UNITED WAY/CENTRAIDE
Windsor – Essex County
DIRECTOR AND OFFICER LIABILITY AND BEYOND

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Part IV
How to Avoid Liability in Fundraising

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A. RESOURCE MATERIALS

- **www.charitylaw.ca**
  - **Article entitled *"Looking a Gift Horse in the Mouth - Avoiding Legal Liability in Fundraising"***
  - **Article entitled *"Donor Restricted Charitable Gifts Revisited: A Practical Overview"***
  - **Article entitled *"Recent Changes to the Income Tax Act Affecting Charities"***
  - **Charity Law Bulletins #8, #9, #13, #17, #21, #23, #35, #40, #41, #54, #55, #56, #59 and #61**
- **www.antiterrorismlaw.ca**
  - **Article entitled *"Charities and Compliance with Anti-terrorism Legislation: The Shadow of the Law"***

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B. LEGAL RESPONSIBILITY OF CHARITIES AND DIRECTORS IN FUNDRAISING

- **Improper or negligent actions by development officers or fundraisers may expose a charity and its directors to legal liability**
- **The court held in *The Aids Society for Children* (Ontario) that**
  - **Third party fundraisers and subcontractors are agents of the charity and may cause liability for both the charity and its board of directors personally**

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- **Fundraising contracts which provide for unreasonable compensation 70% to 80% will be void able based upon both violation of public policy and/or misrepresentation**
- **Misrepresentation is determined by the perception of the donor, not by the intent of the charity or its directors in receiving the gifts**
- **The fiduciary duty of a charity and its board of directors to account for donations applies to the gross amount of donations raised by third party fundraisers, not to the net amount that the charity may be entitled to pursuant to a fundraising contract**

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- **The directors were found personally liable for unreasonable fundraising costs in the amount of $766,000**
- **Fundraising companies were required to repay unreasonable fundraising costs**
- **The directors were subjected to a penalty of $50,000.00 under the *Charities Accounting Act* (Ontario)**

• **The court in *National Society for Abused Women and Children* confirmed**

- **Fiduciary obligation of directors to account for unconscionable fundraising costs**

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- – **Fundraising contract was declared void *abinitio* as being contrary to public policy**
- – **Donors are entitled to know about fundraising and administrative costs when making donations**

- **For more information on these cases, see Charity Law Bulletins #9, #13 and #17 at www.charitylaw.ca**
- **The "buck" stops with the board of directors of a charity after everyone else has left the charity**
- **The board of directors must therefore be made familiar with all fundraising programs and the liabilities that are associated with those programs**

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C. DEVELOPING A PROACTIVE RISK MANAGEMENT APPROACH TO FUNDRAISING

- **Legal liability in fundraising can be reduced by developing a proactive legal risk management approach to fundraising**
- **Fundraising must comply with the applicable corporate objects and powers of the charity**
  - – **The fundraising program must not be *ultra vires* the charitable objects of the charity**
  - – **The charitable purpose being furthered by fundraising must not be *ultra vires* the charitable objects**
  - – **A donor restricted gift resulting from fundraising must not be *ultra vires* the charitable objects**

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- Fundraising must not violate applicable statutory provisions
- Fundraising must not involve gifts that are contrary to public policy
  - Charitable gifts involving discrimination
  - Charitable gifts involving illegal activities

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D. DONOR'S RIGHTS AND REMEDIES IN FUNDRAISING

- General exposure to liability involving donors
  - Misrepresentation involving issuance of charitable receipts and/or the amount
  - Failure to comply with donor restrictions
  - Failure to disclose excessive fundraising costs
  - Detrimental reliance upon charitable endorsements
  - Detrimental reliance upon improper tax advice involving donations
  - Breach of fiduciary duty and/or breach of trust in applying funds to charitable purposes

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- **Donor's statutory rights**
  - ***Charities Accounting Act* (Ontario)**
    - **Section 6 of the CAA (public inquiry)**
    - **Section 10 of the CAA (alleged breach of trust)**
    - **Section 4(d) of the CAA (noncompliance with donor directions)**
    - **Section 3 of the CAA (formal passing of accounts)**
  - **The *Income Tax Act* (Canada)**
    - **Informal complaint to CRA**
    - **Resulting audits**
    - **Receipting and disbursement violations**

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E. AVOIDING LIABILITY FROM TESTAMENTARY CHARITABLE GIFTS

- **Reducing legal risks from estate planning programs**
  - **Shift the legal risk away from the charity**
    - **Download the risk to professionals, i.e. accountants or lawyers, to establish evidence of due diligence**
    - **Raise the shield of liability insurance whenever possible, if available**
    - **Return any original wills or codicils to donors or their lawyers**

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– **Avoid circumstances conducive to allegations of undue influence**
  - **Directing work to a particular lawyer**
  - **Paying for a portion of donor's legal costs**
  - **Acting as either an estate trustee (executor) or attorney under a power of attorney**
  - **Preparing a will or power of attorney**
  - **Providing advice on how to structure disposition clauses in a will**
  - **Providing recommendations on how much of the estate should be given to a charity or charities in general**

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  - **Completing the will guide on behalf of the testator instead of only assisting with background information**
  - **Meeting with the lawyer when the donor gives instructions for the will**
  - **Being present when the will is being signed**
  - **Offering to store the original will, codicil to a will, or power of attorney**

- **Managing testamentary gifts**
  – **Ensure that a copy of the will is received and carefully review charitable gift provisions**
  – **Review any applicable donor restrictions before agreeing to receive the gift**

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- Require progress reports on the administration of an estate
- Request the distribution of gifts to the estate at the earliest opportunity
- Have legal counsel review estate releases as the charity cannot sign an indemnity for money or cause of action beyond what the estate would have otherwise been liable for
- Have legal counsel review estate accounts before signing estate releases
- Review appropriateness of investments
- Ensure that tax credits are used against 100% of income in the year of death and carried back one year, if applicable

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- Make sure that only duly authorized signing officers execute the releases

- Resist voluntarily renouncement of a gift
  - A charity may be asked to renounce a testamentary gift in situations of financial hardship involving family members of the deceased
  - There is no legal authority for a charity to unilaterally renounce a gift
  - Even court authorization for a renunciation of a testamentary gift is unlikely
  - The charity therefore has a fiduciary obligation to pursue testamentary gifts
- Ensure that testamentary gifts continue to honour outstanding pledges

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F. AVOIDING LIABILITY FROM DONOR RESTRICTED CHARITABLE GIFTS

- **The difference between unrestricted and donor restricted charitable gifts**
  - **What is an unrestricted charitable gift?**
    - **An unrestricted charitable gift is a gift to the charity that is not subject to any restrictions or limitations**
  - **What is a donor restricted charitable gift?**
    - **A donor restricted charitable gift that is a gift subject to binding restrictions, conditions or limitations**

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- **Instances of breach of trust involving donor restricted charitable gifts**
  - **Diverting a fund to another application**
  - **Withholding a fund**
  - **Pooling restricted funds with funds of another donor**
  - **Encroaching on the capital of an endowment fund**
  - **Altering the terms of a trust deed**
  - **Borrowing from a restricted fund**
  - **Using surplus funds from a fundraising appeal for a different purpose**

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- **Altering terms of a donor restricted fund without court authorization**

- **Can a donor restriction be unilaterally varied?**
  - **Only a court can vary a donor restricted charitable gift on a *cyprés* application**
- **How should donor restricted gifts be managed once received?**
  - **Identify the nature of the charitable gift**
  - **Review and approve donor restrictions**

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- **Effective ongoing management of donor restricted charitable gifts**
  - **Deposit into the bank account of the named charity**
  - **Invest fund in accordance with applicable investment power**
  - **Do not borrow against restricted fund**
  - **Commingle restricted funds only in accordance with regulations in Ontario and not with general funds**

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- **How can donor restricted charitable gifts be avoided in the first instance?**
  - **Encourage unrestricted gifts**
  - **Alternatively encourage the use of non-binding directions**
  - **Advise donors that all gifts are deemed to be unrestricted unless specifically stated otherwise**

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- **Preventative steps to reduce liability involving donor restricted charitable gifts**
  - **Public fundraising appeals should state that any surplus funds will be used for the general charitable purposes of the charity**
  - **Ensure that donor restricted gift includes a *cyprés* clause that will allow the charity to amend the purpose**
  - **Ensure that documentation creating donor restricted charitable trusts include the words "in trust"**

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- **Protecting donor restricted charitable gifts**
  - **Impact of the Christian Brothers Ont. Court of Appeal decision**
    - **Claims against charities may increase**
    - **Special purpose trust endowments will be at risk to creditors of the charity**
    - **The ability of donors to create enforceable restricted gifts will be weakened**
    - **Donors will be reluctant to give large gifts directly to an operating charity**

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  - **Developing a strategy in response**
    - **Utilize an arms length parallel foundation**
    - **Utilize a community foundation or trust company**
    - **Structure gift as a determinative gift with a gift over to another charity**
    - **For more information see www.charitylaw.ca article on "*Donor Restricted Charitable Gifts Revisited: A Practical Overview*"**
  - **Proposed legislation in B.C. (Bill 63) to protect special purpose charities trusts**

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- **Comparison to conditional gifts**
  - **What is the nature of a conditional gift?**
    - **A conditional gift involves the charity becoming the beneficial owner of the gift subject to being defeated by a condition**
    - **With a special purpose charitable trust, the charity never becomes the beneficial owner of the gift but instead holds it in trust**
  - **Receipting conditional gifts**
    - **Condition precedent gifts cannot be receipted**
    - **Condition subsequent gifts may be receiptable:**
      - **Reversion to donor precludes receipting**
      - **Reversion to another charity can likely be receipted**

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G. AVOIDING LIABILITY IN GIFT AND FUNDRAISING PROGRAMS

- **Gifts of Shares**
  - **Gift of shares or interests in a business will be subjected to the *Charitable Gifts Act* (Ontario)**
    - **Charities can not own more than a 10% interest in a business for longer than 7 years**
    - **If a charity owns more than a 50% interest in a business then reporting requirements to P.G.T. apply**
  - **Potential liability in relation to improper valuing and receipting of shares of publicly traded companies**

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- **Need to review CRA position on determining fair market value**
- **Need to review factors outlined by CRA in valuing shares as set out in Registered Charity Newsletter No. 12**

- **Gifts of real estate**
  - **Three year restriction on leasing property under the *Charities Accounting Act* (Ontario)**
  - **Forty year restriction on leasing property under the *Religious Organization Land Act***
  - **Liability for toxic property and need for environmental assessment**
  - **Need for due diligence searches**
  - **Inability of charity to manage real property**

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- **Receiving used "gifts in kind"**
  - **Need for appraised fair market value**
  - **Potential liability to third parties from using recycled property**
- **Self insured gift annuities**
  - **The difference between self insured and reinsured gift annuities**
    - **Self insured gift annuity**
    - **Reinsured gift annuity**
  - **Legal risks associated with self insured annuities**
    - **Lack of corporate authority**

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- Possible violation of the *Insurance Act* (Ont)
- Operational financial risks
- Restrictions on foundations issuing annuities

- Debt instruments forgivable on death
  - Need testamentary instrument to forgive debt
  - If not properly forgiven, will become an asset owing to the estate
- Bill C-45 Amendments to the Criminal Code (Westray Mines)
  - In effect criminalizes situations which previously were only matters of gross negligence

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  - Charities, directors and officers may be exposed to personal liability
  - insurance may not be available for defence costs
  - See Charity Law Bulletin #35 at www.charitylaw.ca for more details
- Transferring capital funds between charities
  - Ensure that there are charitable objects to permit the transfer of funds
  - Identify donor restricted charitable gifts
  - Identify impossible or impractical donor restrictions
  - Change of trustees by deed of trust
  - Unrestricted funds to be applied for original charitable purpose

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- **Investment issues in fundraising**
  - **Determine which investment powers apply and in what jurisdiction**
  - **Adapt and implement an investment plan**
  - **Investment plan needs to comply with *Trustee Act* (Ontario) particularly for delegation**
  - **Investment plan needs to incorporate and override the investment plan and/or agency agreement of an investment manager**
  - **See www.charitylaw.ca, Charity Law Bulletin #8 and "Looking a Gift Horse in the Mouth Avoiding Liability in Charitable Fundraising" article for more information**

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- **Managed or pooled investment of charitable funds**
  - **Does the recipient charity have the corporate power to operate a pooled fund?**
  - **Does the investment power of each participating charity permit it to invest charitable monies by pooling monies with a third party?**
  - **Does the *Loan and Trust Corporations Act* (Ontario) have application?**
  - **Does the *Securities Act* (Ontario) have application?**
  - **Is court authorization required to pool investment funds of various charities?**

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- **Federal *Competition Act* - Deceptive telemarketing & false or misleading misrepresentation**
  - **Definition of "business" includes the raising of funds for charitable or other non-profit purposes**
  - **The *Competition Act* does not apply to fundraising that is solely charitable in purpose**
  - **However, if the part of the purpose of the fundraising includes promoting products or services, the *Competition Act* may apply**
  - **Telemarketing is prohibited unless there is statutorily mandated disclosure**
  - **Violation of the *Competitions Act* constitutes a criminal offence**

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- **A due diligence defence is available**
- **Directors and officers of a charity can be held personally liable**
- **The prohibition on false or misleading representation applies to telemarketing, door-to-door solicitation, and items offered for sale by the charity**
- **A false or misleading representation does not require that it be proven that any person was deceived or mislead**

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- **Legal issues involving fundraising on the internet**
  - **Territorial jurisdictional issues**
  - **Intellectual property law issues**
  - **Potential for civil action from the internet**
  - **Domain names, trade-marks and the internet**
  - **Marketing and advertising on the internet**
  - **PIPEDA and provincial privacy legislation**

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- **Legal issues in sponsorship arrangements**
  - **Distinguishing between receiptable donations and non-receiptable sponsorship payments**
  - **The importance of documenting sponsorship arrangements**
  - **Protecting and licensing trade-marks in sponsorship arrangements**
  - **Liability exposure from sponsorship arrangements**

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- **Fundraising Liability and Anti-terrorism**
  - **Anti-terrorism Legislation is very complicated, see www.antiterrorismlaw.ca for article *"Charities and Compliance with Anti-terrorism Legislation: The Shadow of the Law"***
  - **Charity and its directors need to have a working knowledge of the anti-terrorism legislation in making a gift to charity**

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- **Even gifts that unintentionally end up in the wrong hands through agents of the charity can violate anti-terrorism legislation and create exposure to liability for the charity and its board**
- **A charity could lose its charitable status**
- **Directors, donors and fundraisers could be found personally liable**
- **Need to develop a due diligence checklist to avoid unintentional violations of the legislation**
- **However, anti-terrorism legislation generally involves strict liability legislation so due diligence is not necessarily a defence**

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