
Ontario Bar Association
A DANGER TO DABBLE:
CHARITY LAW HOTSPOTS

Toronto, Ontario – October 26, 2005

ADVISING THE CHARITABLE CLIENT:
RISK MANAGEMENT STRATEGIES

By Terrance S. Carter, B.A., LL.B.
© 2005 Carter & Associates

CARTERS[™].ca

CARTER & ASSOCIATES
PROFESSIONAL CORPORATION

BARRISTERS, SOLICITORS & TRADE-MARK AGENTS
Affiliated with **Fasken Martineau DuMoulin LLP**

Offices / Bureaux
Orangeville (519) 942-0001
Ottawa (613) 212-2213
Toll Free / San frais:
1-877-942-0001

www.carters.ca[™]

Locations by Appointment /
Bureaux par rendez-vous
Toronto (416) 675-3766
London (519) 937-2333
Vancouver (877) 942-0001

www.charitylaw.ca[™]

ADVISING THE CHARITABLE CLIENT: RISK MANAGEMENT STRATEGIES

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

TABLE OF CONTENTS

A. INTRODUCTION.....	1
B. THE FUNDAMENTALS OF A CHARITY	4
C. THE FUNDAMENTALS OF A NONPROFIT ORGANIZATION.....	5
D. ADVISING DIRECTORS ABOUT THEIR LIABILITY RISKS: THE CHALLENGE IN ADVISING THE CHARITABLE CLIENT	5
1. The Nature of the Charitable Client	5
2. Unrealistic Expectations of the Lawyer by the Charitable Client	7
3. Why the Charitable Client Often Experiences Difficulties.....	8
4. Consequences of Legal Deficiencies in Charitable Structure and Operations	10
5. How the Lawyer can Encounter Difficulties in Advising the Charitable Client.....	12
6. Conflicts of Interest in Advising the Charitable Client.....	14
E. MINIMIZING PERSONAL EXPOSURE TO RISK	16
F. STRATEGIES TO ADDRESS THOSE RISKS.....	17
G. DEVELOPING A LEGAL RISK MANAGEMENT CHECKLIST.....	20
1. Sample Checklist	20
2. How to Utilize a Checklist	21
3. The Structure of the Legal Risk Management Checklist for Charities	22
H. EFFECTIVELY COMMUNICATING WITH THE CHARITABLE CLIENT	23
1. Confirming Retainer.....	23
2. Educational Reports.....	23
3. Documenting Advice Given	24
I. CONCLUSION.....	25
J. Authorities.....	26

Ontario Bar Association
A DANGER TO DABBLE: CHARITY LAW HOTSPOTS

Toronto, Ontario – October 26, 2005

**ADVISING THE CHARITABLE CLIENT:
RISK MANAGEMENT STRATEGIES***

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

A. INTRODUCTION

To collectively describe charities in Canada as “big business” may be perceived by some to be an oxymoron, to others it is a self-evident truth. In 2004, Statistics Canada released its highly anticipated national survey of nonprofit and voluntary organizations in Canada, entitled “Cornerstones of the Community,” which reported that in 2003 there were over 161,000 incorporated nonprofit and voluntary organizations and registered charities¹ in Canada, collectively drawing on two billion volunteer hours, the equivalent of one million full-

* This article has been updated from a paper presented as part of the Law Society of Upper Canada Special Lecture Series, 1996 Estates: Planning, Administration and Litigation (November 1996).

** Terrance S. Carter practices with Carter & Associates Professional Corporation and is counsel to Fasken Martineau DuMoulin LLP on charitable matters, is a member of the Charities Advisory Committee and Technical Issues Committee for Canada Revenue Agency, and a frequent speaker and author in the area of charity, church and not-for-profit law.

¹ It is important at the outset to understand the differences between a charitable organization and a nonprofit (not-for-profit) organization. The *Registered Charities Newsletter*, No. 19 (June 2004) at 7, available at <http://www.cra-arc.gc.ca/E/pub/tg/charitiesnews-19/charitiesnews19-e.pdf>, sets out the differences between the two types of organizations in the following terms:

The *Income Tax Act* [infra note 4] distinguishes non-profit organizations (NPOs) from registered charities. While both classes of organizations are all or partially tax-exempt, registered charities have the additional privilege of issuing official donation receipts to their donors. On the other hand, registered charities are publicly accountable through the CRA, and have to meet more stringent operational requirements.

Whether an organization is a registered charity or an NPO depends on its purposes and activities. Charities have a particular set of purposes—such as the relief of poverty, the advancement of education or religion, or other purposes that benefit the community—that the courts have recognized as charitable.

Under paragraph 149(1)(l) of the *Income Tax Act*, a non-profit organization is defined as “a club, society or association that ... was organized and operated exclusively for social welfare, civic improvement, pleasure or recreation or for any other purpose except profit, no part of the income of which was payable to, or was otherwise available for the personal benefit of, any proprietor, member or shareholder thereof unless the proprietor, member or shareholder was a club, society or association the primary purpose and function of which was the promotion of amateur athletics in Canada.”

Whether the organization is designated as charitable or nonprofit will dictate the filing requirements, the activities in which the organization can engage, and the manner in which the funds are disbursed.

time jobs, generating \$8 billion in individual donations and \$112 billion in total revenues.² Canada Revenue Agency (“CRA”), meanwhile, reports that there are currently over 80,000 charitable organizations³ registered under the *Income Tax Act*.⁴ While one third of the \$112 billion reported revenue is concentrated in the hands of a small percentage of charities made up of hospitals and educational institutions, the remaining vast array of charities are responsible for the remaining two thirds of all reported income for charities in Canada.⁵ Charities have clearly become a major component of the economic engine of Canada as the “third sector”⁶ of voluntarism after the governmental public sector and the business private sector.

However, with the exception of a limited number of lawyers who regularly provide specialized advice involving charities and donations, the vast majority of lawyers who are called upon to advise charitable clients do so on an infrequent basis and either treat charitable clients as step-children compared to their “real” clients, or perceive the professional service that they render to be akin to an act of charity itself, either because the service is given *pro bono* or because acting on behalf of a charity provides a sense of satisfaction in the hope that the advice provided has furthered charitable purposes that are of general benefit to the community. While such motivation is laudable, lawyers should not lose sight of the fact that the services they provide, whether it be done on a *pro bono* basis or at a reduced rate, must be done in a competent and professional manner.

Meeting this requirement, though, is becoming increasingly difficult to achieve. Lawyers called upon to advise charities are expected to have an understanding of numerous and diverse areas of the law, including corporations, charitable trusts, associations, taxation, contracts, real estate, leasing, employment, insurance, risk management, intellectual property and trust accounting, to name only some of the major areas. Coupled with increasing complexities involved in running charities is a heightened level of expectation placed upon leaders of charitable organizations by the courts, the government and the public at large. When individuals who are faced with the responsibility of establishing and operating a charity seek legal advice, it is incumbent upon the lawyer to not only provide answers to the specific question asked, but to also take the initiative to

² Michael H. Hall, Margaret L. de Wit, David Lasby and David McIver, *Cornerstones of the Community: Highlights of the National Survey of Nonprofit and Voluntary Organizations* (Ottawa: Statistics Canada, 2004) at 7-10 [Cornerstones Survey].

³ Canada Revenue Agency, *Online List of Canadian registered charities* (as of 14 October 2005), available at http://www.cra-arc.gc.ca/tax/charities/online_listings/canreg_interim-e.html.

⁴ R.S.C. 1985, c. 1 (5th Supp.) [ITA].

⁵ Cornerstones Survey, *supra* note 1 at 10.

⁶ Theodore Levitt, *The Third Sector: New Tactics For a Responsive Society* (New York, 1973).

ensure that the charitable client is aware of the duties and responsibilities that charities are now facing, as well as knowing what steps can be taken to avoid liability exposure before problems occur.

With the increasing specialization of the practice of law dealing with charities, the provision of legal services in a lack lustre manner based upon the assumption that charitable clients require less effort than full paying clients is no longer an option. Charitable clients not only require competent and complete advice, they also require legal counsel that will take the initiative in guiding them through the intricacies and complexities of the law now inherent in operating a charity in Canada.

Advising the charitable client therefore extends beyond simply “doing good” by assisting individuals who wish to benefit the community. Instead, it requires the provision of professional advice on complicated areas of the law, rendered in a manner that reflects an increasing reliance by clients on counsel to identify legal risks and provide recommendations on how those risks can be avoided. To that end, this paper suggests a more active professional mindset is required to deal with charities, and lawyers should assist charities in identifying areas of risk by utilizing tools such as a charity legal risk management checklist, a sample of which is attached to this paper as an appendix. The paper also explains a number of problems that lawyers may encounter from time to time in advising charities. The paper concludes by emphasizing the importance of communicating with the charitable client and providing informational reports to both assist the client and establish clear evidence of the advice rendered by the lawyer. Accordingly, this paper is not a technical discussion of legal issues, but instead attempts to provide a practical guide for practitioners who wish to develop a proactive approach in advising charitable clients.

With the escalating cutback in social program funding by all levels of government, and the corresponding pressure upon charities to fill the void, the number of charities and the services that they provide will continue to increase, creating a greater demand for competent legal advice. The charitable sector is clearly going through fundamental changes in its evolution into a major presence in the Canadian economy. At the same time, the legal services that lawyers are now called upon to provide to charitable clients is also going through fundamental changes, from that of benign passivity to proactive legal risk management advice.

B. THE FUNDAMENTALS OF A CHARITY

At law, a charity has a specific meaning that often eludes the popular conception. For an organization to be considered charitable at law, its objects or purposes must be undertaken to achieve a charitable purpose. Presently, only four categories or heads of charity are recognized by the courts. In his decision in the case *Special Commissioners of Income Tax v. Pemsel*,⁷ Lord MacNaghten identified four heads of charity: relief of poverty, advancement of education, advancement of religion, and other purposes beneficial to the community not falling under any of the preceding heads. This definition is mirrored in Ontario's *Charities Accounting Act*,⁸ and although the ITA does not make specific reference to these categories, both the Charities Directorate of CRA and the courts rely on the same categories in regulating the sector. The Supreme Court of Canada, in *Vancouver Society of Immigrant and Visible Minority Women v. M.N.R.*,⁹ clarified the Canadian approach to recognizing charities, noting that while the ITA focuses on the character of the activity undertaken by the organization, linking them to the categories established in *Pemsel*, the focus should be on the purpose in furtherance of which an activity is carried out in order to determine whether charitable status should be granted.

Whether an organization operates as a charitable trust, an unincorporated association or a non-share capital corporation, there are clear tax advantages to obtaining charitable status, the primary one being that a charity does not pay tax on income or capital gain. The ability to issue charitable receipts to donors as tax credits for income tax purposes is a significant benefit for those organizations that must rely on individual donations for funding purposes. Recent proposals to amend the ITA include provision to enable a gift for income tax purposes to include consideration to the donor.¹⁰

⁷ [1891] A.C. 531 (H.L.) [*Pemsel*].

⁸ R.S.O. 1990, c. C-10 [CAA].

⁹ [1999] 1 S.C.R. 10 [*Vancouver Society*].

¹⁰ See e.g. Theresa L.M. Man, "July 18, 2005 Draft Amendments to the *Income Tax Act* Affecting Charities: Part I – Definition of Gift & Split-Receipting" in *Charity Law Bulletin No. 76* (8 September 2005), available at www.charitylaw.ca; Theresa L.M. Man and Terrance S. Carter, "February 27, 2004, Revised Draft Amendments to the *Income Tax Act* Affecting Charities" in *Charity Law Bulletin No. 40* (29 March 2004), available at www.charitylaw.ca; and, Theresa L.M. Man and Terrance S. Carter, "Commentary on Draft Technical Amendments to the *Income Tax Act* Released on December 20, 2002 That Affect Charities" in *Charity Law Bulletin No. 21* (30 April 2003), available at www.charitylaw.ca, which discuss amendments to the common law definition of gift, enabling a donor to have a tax benefit under the Act even though the donor (or a person not dealing at arm's length with the donor) received a benefit, provided the value of the property exceeds the benefit received by the donor.

C. THE FUNDAMENTALS OF A NONPROFIT ORGANIZATION

Under the ITA, a nonprofit organization is defined as a

... club, society or association that ... was not a charity ... and that was organized and operated exclusively for social welfare, civic improvement, pleasure or recreation or for any other purpose except profit, no part of the income of which was payable to, or was otherwise available for the personal benefit of, any proprietor, member or shareholder ...¹¹

Although a nonprofit organization, like a charity, has tax exempt status and does not pay tax on income or capital gains, except income from property of an organization whose main purpose is to provide dining, recreation or sporting facilities, the nonprofit organization is not able to issue charitable receipts for income tax purposes. However, it is not required to disburse a specified percentage of its earnings. There are two legal forms available for nonprofit organizations: an unincorporated association and a non-share capital corporation.

D. ADVISING DIRECTORS ABOUT THEIR LIABILITY RISKS: THE CHALLENGE IN ADVISING THE CHARITABLE CLIENT

1. The Nature of the Charitable Client

The challenge in advising the charitable client is a direct result of the unusual nature of a charity that makes it different from advising any other type of client. For instance:

(a) Whereas most clients are motivated by self-interest, those involved in directing a charity are generally motivated by the sense of a greater good that extends beyond themselves. However, due to this increased expectation of good will, the sensitivities of those involved with charities are heightened and are often subject to greater disappointment and misunderstandings than is the case in a business context.

(b) Whereas there is usually continuity in acting as legal counsel for a business or for an individual, due to the frequent changeover in board members involved with charities, there is often an inherent lack of continuity when acting for a charity. As a result, individuals on the board for whom the lawyer provided advice in one year may be different the next year.

¹¹ ITA, *supra* note 4, s. 149(1)(l).

(c) Whereas a business client will generally evidence a reasonable level of commitment to complete a required task, the extent of a volunteer's commitment can range from a superhuman effort that far surpasses anything found in a profit-making business, to those who perceive their involvement as only a position of honour with a corresponding limited sense of commitment to the task at hand.

(d) Whereas a business client by necessity will normally have a well established structure on which the business is based, the nature of voluntarism for those involved with the board of a charity will often mean that there will be a significant difference of opinions concerning how to formally structure the charitable organization or how to implement the structure on a day-to-day basis.

(e) Whereas a business client understands the importance of process to achieve an end result, individuals on the board of a charity will often focus on the charitable purpose that they wish to achieve and feel thwarted by the process required to achieve that goal, particularly when the process involves what is assumed to be bureaucratic and legalistic exigencies.

(f) Whereas the business client is generally not surprised to find there are legal niceties that must be complied with in running a business, the charitable client is often surprised and frustrated to find they must comply not only with normal legal hurdles associated with regular operations, such as compliance with employment standards legislation, but are also subject to often onerous and complicated legal expectations imposed upon charities and their boards under the ITA, as well as trust law that applies to charitable property. The lack of understanding of legal requirements is generally so pervasive with charitable organizations that it is often necessary to assume that the charitable client knows little, if anything, about the legalities that are involved in operating a charitable organization.

(g) With increased cutbacks in government funding to community charities, board members and officers of charities are, by necessity, having to concentrate more on the means of raising the necessary monies to maintain the charitable programs, often at the expense of ensuring the quality of the program or even compliance with basic legal requirements. In addition, there may be a corresponding proliferation of charitable organizations to fill the vacuum once occupied by government funded charitable organizations. Those involved in starting newly created charities, though, will frequently

focus almost exclusively on the current needs that must be met at the expense of putting the necessary charitable structure in place and ensuring applicable rules and laws are complied with.

(h) Of all of the tens of thousands of the individuals who serve as unpaid directors and officers of charitable organizations, it has been correctly stated that “it is unlikely that more than a small fraction of these individuals have any clear ideas of the risks that they are incurring by accepting such positions.”¹²

2. Unrealistic Expectations of the Lawyer by the Charitable Client

In addition to having to deal with the unique character of the charitable client, the lawyer who is called upon to advise charities will generally encounter at least a few of the following unrealistic expectations of the charitable client:

(a) Unless the lawyer is dealing with a large institution with a secure source of government funding, the charitable client will often expect, although not necessarily state, that the lawyer will provide the required legal services either on a *pro bono* basis or subject to a significant reduction. While there is a place for *pro bono* services for a charity, before doing so, the lawyer must first determine the nature of the problem, the solutions required, and whether or not he or she is prepared to devote the time and attention required in order to provide the necessary legal services on a *pro bono* basis, or with a significant reduction. If not, it is incumbent upon the lawyer to clearly identify to the client at the outset that the legal services in question are being done on a fee for service basis at whatever rate the lawyer feels is appropriate in the circumstances.

If the lawyer does undertake a task for a charitable client on a *pro bono* or reduced fee basis, the lawyer must understand that the lack of payment does not justify incomplete or tardy service. If anything, the charitable client may require legal advice and/or services that are much more sophisticated than those which are associated with a medium sized business and, in some instances, such services may be needed immediately.

(b) When a charity retains a lawyer, no matter how small the task and whether or not the lawyer is paid for his or her services, a frequent presumption is that the lawyer’s involvement in even a small

¹² William I. Innes, “Liabilities of Directors and Officers of Charitable and Non-Profit Corporations” (1993), 13 E. & T.J. 1 at 2.

matter provides the equivalent of a legal “Good Housekeeping Seal of Approval” on everything the charity does. The presumption often expressed, after the fact, is that since the charity was not advised by legal counsel that a particular situation or course of action might be a problem, it could assume that the current practices of the charity complied with all applicable laws.

(c) Unrealistic expectations of what the lawyer is to do often flows out of the general confusion and lack of knowledge by volunteer board members concerning the operations of a charity. Board members are generally so involved in pursuing programs to achieve charitable purposes that they do not question whether they have either the time or expertise to ensure they are complying with legal requirements. It is generally perceived this is the responsibility of the lawyer, although this assumption may not have been communicated to the lawyer. This presumption is so prevalent that charities who become embroiled in legal problems will often state that they assumed since they had not heard any warnings from the lawyer that “no news was good news.” When a problem does develop, particularly if it involves potential personal liability of volunteer directors, it is often the lawyer who is the first person singled out for blame in not having warned the director of the risks that could have been avoided.

In summary, the expectation of the charitable client toward a lawyer retained to provide legal advice is that it should be provided, as much as possible, on a *pro bono* basis, or at least with a significant discount; it should be accurate and professional; and, it should include appropriate warnings concerning existing or proposed courses of action that may expose the charity and its board to unnecessary legal risks.

3. Why the Charitable Client Often Experiences Difficulties

The public’s perception of charities is that they are generally benign organizations of individuals who are committed to higher ideals for the good of the community, and as such are somehow immune from the complexities and legal niceties that apply to business organizations. This is particularly so with religious organizations that often function on the mistaken assumption that their dedication to spiritual values elevates them above the need to deal with mundane matters of complying with the laws of the land.

As a result, it often comes as a surprise to many individuals, both in the community and those involved in charitable organizations, that charities are not the simple organizations they are generally perceived to be, but in fact are often sophisticated corporate entities having serious legal issues and complexities in operations that far outweigh those faced by many businesses. For instance, most charities will be faced with having to deal with some or all of the following issues:

- compliance with complicated statutory requirements for charities under the ITA;
- increased directors and officers liability at common law and in accordance with a growing multitude of provincial and federal statutes;
- raising and managing large sums of money each year;
- overseeing the supervision of employees;
- facing the possibility of termination of employees and the corresponding potential for wrongful dismissal;
- maintaining the goodwill of volunteers while at the same time reducing the risk of exposure to legal liability for volunteers;
- establishing and maintaining an appropriate organizational structure;
- dealing with a diffuse decision making process reflecting input from both the board of directors and from executive staff members;
- ensuring the correct treatment of charitable gifts, including compliance with donor restrictions;
- minimizing the potential for sexual abuse and molestation of children and other vulnerable individuals who come in contact with the charity;
- compliance with human rights legislation;
- compliance with employment legislation;
- compliance with requirements of the provincial and federal government concerning operations of charities through both the Canada Revenue Agency and the Public Guardian and Trustee of Ontario;
- establishing and maintaining the involvement of the charity in both a national and/or international structure, if applicable;
- ensuring appropriate protection of intellectual property;
- ensuring applicable investment restrictions are complied with; and

- ensuring the charitable activities of the organization constitutes an appropriate means of fulfilling the charitable purposes as set out in the constitution and/or letters patent of the charity.

4. Consequences of Legal Deficiencies in Charitable Structure and Operations

Few individuals who are themselves involved in charities give much consideration, if any, to the consequences that could flow from legal deficiencies in charitable operations. Some of the problems, though, that a charity and its board of directors may face at different times include of the following:

- legal action by aggrieved parties based on negligent supervision of staff and volunteers;
- legal action many years after the fact by individuals who allege that they had been sexually or physically abused;
- personal liability of board members as a result of breach of trust involving charitable funds;
- violations of human rights legislation;
- actions for wrongful dismissal;
- revocation of charitable status;
- loss of corporate status with the corresponding escheat of assets to the Crown;
- control by special interest groups intent upon pursuing a specific agenda;
- splits in membership of community groups or religious organizations;
- court supervised audit of accounts conducted under the CAA; and
- possibility of a public inquiry under the CAA.

For charities that assume exposure to legal liability is more theoretical than real, reference should be made to the provisions of section 6 of the CAA. The reported and unreported decisions under that section illustrate how disgruntled members of a charity or members of the public can cause upset and significant legal costs for the charity and its directors by requesting a public inquiry. The relevant portions of section 6 of the CAA states as follows:

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.*

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

(3) Wherever the judge is of opinion that the public interest can be served by an investigation of the matter complained of, he or she *may make an order directing the Public Guardian and Trustee to make such investigation as the Public Guardian and Trustee considers proper in the circumstances.*

(4) In making an investigation directed under subsection (3), *the Public Guardian and Trustee has and may exercise any of the powers conferred on him or her by this Act and any of the powers of a commission under Part II of the Public Inquiries Act, which Part applies to the investigation as if it were an inquiry under that Act.*

...

(6) As soon as the Public Guardian and Trustee has completed the investigation, he or she shall report in writing thereon to the Attorney General and to the judge who ordered the investigation.

(7) Upon receipt of the report, *the judge may order a passing of the accounts in question, in which case section 23 of the Trustee Act applies, and the judge may make such order as to the costs of the Public Guardian and Trustee thereon as he or she considers proper.* ... [Emphasis added.]

In the 1988 decision of *Stahl v. Ontario Society for the Prevention of Cruelty to Animals*,¹³ the court held that a complainant under Section 6 of the Charities Accounting Act is in the same position as an informant who complains of a breach of the Queen's peace before a Justice of the Peace. As such, it is assumed that a complainant is acting for the public good and is not liable to costs, although the complainant might be liable for damages for a malicious prosecution, although an unlikely event.

The court in *Stahl* stated that a complainant under the CAA need not give notice of his or her complaint to the charity involved. Instead, the matter may be laid before a Judge of the court on an *ex parte* basis. The Judge considering the complaint is to act in the same manner as a Justice of the Peace in considering criminal information that is presented before him. As such, the Judge need consider only whether the public interest can be served by the investigation of the matter complained of and is not called upon to determine the merits of the complaint itself.

The case of *Boldrini v. Hamilton Naturalists' Club*¹⁴ provides clear evidence of how effectively Section 6 of the CAA can be used to attack a charity. In *Boldrini*, the Club turned down the complainant's request that the Club contribute towards the publication of his book about a creek in the Hamilton area. The complainant then sent a series of letters to the Club requesting information about its organization

¹³ (1989), 70 O.R. (2d) 355, 35 E.T.R. 234 (Dist. Ct.) [*Stahl*].

¹⁴ [1995] O.J. No. 3321 (Gen. Div.) [*Boldrini*].

and operations. Although the Club provided a response, the response did not satisfy the complainant. The complainant then commenced an application under Section 6 of the CAA, raising questions about the manner in which monies were raised from the public, and expenses related thereto, which included money raised by a local walk-a-thon and its associated expenses. The complainant also raised an issue concerning monies transferred by the Club to “others.” The court stated that this raised a question as to whether donations were made by the Club to other organizations controlled or directed by Club members and whether or not the transfers were appropriate donations for the Club to make as a charity. In granting the application, the court held that the public interest could be served by an investigation by the Office of the Public Guardian and Trustee.

5. How the Lawyer can Encounter Difficulties in Advising the Charitable Client

The general nature of the problems encountered by lawyers when providing legal advice to a charitable client was succinctly described by Donald J. Bourgeois:

The confusion and underdevelopment of the law ... make[s] it difficult for lawyers to provide legal advice to clients. There are few texts on the subject. The cases often comment on the lack of legal developments in this area and the need to make analogies to other forms of law, including trust and business law. The policies and practices may not be readily available or explicable. The law is not “transparent.”¹⁵

In addition to the general lack of law and commentaries available to help lawyers advise charities, there are increasing expectations expressed by the courts concerning the professional duties of lawyers in dealing with clients in general that have equal application to advising charitable clients. These legal expectations can be summarized as follows:

- (a) A lawyer dealing with a charity must ensure any transaction with which the charity is involved has been fully explained to the client, particularly unsophisticated members of the board;
- (b) A lawyer advising a charity has a duty to warn the charity of any risks involved in the course of action contemplated by the client. In this regard, the court in *Major v. Buchanan* stated:

A solicitor has the duty of warning a client of the risks involved in a course of action contemplated by the client or by his solicitor ... and of exercising reasonable care and skill in

¹⁵ Donald J. Bourgeois, *The Law of Charitable and Not-for-Profit Organizations, Third Edition* (Markham: Butterworths, 2002) at 5.

advising him. If he fails to warn the client of the risks involved in the course of action and it appears probable that the client would not have taken the risk if he had been so warned, the solicitor will be liable. If he warns the client of the risks ... then he can only proceed to follow such course if the client instructs him to do so.¹⁶

(c) It is also incumbent upon a lawyer dealing with a charity to not only inform the charity of the inherent risks associated with the contemplated course of action, but also to identify if there are better alternatives. “The solicitor has a duty to advise the client whether or not his instructions are unreasonable, or unworkable, or involve certain risks and better alternatives.”¹⁷

(d) Even where the charity specifically instructs the lawyer to only undertake a certain task and no more, if the lawyer in completing that task becomes aware of a risk that the charity is taking, then the lawyer is obliged to advise the client of the risk notwithstanding the limited nature of the retainer. In *Marbel Developments Ltd. v. Pirangi*,¹⁸ the British Columbia Supreme Court held that the existence and extent of a solicitor’s duty to advise a client must, in part, depend on the nature and extent of his or her retainer. In finding that the solicitor in question, using reasonable professional judgment, failed to advise the client of certain inherent risks, the court stated, “the solicitor must not allow his client to define the retainer unilaterally, in ignorance of material risks of which the solicitor is or should be aware.”¹⁹

If a lawyer involved with a charity on a specific matter becomes aware of a potential problem on another matter, such as a breach of trust involving donor restricted trust funds, it is incumbent upon the lawyer to advise the charitable client of the risks associated with the activity that the lawyer has observed.

These expectations are echoed in the *Rules of Professional Conduct* of the Law Society of Upper Canada. Rule 2.01 defines a competent lawyer as one “who has and applies relevant skills, attributes, and values in a manner appropriate to each matter undertaken on behalf of a client including ... recognizing limitations in one’s ability to handle a matter or some aspect of it, and taking steps

¹⁶ *Major v. Buchanan* (1975), 9 O.R. (2d) 491 at 514 (H.C.) [*Major*].

¹⁷ *Elcano Acceptance Ltd. v. Richmond, Richmond, Stambler & Mills* (1985), 31 C.C.L.T. 201 at 219 (Ont. H.C.), rev’d on other grounds (1986), 55 O.R. (2d) 56 (C.A.) [*Elcano*].

¹⁸ (1994), 18 C.C.L.T. (2d) 229 (B.C. S.C.) [*Marbel*].

¹⁹ *Ibid.* at 239.

accordingly to ensure the client is appropriately served.”²⁰ The rule also requires a lawyer to investigate facts, identify issues, ascertain client objectives, considering possible options, and develop and advise the client on appropriate courses of action. In so communicating, the lawyer must do so in a manner that is appropriate to the client’s abilities.²¹

6. Conflicts of Interest in Advising the Charitable Client

In addition to the obligation to actively warn the charitable client of risks, a lawyer involved in acting for a charity can on occasion find himself or herself in difficulties as a result of real or perceived conflicts of interest. Some examples of these conflicts include:

(a) A lawyer as a member of the board of directors of a charity may be asked to provide legal services in return for a fee, whether the fee be at full rate or at a reduced rate. In such a situation, the lawyer would be in breach of his or her fiduciary duty as a director of the charity, no matter how small the amount of remuneration is.²²

(b) Even if the lawyer, in providing legal advice or services while a member of the board of directors, does not receive any remuneration from the charity, there may still be a conflict of interest inherent in the lawyer assuming fiduciary responsibilities as a board member while at the same time acting as the professional legal advisor for the charity. The dichotomy in roles may put the lawyer in an untenable situation, where for instance, the board is reluctant to adopt recommendations contained in the legal opinion from the lawyer. In such a situation, it may become difficult if not impossible for the lawyer to fulfil his or her fiduciary obligation to put the best interests of the charity foremost while at the same time having to deal with the professional consequences of whether or not the advice rendered is acted upon by the client.

This is not to suggest that providing free legal services to a charity by a lawyer who is a member of its board of directors necessarily constitutes a breach of fiduciary duty; rather it indicates that there may, in

²⁰ Law Society of Upper Canada, *Rules of Professional Conduct*, r. 2.01 (updated to February 2005) [Rules].

²¹ *Ibid.*, r. 2.01(b),(d).

²² *Re Public Trustee and Toronto Humane Society* (1987), 60 O.R. (2d) 236 (H.C.) [*Toronto Humane Society*]. See also *Harold G. Fox Education Fund v. Public Trustee* (1989), 69 O.R. (2d) 742 (H.C.) [*Harold G. Fox*], and *Re French Protestant Hospital*, [1951] 1 Ch. 568 [*French Protestant Hospital*].

certain circumstances, be a conflict of interest which can only be resolved by the lawyer either ceasing to act as the solicitor for the charity or removing himself or herself from the board of directors to permit the lawyer to provide totally impartial legal advice. The lawyer is already faced with significant liability simply being a member of the board of directors of a charity without also unnecessarily exposing himself or herself to the increased risk of having detrimental reliance placed upon his or her professional advice given free of charge.

(c) A similar type of conflict could arise when the lawyer is acting as solicitor for two related charities, such as an operating charity and a parallel foundation, where the interests of the two charities are at odds. For instance, when the board of directors of one related charity is in disagreement with the direction taken by board of directors of the other charity, the solicitor may need to declare his or her conflict of interest and recommend that one or both of the associated charities obtain independent legal advice.

(d) Conflicts of interest can also arise where the lawyer is called upon to advise the board of directors of a charity and the advice rendered indicates that the directors could be found personally liable. When this occurs, the lawyer should advise each member of the board of directors that the advice being rendered is directed to the board members in their capacity as directors of the charity and is not being given as legal advice to them in their personal capacity. As a result, the lawyer should advise the board of directors that each member should obtain their own independent legal advice to review the consequences of their actions.

(e) A conflict of interest can also arise where the legal opinion sought by the executive director of a charity results in an opinion which the executive director is reluctant to pass along to the board. In such a situation, the lawyer should expressly request that the legal opinion be communicated to the board of directors. If it is not, then depending upon how serious the matter is, the lawyer may want to send a copy of the opinion letter to the home addresses of the directors, particularly if the lawyer has become aware that the executive director is trying to “stone wall” the board from receiving the legal opinion in question.

Once again, the *Rules of Professional Conduct* clearly warns lawyers against proceeding in the circumstances of a conflict of interest. The commentary to Rule 2.04 cautions that a “client’s affairs may be seriously prejudiced unless the lawyer’s judgment and freedom of action on the client’s behalf are as free as possible from conflict of interest.”²³

E. MINIMIZING PERSONAL EXPOSURE TO RISK

From the case law referred to above, it is clear that it is no longer sufficient for a lawyer in advising a charity to provide the services of a legal technician only without considering and advising the charitable client on the consequences of its action. Since lawyers may now be held liable as much for what they don’t say as for what they do say, lawyers by necessity need to become proactive in advising the charitable client.

Most firms that regularly deal with charities have law clerks who are generally capable in technically creating a charitable corporation, preparing the application for charitable registration with CRA, and completing the necessary government filings. What a lawyer is called upon to do in advising the charitable client is to go a step beyond what the law clerk does and provide active legal counsel to identify and avoid legal problems before they occur. An analogy can be made to the accounting profession, between a bookkeeper who provides only financial statements for his clients at the end of the year and a chartered accountant who is expected to go the extra step and identify problem areas in the business operations and provide recommendations on how to better structure the business in order to improve the net earnings and reduce taxes where possible. In the context of charities, a lawyer must change from providing passive, reactive advice to providing legal counsel in a proactive and preventative context that anticipates problems and reduces legal risks in charitable operations.

Lawyers and consultants who regularly deal in risk management issues have identified the need to practice preventative law. Brian D. Wynn states:

Like wellness in medicine, preventative law is a philosophy or regimen which applies to the planning process. It is designed to reduce conflicts so that only the toughest of issues demand expensive dispute resolution mechanism. ... Contrast it to the other, reactive mode of client/lawyer relations where the embattled client habitually calls on the lawyer “when there is a

²³ *Ibid.*, r. 2.04, commentary.

problem” and requests a remedy or solution. It isn’t hard to see which style promises greater efficiency in the long run.²⁴

F. STRATEGIES TO ADDRESS THOSE RISKS

In the context of advising charities, proactive legal risk management advice is difficult to define with any exactitude, but generally can be said to include the following:

(a) The lawyer must become familiar with the law before he or she can effectively advise the charitable client on how to avoid potential legal risks. This requires that the lawyer have a grasp of different forms of organizational structures for charities, i.e. corporate, unincorporated associations, charitable trusts, and charitable non-share corporations, under both the *Ontario Corporations Act*,²⁵ and the *Canada Corporations Act*,²⁶ and its impending successor legislation, entitled *Canada Not-for-Profit Corporations Act*.²⁷

The lawyer should also have an understanding of the history of charities based upon trust law; a working knowledge of the applicable provisions of the ITA as it applies to charities; familiarity with the various reporting requirements of both the federal and the provincial governments, particularly Ontario’s Public Guardian and Trustee under the CAA; a general understanding of inclusions and exclusions of general liability insurance policies; familiarity with third party liability exposure and the *Occupiers Liability Act*;²⁸ a grasp of title issues related to charities owning real property; an understanding of employment law and contracts; familiarity with the *Trade-Marks Act*,²⁹ and the registrations available thereunder; an understanding of the exposure of directors and officers to personal liability under both the common law and numerous provincial and federal statutes; a grasp of board management issues; familiarity with basic accounting principles involving charitable funds, particularly as it relates to donor restricted trust funds; as well as a general understanding of national and international charitable structures, if applicable.

²⁴ Brian D. Wynn, “Happenings, A Word on Recreational Accidents, Risk Management and Preventative Law” in *Fairs, Festivals and Fund Raisers: Legal and Risk Management Issues for Special Event Organizers* (Toronto: Canadian Bar Association, 1995) Tab 11 at 15.

²⁵ R.S.O. 1990, c. C.38.

²⁶ R.S.C. 1970, c. C-32.

²⁷ Bill C-21, *An Act respecting not-for-profit corporations and other corporations without share capital*, 1st Sess., 38th Parl., 2004. Bill C-21 was referred to Committee on 23 November 2004. The new act, which is intended to simplify and streamline the regulatory burden on not-for-profit corporations and other non-share capital corporations, will replace Parts II and III of the *Canada Corporations Act*. For more information, please see Jacqueline M. Connor and Terrance S. Carter, “New *Canada Not-for-Profit Corporations Act* and its Impact on Charitable and Non-Profit Corporations” in *Charity Law Bulletin No. 60* (30 December 2004), available at www.charitylaw.ca.

²⁸ R.S.O. 1990, c. O.2.

²⁹ R.S.C. 1985, c. T.10.

Without some knowledge in these areas of the law, a lawyer in attempting to advise a charitable client may have a difficult, if not an impossible time, in trying to effectively guide the client in avoiding problems before they occur, let alone simply trying to ensure that the charity complies with all of the basic requisite statutes that have general application to the day-to-day operations of a charity.

(b) In meeting with the charitable client to conduct a legal risk management review, the lawyer should assume nothing. In other words, the lawyer should not assume that the charitable client knows the relevant law, or is aware of problems that may need to be addressed, or is aware of the consequences of the present or proposed course of action. If there are any assumptions of facts which the lawyer makes, it is essential that those assumptions be expressed and confirmed with the charitable client before proceeding; otherwise, confusion or possible negligence could result if the lawyer gives advice based upon either a wrong or an incomplete assumption of the relevant facts.

(c) In meeting with the charitable client, the lawyer needs to be diligent in asking questions of the client to identify either existing or potential problems that the charity may be facing. A good technique to facilitate this process is to use a form of checklist, a sample of which is appended to this paper.

(d) In reviewing the operations of the charity, it is important that the lawyer explain major areas of the law that are particularly relevant to the client, even when there is not necessarily a problem that has been identified, so that the client will be aware of the need to comply with the applicable law in the future. For instance, even though a particular charitable client may not presently be gifting monies to a foreign charity, the issue may have to be faced by the charity at some time in the future. It is therefore helpful to explain in advance the correct means of gifting monies to non-qualified donees outside of Canada so that the charity will be prepared.

(e) When a problem is identified, either in relation to current activities or a proposed action, it is essential for the lawyer to fully explain the consequences of the course of action in question. In this regard, if the consequences may ultimately expose members of the board of directors to personal liability, it is important that this be identified in unequivocal terms, even if the information being conveyed to the charity is not what the client wishes to hear.

(f) Having identified the problem, it is then incumbent upon the lawyer to provide the charitable client with recommendations that can be implemented to rectify the problem, together with other effective alternatives, if possible, that can be adopted to eliminate the risk.

(g) In the event that numerous problems are identified, then at the end of the meeting, it is helpful for the lawyer to set up a priority list of what problems need be dealt with first and in what time frame they should be addressed. Failure to do this can often leave the charitable client overwhelmed by the problems, and potential liability and may, on occasion, have the unfortunate effect of leaving the board of the charitable client paralysed in fear and unable to do anything other than contemplate mass resignation from the board. As such, it is not sufficient for the lawyer to simply provide a list of problems. The lawyer must also provide constructive solutions and an appropriate time frame in which to achieve the steps required to rectify the problems.

(h) It is important that the lawyer then provide a well organized report to the client confirming the advice given, the problems identified, the solutions suggested, and a realistic time schedule to implement those solutions. The report will then become a reference tool for both the client and for the lawyer in monitoring the progress that needs to be made.

(i) The report should be addressed not only to the executive director, if applicable, but to all of the members of the board of directors of the charity. In some circumstances, it may be appropriate for the lawyer to attend the board of directors meeting to provide a summary of the issues addressed in the report, utilizing overheads or summary sheets to facilitate simplifying the presentation on what often involves complicated issues and consequences.

(j) After the provision of a comprehensive report to the client, it is then important to explain that it is the responsibility of the charitable client to decide if the board wishes to adopt the recommendations provided in the report, and if so to communicate those instructions to the lawyer. The reason for doing so is to ensure that having identified the problems and provided the recommended procedures to deal with those problems, the onus is put upon the charitable client to provide the instructions to proceed with implementing the recommended remedial steps. Otherwise, the lawyer may find himself or herself at a later time being criticized

or possibly being held liable in the event the charity's board does not proceed with the recommended course of action.

(k) Assuming the client does provide instructions to the lawyer to commence work on some or all of the recommended course of action, the lawyer should prepare and provide the client with a checklist of the steps that need to be done and the time frame in which those steps are to be accomplished.

(l) In the event the charitable client does not make an initial decision to proceed with the recommended course of action, the lawyer should send a follow-up letter to the client one or two months after the initial report to remind the client of the need to make a decision and to once again confirm that the onus lies upon the client to provide the instructions to proceed. This is important to clarify with the client, since the charitable client may be reluctant to adopt a particular recommended course of action for various reasons, and as such, the lawyer will want to ensure there is no confusion concerning the reason why the recommended course of action has not been adopted, particularly when it involves potential personal liability to directors and officers of the charity.

(m) After the initial problems identified in the report have been addressed, the client should be advised to periodically review matters with legal counsel concerning its ongoing operation on either an annual or bi-annual basis to determine if further issues may have unnecessarily exposed the charity to legal risks.

G. DEVELOPING A LEGAL RISK MANAGEMENT CHECKLIST

1. Sample Checklist

Attached to this paper as Appendix "A" is a document called a "Legal Risk Management Checklist for Charities." The Checklist was developed for two reasons:

- (i) A checklist enables a lawyer to keep track of the many issues that need to be reviewed in meetings with charitable clients.
- (ii) A checklist is another tool to assist the charitable client in identifying areas of potential legal risks on their own, as well as to assist the client in understanding the myriad of legal and risk management issues that need to be addressed to some extent by most charities.

The Legal Risk Management Checklist for Charities has been structured so that it both raises legal issues as well suggesting some tentative solutions. Although the Checklist attempts to be as generic and broad as possible, it is clearly neither all-inclusive nor comprehensive in the dealing with the issues that are identified. As a result, the lawyer utilizing the Checklist will need to modify it as necessary to customize the Checklist to reflect the emphasis each lawyer places on the advice given to their respective clients.

2. How to Utilize a Checklist

When meeting with a charitable client, whether it be to answer a specific question or to conduct a legal review, a copy of the Legal Risk Management Checklist for Charities could be given to the client with the lawyer retaining a copy. This will then permit both the lawyer and the client to review the matters dealt with in the Checklist, identifying potential problem areas and developing suggested solutions. Alternatively, a copy of the Checklist can be forwarded to the charitable client prior to the meeting so the client will be familiar with the format that will be followed during the interview. However, the danger of forwarding the Checklist in advance of the meeting is that the charitable client can often become overwhelmed by the number of issues that need to be addressed. As such, it is generally better to meet with the client in person to explain the need for the Checklist and its contents.

During the interview, the client should be encouraged to make notations on his or her copy of the Checklist, with the lawyer doing the same. These notations will provide a useful tool for the lawyer in structuring the reporting letter concerning the problems that have been identified and the solutions recommended.

A copy of the Checklist should be dated and put into the file so that it can be referred to at a later time in monitoring the progress by the charity in rectifying the problems that have been highlighted. This is particularly useful in those situations where there has been a change in a board of directors or a change in the executive staff, since the new individuals may not be aware that a Legal Risk Management Checklist for Charities had been used in earlier meetings to identify problems and recommend solutions.

For those situations where clients have received a copy of the Checklist, but for whatever reason do not arrange to meet with the lawyer to review the matters raised in the Checklist, it is recommended that

the client be advised the issues raised in the Checklist are complicated, have serious consequences, and as such the client should not attempt to do a review on their own without the assistance of legal counsel. In the event the client decides not to retain the lawyer further, at least there will be correspondence warning the client that a review of the Legal Risk Management Checklist for Charities without legal counsel does not constitute a proper review or determination of the various legal risks a charity may be facing.

3. The Structure of the Legal Risk Management Checklist for Charities

The Checklist begins by explaining in point form why it is important to identify legal risk management issues. This involves reviewing a number of issues and the complexities involved in operating a charity, as well as explaining the types of problems a charity can face, who is exposed, and the need to take corrective steps.

The Checklist then identifies the need to establish a procedure to identify and manage legal risk liabilities, such as the creation of a liability management committee to oversee, identify and reduce legal risks.

The Checklist next deals with some basic issues of deficiencies in legal organization, board management matters, reducing board liability, insurance considerations, third party use of charitable property, real property issues, leasing matters, intellectual property, employment and volunteer matters, charitable activities, fiscal management matters, the dangers of operating with a deficit, compliance with trust fund obligations, maintaining charitable registration, and issues involving national and international structures.

While each lawyer will need to modify the Checklist to prioritize the issues in whatever order the lawyer feels is appropriate, it is important that the Checklist cover as many issues as possible and as a result in reviewing the Checklist, the lawyer and the client should be careful not to rush through the items referred to in it simply because of the volume of issues. It is therefore generally recommended that at least a two hour interview be set up to initially review the Checklist, with possible additional meetings being subsequently scheduled as necessary.

H. EFFECTIVELY COMMUNICATING WITH THE CHARITABLE CLIENT

1. Confirming Retainer

Since the lawyer is often contacted by the charitable client to provide an answer to a question as a “favour,” it is important for the lawyer to determine whether or not he or she is being asked to provide a professional opinion that will be relied upon, or whether he or she has been contacted to provide advice without professional consequences and corresponding liability. More often than not, the lawyer will have been asked a question on the assumption that the charity believes that it can rely upon the answer, whether or not the charity is able to or intends to pay for such advice.

As a result, it is prudent for the lawyer who is contacted by a charity to confirm in writing the advice being sought, the advice given, and whether or not there is to be any charge for the service that has been rendered. Failure to do so could result in an unfortunate situation of the charitable client relying upon an opinion that the lawyer never intended to constitute a professionally researched opinion.

2. Educational Reports

By far the most frequent task for which lawyers are called upon to assist charities is to complete the incorporation process and obtain charitable registration. The lawyer will normally consider the task completed when letters patent have been obtained, the minute book has been organized, and a charitable registration number has been obtained from CRA.

However, it is advisable for the lawyer to explain to the charitable client how the charity is to function as a non-share capital charitable corporation, how to comply with the numerous requirements under the ITA applicable to charities, how to comply with various government reporting requirements, as well as providing an explanation of the basic responsibilities and liabilities members of the board of directors will face in operating the charity. As a result, not only must the lawyer provide a reporting letter on the incorporation and initial organization to the charity, which often is never done, but the reporting letter should be structured as a type of “operating manual” so that the letter can be used for reference purposes by both the current and future members of the board of directors.

3. Documenting Advice Given

When acting on behalf of a charitable client in conducting a legal risk management review, it is important that the lawyer provide a comprehensive report to the charity on the risks that have been identified, the consequences of those risks, and the recommendations made to reduce exposure to legal liability.

Even after a legal risk management review has been completed, there will often be need for subsequent consultations with the client to monitor the progress being made by the charity to implement the recommendations. In addition, an ongoing charitable client will invariably need to contact the lawyer on an “as needs” basis to answer specific questions that may arise out of the legal management review. In all of these situations, it is essential that timely and complete reports be provided to the client concerning the advice sought and the recommendations provided.

In the event that the lawyer is unable to prepare a report shortly after the advice has been given, a practical technique to ensure that timely reports are provided is to do an inventory of all files involving charities at the end of each month to ensure that up-to-date reports as necessary have been prepared and sent to all charitable clients.

I. CONCLUSION

Increasingly, advising charities is becoming a speciality practice of law, especially given the number of charities in Canada, the size of the operations and the complexities of the law involving charitable operations. Accordingly, lawyers who are called upon by charities to provide legal advice must either do so in a thorough and professional manner or not at all, whether or not the work is provided on a *pro bono* basis or at a reduced rate. There is nothing at law which justifies a reduced level of service simply because the work is done as an act of charity itself. What the law does state is that all clients are entitled to assume their legal counsel will take the initiative to warn of pending problems and the consequences associated therewith. This professional expectation has as much application to the charitable client as it does to any other. As a result, lawyers who are called upon to assist charitable clients should approach their task in the context of not only providing technically correct legal services but going further and providing proactive legal counsel to anticipate and advise the client on avoiding unnecessary legal risks before they occur. For those who decide to conduct their practice in this context, they will find that the experience of counselling the charitable client will change from one of frequent frustrations to one of achieving a measure of personal satisfaction in having undertaken a difficult task in what one hopes is a thorough and competent manner.

J. AUTHORITIES

Cases

Boldrini v. Hamilton Naturalists' Club, [1995] O.J. No. 3321 (Gen. Div.) 11

Canada Revenue Agency, *Online List of Canadian registered charities* (as of 14 October 2005). 2

Elcano Acceptance Ltd. v. Richmond, Richmond, Stambler & Mills (1985), 31 C.C.L.T. 201 at 219 (Ont. H.C.), rev'd by (1986), 55 O.R. (2d) 56 (C.A.) 13

Harold G. Fox Education Fund v. Public Trustee (1989), 69 O.R. (2d) 742 (H.C.) 14

Major v. Buchanan (1975), 9 O.R. (2d) 491 at 514 (H.C.) 13

Marbel Developments Ltd. v. Pirangi (1994), 18 C.C.L.T. (2d) 229 (B.C. S.C.) 13

Re French Protestant Hospital, [1951] 1 Ch. 568. 14

Re Public Trustee and Toronto Humane Society (1987), 60 O.R. (2d) 236 (H.C.) 14

Special Commissioners of Income Tax v. Pemsel, [1891] A.C. 531 (H.L.) 4

Stahl v. Ontario Society for the Prevention of Cruelty to Animals (1989), 70 O.R. (2d) 355, 35 E.T.R. 234 (Dist. Ct.) 11

Vancouver Society of Immigrant and Visible Minority Women v. M.N.R., [1999] 1 S.C.R. 10. 4

Statutes

An Act respecting not-for-profit corporations and other corporations without share capital, Bill C-21, 1st Sess., 38th Parl., 2004. 17

Canada Corporations Act, R.S.C. 1970, c. C-32 17

Charities Accounting Act, R.S.O. 1990, c. C-10 4

Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.) 2

Occupiers Liability Act, R.S.O. 1990, c. O.2. 17

Ontario Corporations Act, R.S.O. 1990, c. C.38 17

Trade-marks Act, R.S.C. 1985, c. T.10. 17

Rules

Law Society of Upper Canada, *Rules of Professional Conduct*, r. 2.01. 14

Other Authorities

Bourgeois, Donald J. *The Law of Charitable and Not-for-Profit Organizations, Third Edition* (Markham: Butterworths, 2002). 12

Canada Revenue Agency, Charities Directorate. *Registered Charities Newsletter, No. 19* (June 2004). 1

Connor, Jacqueline M. and Carter, Terrance S. “New *Canada Not-for-Profit Corporations Act* and its Impact on Charitable and Non-Profit Corporations” in *Charity Law Bulletin No. 60* (30 December 2004). 17

Hall, Michael H., de Wit, Margaret L., Lasby, David, & McIver, David McIver. *Cornerstones of the Community: Highlights of the National Survey of Nonprofit and Voluntary Organizations* (Ottawa: Statistics Canada, 2004). 2

Innes, William I., “Liabilities of Directors and Officers of Charitable and Non-Profit Corporations” (1993), 13 E. & T.J. 1 7

Levitt, Theodore. *The Third Sector: New Tactics For a Responsive Society* (New York, 1973). 2

Man, Theresa L.M. “July 18, 2005 Draft Amendments to the *Income Tax Act* Affecting Charities: Part I – Definition of Gift & Split-Receipting” in *Charity Law Bulletin No. 76* (8 September 2005). 4

Man, Theresa L.M. and Carter, Terrance S. “Commentary on Draft Technical Amendments to the *Income Tax Act* Released on December 20, 2002 That Affect Charities” in *Charity Law Bulletin No. 21* (30 April 2003). 4

Man, Theresa L.M. and Carter, Terrance S. “February 27, 2004, Revised Draft Amendments to the *Income Tax Act* Affecting Charities” in *Charity Law Bulletin No. 40* (29 March 2004). 4

Wynn, Brian D. “Happenings, A Word on Recreational Accidents, Risk Management and Preventative Law” in *Fairs, Festivals and Fund Raisers: Legal and Risk Management Issues for Special Event Organizers* (Toronto: Canadian Bar Association, 1995) Tab 11. 17

Appendix A

Legal Risk Management Checklist for Charities

LEGAL RISK MANAGEMENT CHECKLIST FOR CHARITIES

By Terrance S. Carter, B.A., LL.B. and Jacqueline M. Connor, B.A., LL.B.

A. INTRODUCTION

The operations of charities have become complex and the possibility of litigation against charities occurring as a result of their operation is greater than ever before. The exposure of charities to liability goes further than the loss of charitable assets and/or the insolvency or winding up of a charity. Directors of charities may also personally face legal actions against themselves by donors, members, third parties and governmental authorities for breach of their fiduciary duties or even breach of trust in failing to adequately protect or apply the assets of a charity. Given the increased risks to both charities and their directors, there is an increasing need to protect charitable assets from lawsuits and creditors on a pro-active basis.

The purpose of this legal risk management checklist is to provide a brief outline of some of the more important issues that directors and/or executive staff of a charity, whether incorporated or not, may need to consider in ensuring due diligence in the operation of the charity, as well as an overview of liability exposure faced by charities in Canada and some of the steps that could be taken to protect charities against such risks. As it is impossible to adequately address all aspects of liabilities faced by charities, and the pro-active steps which should be taken to protect against such risks, this checklist provides only a general overview of the considerations that charities and their boards of directors may need to be aware of to both identify and manage legal risks. Some of the comments and recommended procedures contained in this legal risk management checklist may also be applicable to not-for-profit non-charitable organizations.

B. IDENTIFICATION AND MANAGEMENT OF LEGAL RISKS

1. Is charitable status needed?
 - a) Do charitable receipts need to be issued?
 - b) Can the organization work under the auspices of an existing charity?
 - c) Business donors may not require charitable receipts.

2. General overview of organizational & legal documentation
 - a) Identify the existence and location of key organizational documents
 - Develop an inventory of key documents
 - Maintain central location for key documents
 - b) Identify key organizational documents for an unincorporated charity
 - Constitution and amendments, if applicable
 - Policy statements, if applicable
 - c) Key organizational documents for a corporate charity
 - Letters patent and supplementary letters patent, if applicable
 - Membership covenant and mission statement, if applicable
 - By-laws and resolutions
 - Directors, members and debt registers
 - Copies of government filings
 - d) Determining other key legal documents
 - Leases, deeds and mortgages
 - Agency, association and joint venture agreements
 - License agreements
 - Business name, trade-marks, Section 9 official marks and domain names
 - Charitable registration number
 - Policy statements, i.e. sexual abuse and volunteer policy statement
 - Insurance policies
 - Privacy policy
 - Investment policy

3. Review of key documents for unincorporated charity
 - a) Are the objects clearly stated in the constitution and are they exclusively charitable?

- b) Do constitutional documents correctly reflect how the organization is actually structured and operated?
 - c) Is a copy of the constitution filed with the appropriate government agencies, i.e. with Canada Revenue Agency (“CRA”) and the Public Guardian and Trustee (“PGT”)?
4. Review of key documents for an incorporated charity
- a) Review of letters patent
 - Is the name in the letters patent the correct name of the charity and is it consistent with the charitable objects of the charity?
 - Are its objects exclusively charitable?
 - Are the activities carried out by the charity authorized by its charitable objects?
 - Is the dissolution clause complementary to the charitable objects?
 - b) Review of supplementary letters patent
 - Has there been a change of corporate name?
 - Has there been a change of corporate objects?
 - What is the effect of a change of objects upon existing charitable property?
 - c) Letters patent of amalgamation (only for Ontario corporations)
 - Are the charitable objects the same or similar?
 - What are the terms of the amalgamation agreement?
 - Is the existing charitable property held in trust for the charitable objects of the previous charitable corporations?
 - d) Review of corporate by-law for basic terms,
 - Do provisions conflict with letters patent?
 - Do provisions reflect changes to applicable corporate legislation?
 - Is there an adequate indemnification provision?
 - Has the indemnification provision been authorized in accordance with the *Charities Accounting Act* (Ontario)?
 - Are the by-law amendment procedures consistent with corporate legislation?
 - e) Was the initial corporate organization of the charity properly done?
 - f) Was there a documented transfer of assets and liabilities on incorporation?
 - g) Are the records of board decisions and/or membership meetings complete?
 - h) Was there adequate board and/or members’ authorization for indebtedness?
 - i) Have corporate records been properly maintained?
 - j) Have necessary corporate filings and registrations been kept up to date?
 - Ontario Corporations:

- ◆ Initial Notice and Notice of Change - Form 1
 - ◆ *Business Name Act* (Ontario) registrations
 - ◆ Mandatory reporting to Public Guardian and Trustee
 - Canada Corporations:
 - ◆ Annual Summary (Form 3) – Canada
 - ◆ Extra-Provincial Initial Notice (Form 2) – Ontario
 - ◆ *Business Name Act* (Ontario) registrations
 - ◆ Mandatory report to Public Guardian and Trustee
 - Does the charity operate and/or fundraise in any other provinces? If so, there may need to be registration as an extra-provincial corporation and/or fundraiser in other provinces, together with applicant business name registrations.
- k) Does the charity need to continue itself under the proposed new *Canada Not-for-profit Corporations Act*? (Note: Expected to be proclaimed into force in Spring 2006).
- l) Has there been loss of corporate status for failure to maintain government filings?
- m) Is the charity aware of the importance of proper use of corporate name and operating names?
- n) Has the charity developed and implemented risk management policy statements on:
- child abuse,
 - sexual abuse,
 - sexual harassment,
 - bullying,
 - volunteer conduct, and
 - safety in the workplace, where applicable?
- o) Has the charity conducted an inventory of its charitable assets?

C. UTILIZING MULTIPLE CHARITABLE CORPORATIONS

1. Should the charity consider utilizing multiple charitable corporations for its high risk activities in order to reduce liability exposure and protect assets?
2. Should the charity consider establishing and utilizing a parallel foundation for either fundraising or protection of charitable assets?
3. Has consideration been given to balancing indirect control of multiple corporations with issues involving cross over liability?
4. Has consideration been given to implementing effective indirect control through contracts and/or licensing agreements as an alternative to overt corporate control?

D. BOARD MANAGEMENT ISSUES

1. Is the charity able to identify which group is in charge of the charity?
 - a) Where does the *de facto* control of the charity lie? Is it with a board, a committee or executive staff?
 - b) Is board authority recognized by the membership?
2. Are there clearly defined lines of authority between the board and the executive staff?
3. Does the board meet on a regular basis and do all directors regularly attend?
4. Has an independent audit committee been established to review financial statements and the auditors' report?
5. Is there adequate communication of board responsibilities to existing and future board members?
 - a) Need to create a board binder of all corporate documents, as well as an explanation of the general operations of the corporation as a charity and the board of directors' legal duties and liabilities.
 - b) Need to provide regular updates on changes in the law to board members.

E. REDUCING BOARD LIABILITY

1. Do any directors receive direct or indirect remuneration or other financial benefit from the charity in contravention of their fiduciary duties?
2. Has the charity adequately indemnified its directors and officers in accordance with the *Charities Accounting Act* (Ontario)?
3. Is there corporate authority to acquire directors' and officers' liability insurance in accordance with the requirements of the *Charities Accounting Act* (Ontario)?
4. Has the board delegated too much responsibility to executive staff by restricting itself to policy decisions only without careful and ongoing monitoring and review?
5. Should the charity consider reducing the size of the board to limit the number of people who are exposed to liability as directors?
6. Is the charity effectively making use of committees as an alternative to a large board of directors?
7. Do the board members occasionally need to receive independent legal advice due to the possibility of liability exposure?

8. Should the charity consider implementing an advisory board to complement the board of directors without a corresponding exposure to liability?
9. Has the charity established a comprehensive due diligence review procedure by establishing and utilizing the appropriate legal risk management checklist?
10. Has a legal risk management committee of the board been established?

F. INSURANCE CONSIDERATIONS

1. Has the charity maintained a historical record of its insurance coverage in the event of a future claim?
2. Is there occurrence-based or claims-made insurance coverage for sexual abuse?
3. Has the charity provided full written disclosure of all risks to its insurer to avoid denial of coverage?
4. Does the charity request regular reports from its insurance broker on existing coverage, exclusions from coverage and recommendations to enhance coverage?
5. Is there a regular review of the adequacy and extent of general liability coverage and property insurance?
6. Is there directors' and officers' liability coverage in place and is it reviewed on a regular basis?
7. Do there need to be special insurance endorsements to extend insurance coverage, e.g. activities of agents in foreign countries?

G. THIRD PARTY USE OF CHARITABLE PROPERTY

1. Is the charity aware of the potential liability exposure in permitting third parties to use its property?
2. Has the charity developed and implemented a third party property use agreement with appropriate releases and indemnification?
3. Does the charity require evidence of liability insurance from third party users of its facilities?
4. Does the charity charge appropriate fair market rental fees to non-charities?

H. REAL PROPERTY ISSUES

1. Has an environmental assessment been conducted to determine the extent of possible liability exposure for contamination?

2. Are there trust provisions in old trust deeds or title, and if so, are they being complied with?
3. Has the charity addressed and rectified encroachments with neighbouring lands?
4. Are municipal zoning and legal non-conforming uses being complied with?
5. Could the charity be forced to sell off surplus land under *Charities Accounting Act* (Ontario) if it has been held for more than three years?
6. Has the charity reviewed its entitlement to possible exemption from municipal property taxation, or reviewed its assessment for accuracy, or its entitlement to a possible rebate of property taxes?
7. Has the charity entered into a lease and has its terms been reviewed for possible liability, such as a restoration clause or relocation clause?

I. INTELLECTUAL PROPERTY ISSUES

1. Does the charity need to register any of its key names and/or logos as trade-marks?
 - a) Identify trade-marks
 - b) Protect trade-marks by registration
 - c) Use trade-marks in conjunction with appropriate markings
 - d) Ensure that any third parties using trade-marks enter into a trade-mark licensing agreement
2. Has the charity protected its trade-marks by multiple corresponding domain names?
3. Who owns the copyright for publications of the charity?
4. Should copyright be registered, assigned or licensed?

J. EMPLOYMENT AND VOLUNTEER MATTERS

1. Is the individual being paid an employee or an independent contractor?
2. Has the charity developed appropriate hiring policies and practices for its employees?
3. Is there compliance with applicable human rights legislation?
4. Is there need for an employment contract with employees?
5. Is there a need to develop and adopt policy statements and/or manuals for employees as well as volunteers?

6. Do employees and volunteers who deal with children need to be screened and supervised, together with criminal record checks, in accordance with an appropriate sexual abuse policy statement?
7. Is there need for a discipline procedure for employees and/or volunteer members?
8. Has the charity developed appropriate policies and practices regarding the termination of employees and complied with appropriate provincial and/or federal legislation?
9. Is the charity aware of and complying with applicable statutory requirements, such as pay equity, employment standards, human rights legislation, privacy legislation and occupational health and safety prerequisites?
10. Are the charity and board exposed to criminal liability under the *Criminal Code* i.e. Bill C-45 (Westray Mines)?

K. CHARITABLE AND FUNDRAISING ACTIVITIES

1. Has the charity ensured that its charitable activities are done in accordance with its charitable objects?
2. Are fundraising and/or administrative costs kept within the 80/20 disbursement quota?
3. Has provincial fundraising legislation, where applicable, been complied with?
4. Have fundraising programmes been reviewed by legal counsel?
5. Are donors' rights to require accountability respected, particularly rights under the *Charities Accounting Act* (Ontario)?
6. Does the charity have a privacy policy in place in order to protect donors' rights?
7. Are sponsorship arrangements properly documented?

L. FISCAL MANAGEMENT ISSUES

1. Are all salaries, benefits and statutory deductions being paid by the charity on a timely basis with appropriate reports to the board of directors?
2. Is the charity operating with a deficit and, if so, for how long?
3. How is the deficit being funded?
4. Has a sinking fund been established to retire debt of the charity?
5. Are investments being offered to the public without full disclosure to potential investors?

6. Is there an audit committee in place?
7. Are charitable funds being used to fund separate business operations of the charity?
8. Is there a violation of the *Charitable Gifts Act* (Ontario) by the charity owning more than 10% of a business?

M. INVESTMENT ISSUES

1. What investment powers apply to the investment of surplus funds of the charity?
 - a) Prudent investor rule under the *Trustee Act* (Ontario) will generally apply
 - b) However, specific investment powers may sometimes apply as contained in
 - Letters patent or supplementary letters patent,
 - Endowment and gift agreements, or
 - Testamentary gifts.
2. Does the charity need and/or have an investment policy?
 - a) Documenting compliance with prudent investor rule
 - b) Establishing requirements for delegation of investment decision making
 - c) Prohibition on sub-delegation

N. DONOR RESTRICTED TRUST FUNDS

1. Are there donor restricted trust funds being held by the charity?
 - a) Building funds
 - b) Endowment funds (perpetual)
 - c) Ten year gifts under the *Income Tax Act*
 - d) Special project funds
2. Are restricted funds being used only in accordance with applicable restrictions?
3. Are restricted funds being used in whole or in part for general operational purposes or are they being borrowed against?
4. Are restricted funds segregated from operating funds?
5. Is there compliance under the *Charities Accounting Act* (Ontario) to co-mingle restricted funds for investment purposes?

6. Is the board of the charity aware of the consequences of breach of trust for failing to comply with restricted funds?

O. MAINTAINING CHARITABLE REGISTRATION

1. Is the legal name of the charity and/or its operating name consistent with the records of CRA?
2. Does CRA have the current head office address of the charity?
3. Has the charity obtained Quebec charitable status for fundraising in Quebec?
4. Does the charity submit its annual charity information return (Form T3010A) within 6 months of the financial year end of a charity?
5. Has the charity complied with its disbursement quota?
6. Can the charity comply with the new disbursement quota rules as of December 2004?
7. Is the charity involved in political activities within CRA limits?
8. Is the charity involved in related business activities within CRA guidelines?
9. Is the charity aware of the applicable rules concerning the issuance of charitable receipts including the new rules on split receipting and anti-tax shelter provisions?
10. Are agency and/or joint venture relationships with non-qualified donees properly documented and implemented?
11. Does the board of directors review the annual return (T3010A) for the charity before it is filed each year?
12. Is the charity prepared for a spot audit by CRA?

P. NATIONAL AND/OR INTERNATIONAL RELATIONSHIPS

1. Are relationships with national organizations and/or subsidiary chapters adequately documented with specific reference to controlling trade-marks?
2. Are relationships between national and international organizations adequately documented in order to effect an international operation?
3. Has the ownership of trade-marks and/or copyrights been determined and documented?
4. Have trade-marks and copyrights been adequately protected and licensed in Canada and in other countries as necessary?

Q. ANTI-TERRORISM LEGISLATION

1. Does the charity carry on operations that may require it to be in compliance with anti-terrorism legislation?
 - a) International operations
 - b) Domestic operations
2. Has the charity undertaken appropriate due diligence procedures in complying with anti-terrorism legislation?
 - a) Development of an anti-terrorism policy statement
 - b) Development of resource materials on anti-terrorism legislation
 - c) Requiring disclosure statements for board members and staff
 - d) Evaluating all charitable programs for compliance
 - e) Requiring disclosure statements from affiliated charities, third party agents and/or partners and conducting appropriate inquiries
 - f) Determining when to make inquiries of donors
 - g) Conducting due diligence internet searches on directors, officers and agents
3. Are directors aware of risks associated with failing to comply with anti-terrorism legislation?
 - a) Loss of charitable status
 - b) Personal liability in civil law
 - c) Possible criminal law sanctions