THE INSTITUTE OF CHARTERED ACCOUNTANTS OF ONTARIO
BOARD OF DIRECTORS RESOURCE MATERIALS

The Legal Duties of Directors of Charities and Not-For-Profits
(Power Point Presentation)

May 13th, 2003

By Terrance S. Carter, B.A., LL.B.
&
Jacqueline M. Connor, B.A., LL.B.
A. OVERVIEW OF TOPICS

• Introduction

• Common Law Duties and Liabilities

• Statutory Duties and Liabilities

B. COMMON LAW DUTIES AND LIABILITIES

• Management of the Corporation
  – Directors responsible for all aspects of corporations operations
  – To fulfill duties, directors must ensure:
    • Objects are properly carried out and activities comply
    • Corporation’s financial stability and overall performance
    • Proper hiring and supervision of management and staff
• Duty of Care
  – Directors of all corporations must exercise certain standard of care in carrying out duties
  – But standard of care varies depending on type of corporation
    • Business corporation
      – Statutory objective standard of care
      – Reasonably prudent person

• Not-for-profit corporation (non-charity)
  – Common law subjective standard of care
  – Director’s own knowledge and experience important
• Charitable corporation
  – Additional expectations beyond subjective standard
  – Directors of charities also subject to fiduciary duties as quasi-trustees of charitable property
• Liability Risk for Lack of Corporate Authority
  – Corporate authority defined by corporate objects in governing documents
  – All corporate activities must fall within parameters of these objects
  – Liability results where directors act outside scope of this authority

• Liability Risk for Negligent Mismanagement (Tort)
  – Tort is civil wrong for which injured party can seek damages from the court
  – Directors can be personally liable for corporation’s torts where own conduct contributed to victim’s injury

• Liability Risk in Contract
  – Directors generally not personally responsible for contracts signed for corporation
  – However, need to have proper corporate authority to sign contracts and ensure contractual terms are complied with
• Liability Risk for Breach of Fiduciary Duty
  – Overview
  • Directors of charitable corporations, subject to fiduciary duty to act as quasi trustee of charitable property
  • Directors have primary obligation to exercise due diligence in overseeing corporation
  • Fiduciary duties owed to charitable objects, corporation, donors and creditors

– Summary of fiduciary duties
  • Duty to act honestly
    – Conflicts of interest to be avoided and disclosed
    – Directors must not act fraudulently
  • Duty of loyalty
    – Director’s sole interest is to the corporation
    – Director’s interests not to be placed in conflict with those of corporation
- Duty of diligence/duty to act in good faith
  - Directors to diligently attend to duties by being familiar with all aspects of corporation
  - Where necessary, advice of qualified professionals to be sought
- Duty to exercise power
  - Directors responsible for managing corporation

- Delegation to management, staff and volunteers is possible, but directors must always supervise
- Duty of obedience
  - Directors must comply with applicable legislation and corporations governing documents
  - All valid corporate decisions must be implemented
• Duty to avoid conflict of interest
  – Conflicts of interests to be avoided
  – Directors must also avoid anything that
gives director appearance of a personal
benefit
  – Where conflicts occur, they are to be
declared, director to not participate in
discussions or vote, and may even have
to resign

• Duty of prudence
  – Directors with special expertise must
use it prudently to achieve best result
for corporation

• Duty to continue
  – Resignation as director will not
relieve all obligations
  – May even constitute breach of trust
  – Independent legal advice should be
obtained in considering resignation
• Liability for Breach of Trust
  – Overview
    • In addition to fiduciary quasi trustee duties, directors of charitable corporations may also be trustees of charitable property
    • However, fiduciary duties and trustee duties essentially the same
    • Aids Society case emphasizes that directors have obligation to apply charitable property to charitable objects

• Where charitable property lost as a result of actions or inactions of directors, breach of trust could be found
  – Potential liability risks
    • Remuneration of directors
      – In Ontario, directors of charitable corporations can not receive direct or indirect remuneration, e.g. as employee or contractor, without court approval
      – Indemnification and directors’ insurance now available
• Dealing with charitable property
  – Directors responsible for handling of charitable property
  – Personal liability results where mismanagement occurs
• Dealing with charitable objects
  – Charitable property only to be applied to charitable objects
  – Failure to properly apply charitable property may result in liability

• Dealing with special purpose charitable trusts
  – Directors of charitable corporations have fiduciary obligations to donors
  – Liability for breach of trust possible where donor restrictions or terms of endowment funds are not complied with
• Investment of charitable funds
  – Directors may sometimes have specific duty to invest charitable property
C. STATUTORY DUTIES AND LIABILITIES

• Overview
  – Many federal and provincial statutes impose offences and penalties for acts and omissions of corporate directors
  – Directors can be held personally liable, as well as jointly and severally, with other directors
  – Only defence is due diligence
  – Resigning as a director may not limit liability though there are generally limitation periods
• Federal Statutes
  – *Canada Corporations Act*
    • Wages and vacation pay
    • Conflict of interest
    • Reporting requirements
    • Books, minutes and records
    • Identification of corporation
    • Membership lists
    • Winding up
    • General penalty

• *Income Tax Act* (Canada)
  • Directors liability to pay employee income tax deductions for two years after term of office
  • Personal liability possible for failure to comply with reporting requirements, e.g. annual charity information return or improper charitable receipts, or for giving improper tax advice
  • Avoid liability by showing positive steps taken to ensure compliance
– **Excise Tax Act** (Canada)
  • Directors liable for corporation’s failure to collect & remit GST
  • Liability continues for two years after cease to be director

– **Canada Pension Plan**
  • Joint and several liability where corporation fails to remit employee pension premiums

– **Canadian Environmental Protection Act**
  • Positive duties imposed on directors to ensure compliance in relation to air and water pollution as well as toxic substance storage and disposal
  • Failure to comply could result in prison terms and fines

– **Anti-terrorism Legislation**
  • Legislation has serious liability risks for charitable corporations and directors, particularly those involved in overseas work
Risks include seizure of charitable property, loss of charitable status and criminal code charges

- See antiterrorismlaw.ca

- Ontario Statutes
  - *Corporations Act (Ontario)*
    - Reporting requirements
    - Conflict of interest
    - General offence provision

- *Employment Standards Act (Ontario)*
  - Fines imposed on directors for failure of corporation to pay wages, vacation pay and severances
  - 6 months liability for wages and 12 months liability for vacation pay, plus fines
  - However, limitation periods are available
– *Retail Sales Tax*
  - Directors jointly and severally liable where corporation fails to remit

– *Workplace Safety and Insurance Board Act (Ontario)*
  - Directors liable for corporation’s failure to remit premiums unless it can be shown they did not intend to pay them

– *Pension Benefits Act (Canada)*
  - Directors who fail to pay corporation premiums for employee’s pension plans and to hold monies in trust may be ordered to make up contribution
  - Failure to comply may subject directors to fines

– *Ontario Health Insurance Program*
  - Directors will be held personally liable for premiums and health tax not paid by corporation
– *Occupational Health and Safety Act* (Ontario)
  
  • Directors required to take reasonable steps to comply with workplace health and safety requirements
  
  • Failure to do so will result in fines to corporation and its directors

– *Environmental Protection Act* (Ontario) and Related Legislation
  
  • Directors required to take reasonable care to prevent unlawful discharge of contaminants

• Persons in control of contaminants are responsible for cleanup and related costs

• Appropriate environments audits need to be obtained before purchasing or receiving land

– *Child and Family Services Act* (Ontario)
  
  • Failure to report child abuse is an offence

  • A charitable corporation and its directors may be liable where employees fail to report abuse or where it occurs because of failure to monitor employees and operations
– *Trustee Act* (Ontario)
  
  - Act establishes that directors of charitable corporations have power and duty to invest assets of charity
  - Investments must be in accordance with prudent investor standard
  - See charity law bulletin #8 at www.charitylaw.ca

– *Charities Accounting Act* (Ontario)

  - Act gives rights to donor and Public Guardian and Trustee (PGT) to call directors to account for improper use of

Charitable property as well as fundraising practices

  - Co-mingling of donor restricted funds is permitted provided there is strict compliance with the act’s requirements

- Fundraising
  - Specific charitable statutes concerning fundraising
  - General statutes affecting charitable fundraising
DISCLAIMER

This handout is provided as an information service by Carter & Associates. It is current only as of the date of the handout and does not reflect subsequent changes in law. This handout is distributed with the understanding that it does not constitute legal advise or establish the solicitor/client relationship by way of any information contained herein. The contents are intended for general information purposes only and under no circumstances can be relied upon for legal decision-making. Readers are advised to consult with a qualified lawyer and obtain a written opinion concerning the specifics of their particular situation.
© 2003 Carter & Associates