
WILD ROSE FOUNDATION – VITALIZE 2008

**DIRECTOR’S AND OFFICER’S LIABILITY:
THE ESSENTIALS AND BEYOND
FOR CHARITIES AND NONPROFITS**

Edmonton – June 13, 2008

Part I
**The Legal Duties of Directors and Officers
of Charities and Not-for-Profits (Alberta)**

By Terrance s. Carter, B.A., LL.B., Trade-Mark Agent

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A. OVERVIEW OF TOPICS

- Definition of Director and Officer
- Different Types of Corporations
- Common Law Duties and Liabilities
- Statutory Duties and Liabilities

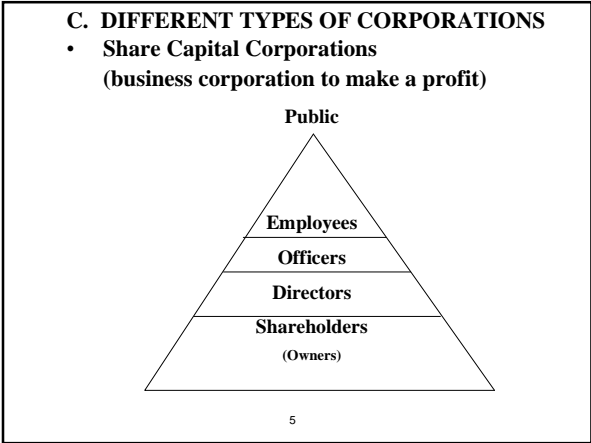
Note: For a more detailed discussion, see
Summary "A" entitled "The Legal Duties
of Directors of Charities and Not-for-Profits
(Alberta)" available at
<http://www.carters.ca/pub/article/charity/2008/tsc0613a.pdf>

B. DEFINITION OF DIRECTOR AND
OFFICER

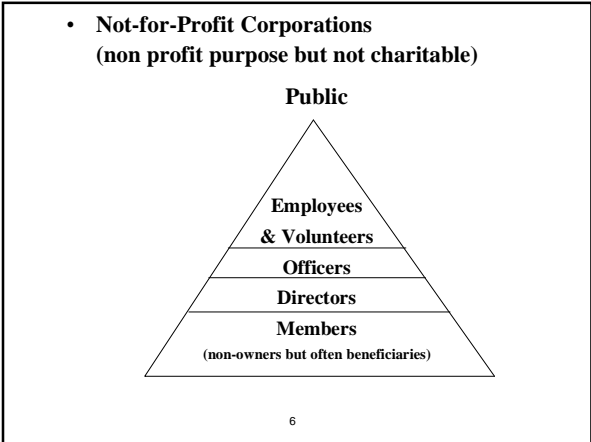
- For this presentation, references to
corporation include an unincorporated
association, a corporation and a trust
- A director is generally anyone who takes on
the role of the directing mind of a corporation
- A director can be known as a trustee,
governor, board member, or even an elder or
deacon of a religious organization

- An officer carries out the day to day functions of the corporation at the direction of the board
- An officer can also be a director or can become a *de facto* director and be subject to fiduciary obligations
- For purposes of this presentation, reference to director is deemed to include officer unless stated otherwise

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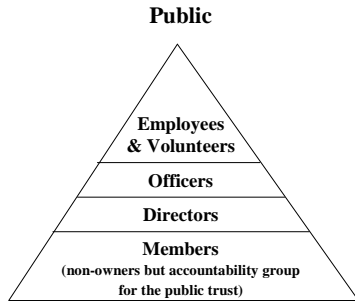


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- **Charitable Corporations**
(charitable purpose akin to a public trust)



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D. COMMON LAW DUTIES AND LIABILITIES

- **Management of the Corporation**
 - Directors are responsible for all aspects of corporation's operations on a joint and several basis
 - To fulfill duties, directors must ensure:
 - Objects are properly carried out and activities comply with objects
 - Corporation's financial stability and overall performance
 - Proper hiring and supervision of management and staff
 - Failure to act, i.e. inaction, can result in personal exposure to liability, i.e. liability of WorldCom and Enron directors

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- **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

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- **Not-for-profit corporation (non-charity)**
 - Common law subjective standard of care
 - Director’s own knowledge and experience important
- **Charitable corporation**
 - Ontario case law states that directors of charitable corporations are subject to fiduciary duties as quasi trustees of charitable property
 - This is not currently the law of Alberta, although reform in this area has recently been considered by the Alberta Law Reform Institute

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- **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

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- **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 or inaction 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

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• **Liability Risk for Breach of Fiduciary Duty**

– **Overview**

- **Directors of both not-for-profit and charitable corporations have fiduciary duties to put the interest of the corporation ahead of their own interest**
- **Fiduciary duties are owed to corporate objects, the corporation itself, donors, members and creditors**
- **Ontario case law has found that directors of charitable corporations are subject to fiduciary duty to act as quasi trustees of charitable property**

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– **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 the corporation**

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▪ **Duty of diligence/duty to act in good faith**

- **Directors to diligently attend to duties by being familiar with all aspects of corporation**
- **Directors may have liability exposure at common law for failure to attend to their legal duties or those of the corporation**
- **Where necessary, advice of qualified professionals should be sought**

▪ **Duty to exercise power**

- **Directors responsible for managing corporation**

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- Delegation to management, staff and volunteers is possible, but directors must always supervise
- Duty of obedience
 - Directors must comply with applicable legislation and the corporation's governing documents
 - All valid corporate decisions must be implemented

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- 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 from the board
 - In Ontario, directors of charitable corporations cannot receive any remuneration from a charitable corporation, directly or indirectly, without court approval

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- 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

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- **Liability for Breach of Trust**
 - **Overview**
 - Ontario case law has generally held that directors will be bound by trustee standards in dealing with charitable property
 - The *Companies Act* (Alberta) and the *Societies Act* (Alberta) are silent on this issue, and it has not been tested in an Alberta court
 - But if a donor makes a restricted gift (i.e. a gift restricted for a specific use) to a charitable corporation in Alberta, a trust may be found
 - Directors would then become trustees of the gift and would need to abide by the principles of trust law, including the *Trustee Act* (Alberta)

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- **Potential liability risks for directors as trustees**
 - **Remuneration of directors**
 - In Ontario, directors of charitable corporations cannot receive direct or indirect remuneration from the charity, e.g. as an employee or contractor, without court approval
 - As well, in Ontario, corporate indemnification of directors and officers can be given and director and officer insurance can be obtained, provided that regulations under the *Charities Accounting Act* (Ontario) are complied with
 - There is no case law on this issue in Alberta

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- **Dealing with charitable property**
 - Directors responsible for handling of charitable property
 - Personal liability results where mismanagement occurs
- **Dealing with charitable objects**
 - Charitable property can only be applied to charitable objects
 - Failure to properly apply charitable property may result in personal liability

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- **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 have a duty to invest charitable property
 - *Trustee Act* (Alberta) may apply

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- Liability can result from failure to comply with investment powers as well as bad investments, overly conservative decisions and missed opportunities
- **Commingling of donor restricted funds**
 - Are gifts subject to restrictions or limitations?
 - Gifts which are subject to restrictions or limitations at common law should not be commingled and may need to be kept separate from both one another and general funds
 - Compare to recent regulations under the *Charities Accounting Act* (Ontario) that permit commingling

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- E. 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 at common law is due diligence
 - Resigning as a director may not limit liability though there are generally limitation periods

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• **Federal Statutes**

– *Canada Corporations Act*

- **Wages and vacation pay (s.99, 204)**
- **Conflict of interest (s. 98, 49)**
- **Reporting requirements (s. 133)**
- **Books, minutes and records (ss. 109, 112, 113, 117)**
- **Identification of corporation (s. 27)**
- **Membership lists (s. 111.1)**
- **Winding up (s. 150)**
- **General penalty (s. 149)**

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– *Income Tax Act (Canada)*

- **Directors jointly and severally liable to pay employee income tax deductions for two years after term of office (s. 227.1)**
- **Directors may be personally liable if charity fails to comply with numerous reporting requirements, e.g. annual charity information return, improper charitable receipts, or giving improper tax advice (s. 238)**
- **Directors may also face fines and imprisonment if they are involved in making false or deceptive statements or evading compliance with the *Income Tax Act* (s. 239)**
- **Avoid liability by showing positive steps taken to ensure compliance**

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– *Excise Tax Act (Canada)*

- **Directors jointly and severally liable for corporation’s failure to collect & remit GST (s. 323)**
- **Due diligence defence**
- **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 (s. 21.1)**

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– *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 (s. 280.1)
- Failure to comply could result in prison terms and fines (s. 280)

– *Anti-terrorism Legislation*

- Legislation has serious liability risks for charitable corporations and directors, particularly those involved in overseas work

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- Risks include seizure of charitable property, loss of charitable status and *Criminal Code* charges
- See www.antiterrorismlaw.ca

– *Criminal Code*

- Bill C-45 (Westray Mines) for negligence in work place safety
- Section 336 – criminal breach of trust

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- Alberta Statutes
 - *Companies Act* (Alberta)
 - Wages (s. 91)
 - Directors jointly and severally liable to clerks, labourers, servants and apprentices for all debts for services performed for the company during the period they were directors
 - Maximum of 6 months wages
 - Reporting requirements (see ss. 66, 69(3), 93, 94, 98).
 - Conflict of interest (s. 92)
 - General offence provision (s. 313)
 - Residency requirements (s. 90)

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– *Societies Act (Alberta)*

- Does not specifically address issues of director’s and officer’s liability

– *Workers Compensation Act (Alberta)*

- Directors are not liable for corporation’s failure to remit premiums unless it can be shown they did not intend to pay them (s. 152.01)

– *Employment Pension Plans Act (Alberta)*

- Directors who fail to pay corporation premiums for employee’s pension plans and to hold monies in trust may be found guilty of an offense and liable to a penalty (s. 92(3))

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– *Health Insurance Premiums Act (Alberta)*

- Directors can be liable to a penalty if they directed, authorized, assented to, acquiesced in or participated in the failure or refusal to remit payment of a premium the Corporation was liable to remit (s. 16)

– *Occupational Health and Safety Act (Alberta)*

- Only directors assigned the task of overseeing occupational health and safety are liable to a penalty if the corporation fails to comply with workplace health and safety requirements (s. 1(k)(iv),(u); s. 2)

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– *Environmental Protection and Enhancement Act (Alberta)*

- Directors can be found liable to penalty if they permit the contravention of various environmental protection measures the corporation is required to meet (s. 232)

– *Human Rights, Citizenship and Multiculturalism Act (Alberta)*

- Allowing interference with administration of Human Rights Commission can cause liability of directors (s. 42(3))

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– *Trustee Act (Alberta)*

- Act establishes that directors of charitable corporations, where found to be trustees, are subject to certain powers and duties in investing assets of the charity
- Investments must be in accordance with prudent investor standard and comply with the Act’s description of the power and duty to invest (s. 3, s. 4)
- See Charity Law Bulletin #8 at <http://www.carters.ca/pub/bulletin/charity/2001/chylb08-01.pdf> for discussion of the comparable Ontario statutory provisions

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• Fundraising

– *Charitable Fund-Raising Act (Alberta)*

- Directors may be liable to return improperly used funds to donors (s. 53)
- Directors are required to make sure employees who are responsible for solicitations comply with fundraising standards of practice and requirements of the Act (s. 32)

– Other specific charitable statutes concerning fundraising:

- *Income Tax Act (Canada)*
- *Charities Accounting Act (Ontario)*

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- *Charitable Gifts Act (Ontario)*
- *Religious Organizations’ Lands Act (Ontario)*
- *Charitable Purposes Preservation Act*
- *Charitable Fund-raising Businesses Act (Saskatchewan)*
- *Charities Endorsement Act (Manitoba)*
- *Charities Act (Prince Edward Island)*
- Proposed ULCC *Uniform Charitable Fundraising Act* see Charity Law Bulletin #79 at <http://www.carters.ca/pub/bulletin/charity/2005/chylb79.pdf>

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– General statutes affecting charitable fundraising:

- *Competition Act (Canada)*
- *Privacy Act (Canada)*
- *Insurance Act (Alberta)*
- *Loan and Trust Corporations Act (Alberta)*
- *Securities Act (Alberta)*
- *Trustee Act (Alberta)*

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