

FIDUCIARY RELATIONSHIPS IN FUNDRAISING: THE IMPACT OF THE AIDS SOCIETY FOR CHILDREN DECISION

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

| Carter & Associates

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Editor: Terrance S. Carter, B.A., LL.B

A. INTRODUCTION

The recent decision of the Ontario Superior Court of Justice in *The Aids Society for Children (Ontario)*, 105 A.C.W.S. (3rd) 1044, will have a serious impact upon charitable fundraising and the relationship of charities with fundraisers, both in Ontario and across Canada. This Charity Law Bulletin provides a summary overview of the case and explains its implications upon fundraising activities involving charities.

B. BACKGROUND FACTS

The Aids Society for Children (Ontario) (the “Aids Society”) was incorporated on November 28th, 1994, and obtained charitable status from Revenue Canada (now Canada Customs and Revenue Agency “CCRA”) 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.

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, CCRA 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)*. 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 *Income Tax Act (Canada)*, and, if so, what is the effect, if any, upon the contractual arrangements between the Aids Society and the fundraising companies?

C. SUMMARY OF DECISION

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 *Income Tax Act* 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.

With the Court having provided its answers to the questions raised by the PGT, the PGT was able to proceed with the completion of the formal passing of accounts of the Aids Society and its directors.

D. IMPLICATIONS OF DECISION ON FUNDRAISING

The following implications can be drawn from the decision of the Court on 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 a 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 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 be 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.

E. CONCLUSION

The Aids Society case consolidates equitable principles of law concerning fiduciary obligations as they relate to charities and their board of directors in the context of fundraising. Although the case does not establish new law, it articulates the serious implications of the imposition of fiduciary obligations upon charities and their board of directors in relation to fundraising activities that will not have been fully understood before. Therefore, it is essential that charities, their board of directors, their executive directors, and their legal counsel be fully aware of the significant ramifications of this decision.

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Carter & Associates

BARRISTERS, SOLICITORS & TRADE-MARK AGENT

211 Broadway, P.O. Box 440
Orangeville, Ontario, L9W 5G2

Telephone: (519) 942-0001

Fax: (519) 942-0300

tcarter@carterslawfirm.com

www.carterslawfirm.com

www.charitylaw.ca