expenditure of Ten Year Gifts After Expiry of Ten Years

The 10 year gift exemption requires only that the trust or direction creating the 10-year gift specify that the capital is to be held for a period of "*not less than ten years*." This means that a gift which is subject to a trust or direction that it be held for a longer period of time, including a trust or direction that the capital be held in perpetuity as an endowment, would also qualify as a 10-year gift.
It would therefore be open for a donor to create a 10 year gift to specify the donor's directions concerning the expenditure of the gift after the minimum 10 year period. Silence by the donor or his or her legal counsel to articulate the donor's directions in this regard would mean that the charity would be at liberty to use the 10 year gift or income in any manner that the charity wanted to, in accordance with its charitable objects once the 10 years had expired, even if that were not the intention of the donor.

On the other hand, just because a gift is categorized as a 10-year gift in the charity's T3010 Annual Charity Information Return does not necessarily mean that the capital of the 10-year gift can be expended after 10-years. That issue is determined by the wording of the document creating the 10-year gift. As such, it is important for a charity and its board of directors to ensure that the wording creating a ten year gift is carefully reviewed to determine if there are any restrictions that continue after the expiry of the 10 year minimum period, such as a restriction that the capital be held as an endowment fund in perpetuity.

E. Transfer of 10-Year Gifts

It would be reasonable to assume that the transfer of a 10-year gift from one registered charity to another registered charity should have a neutral impact upon the disbursement quota of both charities. However, as a result of what appears to be a drafting error in the wording of paragraph A.1 of subsection 149.1(1) of the *ITA* in failing to accommodate the designation of a 10-year gift as a specified gift, the transfer of a 10-year gift from a registered charity to a foundation will result in either the 10-year gift being included in the disbursement quota of the transferee foundation, or alternatively, being included in the disbursement quota of the transferor charity with no offsetting disbursement being available to match the increase in the disbursement quota of the transferor charity. Normally, in order for a transferee foundation to exclude the receipt of a 10-year gift from the calculation of its disbursement quota, the transferor charity would need to designate the gift as a specified gift pursuant to subsection 149.1(1) of the *ITA*. (Specified gifts are gifts given from one charity to another charity that are designated as such in the transferor charity's information return for the year in which the gift is made so that the disbursement quota of the transferee charity is not increased and, similarly, the transfer does not count in meeting the disbursement quota of the transferor charity.)

However, because of the wording of paragraph A.1 of subsection 149.1(1) of the *ITA* that defines what a disbursement quota is, the transferor charity cannot record the 10-year gift as a specified gift, since to do so would preclude the transferor charity recording the 10-year gift as a disbursement to offset the inclusion of the transfer of the 10-year fit in the disbursement quota of the transferor charity. What subparagraph (a) of paragraph A.1 of subsection 149.1(1) should have stated is that the inclusion of a 10-year gift in the disbursement quota of the transferor charity specifically excludes a 10-year gift when designated as a specified gift.

As a result of this drafting error (which, it is to be hoped, will be corrected soon), a charity that is intending to transfer a 10-year gift to a foundation will need to either apply for a reduction in its disbursement quota in accordance with subsection 149.1(5) of the *ITA* by the amount of the 10-year gift being transferred and designate the gift as a specified gift in order to avoid the gift being included in the disbursement quota of the transferee foundation or, alternatively, the transferor charity would need to elect not to designate the 10-year fit being transferred as a specified gift but, instead, have the transferee charity apply for a reduction in its disbursement quota pursuant to subsection 149.1(5) of the *ITA* for the amount of the 10-year fit. Either of these alternatives is unnecessarily awkward, but until the *ITA* is amended to correct the apparent drafting error, the alternatives described above appear to be the only practical avenues open to a charity in order to effect a transfer of a 10-year gift in favour of a foundation.

F. Managing 10-Year Gifts

Although many charities customarily co-mingle their various restricted funds in one single account for investment purposes, and even though such practice may be permitted under pending regulations expected under the *Charities Accounting Act*, it would be prudent for a charity to maintain each 10-year gift in a separate account. Although administratively awkward, this approach would avoid potential problems with ten year gifts, including the following:

- Since the capital (as defined earlier) of a 10-year gift cannot be expended for a minimum of 10 years, and since CRA takes the position that any capital gains accruing on the original gift or "*property substituted therefor*" are part of the original property that must be held for 10 years, it is essential that the charity be able to clearly identify what the original property of the 10 year gift was, what property was substituted for it, and what capital gains have accrued on the said property. This can be best facilitated by tracking each 10-year gift in a separate account.

- Maintaining a separate account for each 10-year gift would help to ensure that the expenditure of capital during the mandatory minimum ten year period did not occur in an attempt to meet the 4.5% disbursement quota required for foundations.

- Since each ten year gift may be subject to different terms and conditions imposed by the donor, i.e., the length of time that the gift is to be held or what investment powers are to apply, the utilization of separate accounts for each 10-year gift would help track when the capital can be expended in accordance with the specific terms of the trust or donor direction and what type of investments the said capital can be put into without breaching the investment powers provided for in the document creating the 10- year gift that may be different from the investment powers of the charity itself.

14. CONDITIONAL GIFTS

A. What is the Nature of a Conditional Gift?

The distinction between a conditional gift and a special purpose charitable trust is not easy to identify, particularly since a conditional gift can also be a special purpose charitable trust. Part of the distinction relates to the ownership of the gift and the other part relates to the wording accompanying the gift.

A conditional gift involves the charity becoming the beneficial owner of the gift, either after the condition has been fulfilled or until a condition subsequent fails or occurs, as the case may be. With a special purpose charitable trust, on the other hand, the charity never becomes the beneficial owner of the gift. Instead, the charity holds title to the gift in trust, subject to certain terms and restrictions. It is possible for a conditional gift to also be a special purpose charitable trust if the gift involves both a condition and a donor requirement that the gift be used for a particular purpose. For example, the donor says “I give one million dollars as a perpetual endowment for cancer research, on the condition that the charity opens a cancer research facility in Calgary by the year 2000.”

With a conditional gift, the operative wording involves a transfer of beneficial ownership of the gift, subject to an independent clause of defeasance commencing with words such as “but if,” “provided that,” or “on condition that.” It is not sufficient, however, to look only at a particular phrase or word to determine if a gift is conditional; it is important to look at the whole wording of the document by which the gift is given.[162]

[162] See Picarda, *supra* note 67 at p. 202.

B. Receipting Conditional Gifts

The transfer of title of a gift subject to a condition precedent does not occur until after the condition precedent is met. As such, the charity cannot issue a tax receipt until after the condition precedent is fulfilled and the transfer of the gift is complete.

What is more problematic is when a gift is subject to a condition subsequent. If a charity has issued a tax receipt for a gift subject to a condition subsequent and there is a subsequent reversion of the gift back to the donor, it would be important for the charity to advise CRA so that it can ensure that the donor reported as income the amount of the receipted gift in the year in which the reversion of the gift to the donor occurred.

CRA may go further and take the position that a gift subject to a condition subsequent which includes a reversion of the gift back to the donor does not entitle the charity to issue a tax receipt in the first place because there was never an absolute transfer of title of the gift to the charity. As such, where a charity is presented with a gift subject to a condition subsequent, it would be important to obtain an opinion from CRA to determine whether or not a charitable receipt could be issued for the gift in the circumstances. It may be that if the wording of the condition subsequent results in the gift becoming vested in another charity, CRA may view it as a valid gift at law since no portion of the gift could revert back to the donor. However, because of the uncertainty on this issue, it would be prudent to first obtain an opinion from CRA before the charity issued a tax receipt to the donor involving any type of gift involving a condition subsequent.

15. CONCLUSION

Given the number and complexities of the legal issues involved in charitable fundraising, it is likely that lawyers will increasingly become involved in advising charities on liability issues in fundraising and how to avoid such risks in the future. However, the broad range of advice that charities will require necessitates that lawyers become familiar with the various statutes, regulations and case law that impact upon a charity's ability to operate various fundraising programs. The need for legal advice in this area is considerable and is likely to expand in the future as fundraising programs become more complicated and corresponding legislation and regulations increase in number.

In this regard, it is hoped that this paper will have provided a practical overview to lawyers, fundraisers and senior management of charities, who wish to become better informed in this area of the law, as well as providing a helpful reference source to conduct further research as may be necessary in providing legal advice and service in this expanding and challenging area of the law.

16. APPENDIXES AND SELECTED BIBLIOGRAPHY

A. List of Appendixes

Appendix 1 - *The Ethical Fundraising & Financial Accountability Code* by the Canadian Centre for Philanthropy

Appendix 2 - *A Donor's Bill of Rights* by the American Association of Fund Raising Counsel, Association for Health Care Philanthropy, Council for Advancement and Support of Education and Association of Fundraising Professionals.

Appendix 3 - *Code of Ethical Principles and Standards of Professional Practice* by the Association of Fundraising Professionals.

Appendix 4 - "'New Era' Scandal in U.S. Has Lessons for Canadian Charities", *Church & the Law Update*, Volume 1, Number 6, June 14, 1995.

Appendix 5 - "Impact of the *Personal Information Protection and Electronic Documents Act* (PIPEDA) on Charitable and Non-Profit Organizations", *Charity Law Bulletin No. 28,* by Mark J. Wong, assisted by U. Shen Goh and Suzanne E. White, November 29, 2003.

Appendix 6 - *Letter from Superintendent of Financial Institutions on Self-Insured Annuities*, British Columbia, November 5, 1999

Appendix 7 - Summary entitled "*Checklist and Reference Guide: Avoiding Wasting Assets II – Trade-mark and Domain Name Protection for Charities*" by Terrance S. Carter, April 14, 2004.

Appendix 8 - *Summary of Changes to the CRA Website from 2002 – 2004* by Terrance S. Carter and Suzanne E. White, March 2004.

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