APPENDIX B

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GOOD GOVERNANCE IN MEETING THE DUTIES OF DIRECTORS OF CHARITIES AND NOT-FOR-PROFITS

By Terrance S. Carter, B.A., LL.B. and
Theresa L.M. Man, B.Sc., M.Mus., LL.B.

A. INTRODUCTION

Various jurisdictions in Canada and the United States have been looking at developing tougher corporate governance laws since the collapse of Enron and Worldcom. Accountability requires good governance from the not-for-profit and charitable sector as much or more than in the for-profit sector. In the for-profit sector, corporations are primarily accountable to their shareholders for the ability of the corporation to return a profit. In the not-for-profit and charitable sector, however, organizations are accountable to their members as well as to the general public. This summary outline examines the role of good governance in achieving accountability to a not-for-profit and charitable corporation's members, stakeholders, and the public.

B. WHAT DOES "GOOD GOVERNANCE" MEAN?

1. <u>Governance is not the same as "Good Governance"</u>

- "Governance" in the voluntary sector means "the processes and structures that an organization uses to direct and manage its general operations and program activities "
- It includes the "structures, functions (responsibilities), processes (practices) and organizational traditions that the board of an organization uses to ensure accomplishment of the organizational mission"
- "Good Governance" means achieving desired results and achieving them in the right way, i.e. in ways that are consistent with the normative values of democracy and social justice

2. Characteristics of "Good Governance"

In 1997, the United Nations published a list of characteristics of good governance, which includes:

- Participation in decision making and reaching broad consensus on what is in the best interest of the organization
- Accountability and transparency
- Responsive, effective and efficient performance
- Equity and sound rule of law
- Strategic planning

3. Elements of "Good Governance "

(From M. Gill, "Governance Do's and Don'ts – Lessons from Case Studies on Twenty Canadian Non-Profits", Final Report, June 2001)

- Vision - envisioning the future and developing a corporate mission that will be flexible and responsive to possible future challenges and opportunities
- Direction - setting goals for the corporation
- Resources - securing resources to achieve the desired results and realize the corporation's vision and goals
- Monitoring - periodically reviewing the relationship between the corporation's resources and its vision and direction, ensuring that the organizational vehicle is well-maintained and progressing, within legal limits, towards its destination
- Accountability - ensuring efficient use of resources and reporting progress and detours to the corporation's stakeholders

C. HOW TO ACHIEVE GOOD GOVERNANCE

Good governance is the responsibility of the directors, who have the duty and power to manage the affairs of a corporation. The key for the directors achieving good governance is the exercise of due diligence. In order to exercise due diligence, directors must be familiar with and understand the governing documents of the corporation, its objects and activities, and its financial position. The directors must also understand the statutes, regulations and policies under which the corporation operates and be familiar with the regulators who have jurisdiction over the corporation. Good governance also includes being aware of and taking a pro-active approach in the following areas that are identified in a Report by the Panel on Accountability and

Governance in the Voluntary Sector, entitled "Building on Strength: Improving Governance and Accountability in Canada's Voluntary Sector", February 1999:

1. Mission and Strategic Planning

- Directors are responsible for developing and carrying out the mission of the corporation, which includes determining the organization's vision and direction as well as ensuring the availability of resources. In carrying out their duties, the directors must fulfill their duty to ensure that the corporation act within the authorized powers of the corporation.
- The organization's mission statement and organizational goals must be consistent with the law and within the corporation's authorized powers, including, but not limited to:
  - the letters patent of the corporation
  - the organization's constitution
  - the corporate by-laws
  - the organization's trust deed
  - federal and provincial legislation
  - other restrictions
- Directors should undertake a periodic review of the corporation's mission and strategic plan to ensure that they are compatible with the organization's vision, direction, and resources, as well as in compliance with the law.

2. Transparency and Communication

- Directors are responsible for communicating to members, stakeholders and the public about the affairs of the corporation.
- In order to ensure effective communication, the board should:
  - establish policies for communication and feedback
  - establish a code of ethics for the board
  - establish a complaint and grievance procedure
  - meet regularly
  - focus on ensuring accountability
  - keep proper minutes and corporate records
  - respond appropriately to requests for information
  - develop a privacy policy
- Effective communication from the board to its members, stakeholders and the public and the establishment of appropriate means for the latter to be heard will ensure the ability of the board to

respond to appropriately to issues that may arise and to evaluate the corporation's mission and goals.

3. Organizational Structures

- Directors must develop appropriate structures for the organization that will enable it to achieve its vision.
- Developing an organizational structure includes deciding whether to incorporate or to carry on as an unincorporated association.
- No single structure is appropriate for all organizations; each organization is different and its structure may change over time.
- Depending on what organizational structure is deemed appropriate, the directors must produce the documents which determine the organization's structure, objects and authority, such as:
  - letters patent
  - constitution
  - by-laws
- Directors must ensure the proper and legal approval of:
  - directors' resolutions
  - members' resolutions
  - external approvals, e.g. proper incorporation
- In order for the structure of an organization to be effective, the directors must develop proper and legal procedures for directors and members meetings
- A corporate audit committee is a useful and important means to help ensure that the directors' duty to comply with the statutory and common law are satisfied by reviewing the structure of the corporation at regular intervals and reporting on whether the organization is in compliance with the laws, rules, regulations etc., and whether the management, information and control systems are in place to carry out these laws.

4. The Role of the Board

- In addition to understanding the corporation's goals, structure, and activities, directors must understand the role of the board and their duties as directors
- Directors should develop a board governance policy and a code of conduct for board members to give the directors guidance for how to proceed under various circumstances that might arise and ways in which the directors may discharge their duties.
- The board should develop a conflict of interest policy to assist the directors to discharge their duty to avoid conflict of interests so that expectations of directors in the event of conflict of interest are clear both to the directors themselves, to members or other stakeholders, or to the public.

- Directors need to ensure their continuous education with regard to the activities of the corporation, relevant legislation, and the industry within which the organization operates.

5. Fiscal Responsibility

- Fiscal responsibility is a very important part of ensuring that a corporation can meet its goals and objectives.
- Even if management runs the day-to-day affairs of the corporation, the directors are ultimately responsible for establishing and maintaining fiscal responsibility in order that the directors may discharge their duty to manage and protect the assets of the organization.
- Directors must establish a budget, monitor and control expenditures, and maintain proper accounting books and records.
- Directors must prepare and audit the financial statements of the corporation.
- Directors must exercise proper management of the assets of the corporation, investing them appropriately if necessary.

6. Human Resources

- Directors should ensure that an effective management team is in place and providing oversight of human resources.
- Effective management of employees includes:
  - ensuring compliance with employment legislation and workplace safety regulations
  - establishing policies and procedures for the day-to-day operations of the corporation and for certain extraordinary circumstances that might arise
- Effective management of volunteers involves establishing policies for recruitment and supervision of volunteers, and especially screening potential volunteers.

7. Implementing Assessment and Control Systems

- Directors should establish a framework of internal regulation, including a code of ethical conduct and policies on various areas of concern, to give management and employees guidance on how to handle issues that might arise. This would assist the directors to fulfill a number of their duties, such as the duty of honesty, the duty of loyalty, and the duty to act in the best interests of the organization etc.
- Establishing periodic review and audit procedures for the corporations, policies and assessment and control systems will enable a pro-active approach to emerging issues and challenges or to changes in the legislative or operating environment of the corporation.
- Establishing an audit committee.
- Establishing legal risk management procedures.
- Establishing a legal risk management committee.

8. Planning for the Succession and Diversity of the Board

- One of the main benefits of incorporation is longevity; a corporation is not contingent on the availability or capacity of its members.
- In appointing new directors it is important to ensure the diversity of the board, making sure that the directors bring a variety of useful and relevant expertise to the operations of the corporation.
- New directors need to be given appropriate orientation to the organization and its governing documents, structure, and activities, as well as the duties of directors.
- Existing directors need to be continually reminded of their duties, as well as to keep up-to-date with changes in the law that is relevant to the operations and governance of the organization.

For more information and resource materials on Director Liability and Legal Risk Management see:

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Main Office Location
211 Broadway, P.O. Box 440
Orangeville, ON, Canada, L9W 1K4
Tel: (519) 942-0001
Fax: (519) 942-0300
Toll Free: 1-877-942-0001
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Toronto (416) 675-3766
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