
THE HAMILTON LAW ASSOCIATION
Continuing Legal Education Committee

“Charity Law”

Hamilton – June 2, 2010

Advising the Charitable Client

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A. OVERVIEW

- The Significance of Charities and Charity Law
- The Fundamentals of a Charity
- The Fundamentals of a Not-for-Profit Organization
- The Challenge in Advising the Charitable Client
- Minimizing the Lawyer’s Exposure to Risk
- Strategies to Address Those Risks
- Developing a Legal Risk Management Checklist

Note: For more details see articles and newsletters at www.charitylaw.ca

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B. THE SIGNIFICANCE OF CHARITIES AND CHARITY LAW

- Statistics Canada published *Caring Canadians, Involved Canadians: Highlights from the 2007 Canada Survey of Giving, Volunteering and Participating* in June 2009
- In the twelve-month period covered, 84% of the population made a financial donation to a charitable or non-profit organization
- In 2007, charitable giving increased from previous years to \$10 billion
- Most lawyers advise charities on an infrequent basis and often do so for reduced fees or on a *pro bono* basis

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- Advising charities, however, is now a very complicated area of the law and is becoming more so all the time
- Charities are facing fundamental changes and challenges, particularly in a more litigious society
- Charities need to rely on legal advice more than they have in the past
- Lawyers must provide professional and competent advice no matter what the fee charged is
- Lawyers need to have a more active mind-set in identifying problems and providing legal advice to charitable clients
- Legal advice needs to change from benign passivity to proactive legal risk management

- C. THE FUNDAMENTALS OF A CHARITY**
- What is a charity?
 - At common-law (the *Pemsel Test*) includes
 - Relief of poverty
 - Advancement of education
 - Advancement of religion
 - Other purposes beneficial to the community as recognized by the courts

- Under the *Charities Accounting Act* – “charitable purpose” is defined
 - It codifies the common law definition of what is a charity
 - Definition does not extend to broader definition under the *Income Tax Act* (“ITA”)
- Under the ITA– “qualified donee” concept introduced
 - Includes a “registered charity”
 - Defined as “charitable organization”, “public foundation” and “private foundation”

- No definition of a “charity” but reflects the common law
- Includes extended statutory list of “qualified donees”
 - Registered Canadian amateur athletics associations
 - Low-cost housing co-operatives for the aged
 - Municipalities
 - United Nations
 - Prescribed universities
 - Charitable organizations outside Canada to which the government has made a gift in the last 12 months
 - Her Majesty in right of Canada or a province

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- What are the tax advantages of being a charity?
 - A charity does not pay tax on income or capital gains
 - A charity can issue charitable receipts to donors as tax credits for income tax purposes
 - A gift for income tax purposes can now include consideration to donor (“split-receipting”)
- What are the legal forms available for a charity?
 - Unincorporated associations
 - Charitable trusts
 - Non-share capital corporations

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- D. THE FUNDAMENTALS OF A NOT-FOR-PROFIT ORGANIZATION**
- Under the ITA a not-for-profit is defined as a non-profit organization
 - What is a non-profit organization under the ITA?
 - Club, society or association
 - Must **not** be a charity
 - Organized and operated exclusively for social welfare, civic improvement, pleasure or recreation, or any other purpose, except profit
 - No part of the income can be payable or available to any proprietor, member or shareholder

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- CRA has indicated that, “profit should generally be unanticipated and incidental to the purpose or purposes of the organization”
- CRA has cautioned that retaining excess funds beyond immediate operating costs may be evidence that an organization is operating with a profit purpose, but, “this will not in and of itself result in the organization failing to qualify as a 149(1)(l) entity”
- Therefore, non-profits must carefully justify any excess surplus as this could put them in danger of losing non-profit status

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- What are the tax advantages of being a non-profit organization?
 - A non-profit organization does not pay tax on income or capital gains, except income from property of an organization whose main purpose is to provide dining, recreation or sporting facilities
 - A non-profit organization cannot issue charitable receipts for income tax purposes

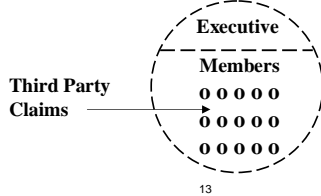
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- What are the legal forms available for not-for-profit organizations?
 - Unincorporated associations
 - Non-share capital corporations
- It is up to CRA to determine whether or not a non-share capital corporation or an unincorporated association qualifies as a nonprofit organization under subsection 149(1)(l) of the ITA
- Examples would include
 - Recreational clubs
 - Service clubs
 - Trade associations
 - Professional associations

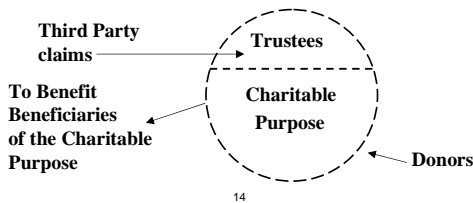
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E. THE CHOICE OF ORGANIZATIONAL STRUCTURE

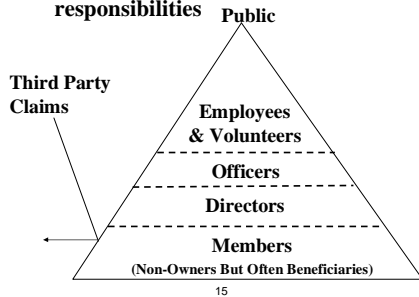
- Charities and Not-for-Profits as Unincorporated Associations
 - Not a legal entity
 - Generally used for starting up a charity or not-for profit in its early stages
 - Flow through liability to members



- Charities as Charitable Trusts
 - A trust is a relationship between trustees and beneficiaries involving the separation of legal and beneficial ownership of property
 - Available for charitable organizations, public foundations and private foundations
 - Trustees are exposed to liability



- Charities and Not-for-Profits as Corporations
 - Separate legal entities
 - Members are not exposed to liability
 - Directors may be still exposed to personal liability from fiduciary and management responsibilities



F. THE CHALLENGE IN ADVISING THE CHARITABLE CLIENT

- **The nature of the charitable client**
 - Motivated by a sense of the greater good
 - Inherent lack of continuity, i.e. frequent change in directors and executive staff
 - Varied extent of commitment by volunteers
 - Frequently internal differences of opinion in how to structure and operate the charity
 - Generally feel thwarted by legal process and the need to comply with the law

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- General lack of understanding of legal requirements by directors and executive staff
- Generally focus on programs and fundraising over compliance with legal requirements
- Generally a lack of understanding of the exposure of directors and officers to personal liability
- Frequently there is an unrealistic expectation of the lawyer by the charitable client
 - Lawyers may be expected to provide complicated legal services *pro bono* or at significantly reduced rates

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- Reduced fees or *pro bono* service does not justify incomplete legal advice
- Lawyer's involvement in even small matters is often seen as the legal seal of approval on everything that a charity does
- Lawyers may be susceptible to accountability in not having warned the client of potential risks
- Why the charitable client often experiences difficulties
 - The need to comply with complicated statutory requirements both federally and provincially

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- Increased exposure of directors and officers to liability arising from a more litigious environment
- Complicated tax issues, particularly with recent technical changes to the ITA
- Fundraising requirements both federally and provincially
- Complicated management of gifts and compliance with receipting requirements
- Inherent risks in operations, such as sexual abuse of children
- Compliance with requirements under anti-terrorism legislation

- Determining appropriate investment policies involving charitable funds
- Complicated organizational structures
- Interrelationships between multiple corporations
- Employment issues involving full and part time staff
- Privacy issues
- Lack of adequate contractual documents

- Consequences of legal deficiencies in charitable structure and operations
 - Legal actions by donors and/or the Public Guardian and Trustee
 - Allegations of breach of trust
 - Revocation of charitable status
 - Confusion in corporate operations
 - Loss of corporate status
 - Undertaking *ultra vires* activities
 - Court supervised audit of accounts
 - Inquiries under *Charities Accounting Act*

- **How the lawyer can encounter difficulties in advising the charitable client**
 - Charities often do not know what questions to ask, let alone the answers
 - Lawyers must fully explain the legal process to the charitable client
 - Lawyer must warn the charity of applicable risks
 - Lawyer must advise if there are better alternatives available
 - Lawyer must advise charitable client on related risks notwithstanding limited nature of retainer

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- **Conflicts of interest for lawyers in advising the charitable client**
 - If a lawyer is a member of the board of a charity, the lawyer cannot receive fees
 - Lawyers who are members of a board may face conflict if called upon to provide legal advice to the charity
 - Acting as solicitor for two related charities
 - Lawyer acting for a charity cannot advise directors of that charity personally
 - May need to communicate with board members directly where executive director is blocking communication from the lawyer

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- G. MINIMIZING THE LAWYER'S EXPOSURE TO RISK**
- Need to develop a preventative proactive response
 - Lawyer must be more than a legal technician
 - Must change from giving passive advice that is reactive only to proactive advice given in a preventative context
 - Need to identify and avoid legal problems before they occur

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H. STRATEGIES TO ADDRESS THOSE RISKS

- **Lawyer must be familiar with many aspects of the law in order to advise charitable clients of all applicable legal issues**
 - **Federal and Provincial Tax Issues**
 - **Corporate matters**
 - **Trust issues**
 - **Contracts**
 - **Risk management**
 - **International relationships**
 - **Intellectual Property**

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- **Lawyers also need to be familiar with change in the law. For example in the past year there have been significant changes:**
 - **i.e. *Canada Not-for-Profit Corporations Act***
 - **i.e. *Ontario Not-for-Profit Corporations Act***
 - **March 2010 Federal Budget and DQ Reform**
 - **Ontario Bill 212**
- **Lawyer should assume that the charitable client knows little about charity law**

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- **Lawyer must be diligent in asking questions of the charitable client**
- **Lawyer needs to explain the relevant law to the client in order to avoid problems in the future**
- **Lawyer needs to fully explain consequences of intended course of action and alternatives**
- **Lawyer needs to provide recommendations to rectify the problems identified**

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- Lawyer needs to provide a prioritization of action items to be undertaken, in an organized report to the client even if it is only in point form
- The onus to respond or take action should be clearly placed on the client
- Lawyer needs to provide explanation of steps that need to be taken and time frame to do so
- Lawyer should try to follow up with client, particularly where there is a change of staff or board members

- I. DEVELOPING A LEGAL RISK MANAGEMENT CHECKLIST**
- Checklist helps to keep track of a multitude of legal issues
 - Assists clients in understanding the interrelationship between legal issues
 - Helps to identify and focus on problem areas to be addressed

- See attached Risk Management Checklist as a sample
- How to utilize a checklist
 - Provide a copy of a checklist to the client and retain a file copy
 - Keep notes on the checklist
 - Provide a report and review of the checklist
 - Hold subsequent meeting with client to follow up on the checklist

J. EFFECTIVELY COMMUNICATING WITH THE CHARITABLE CLIENT

- **Written report to charitable client is essential**
 - The collective memory of a charitable client can quickly lapse because a charity is an institution with changing stakeholders
 - e.g. frequent change of executive staff and/or directors
 - e.g. poor record keeping by the charity
- **Confirm retainer with charitable client**
 - What the lawyer is doing for the client
 - What the lawyer is not doing for the client

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- **Report to client should be of an educational nature**
 - Explain issues to be addressed
 - Explain law and application to facts
- **Document advice given to charitable client**
 - Identify who the advice is being given to
 - Confirm any verbal advice given
 - Set out steps to remedy problems
 - Explain areas of uncertainties

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- **Provide proactive action plan for the charitable client**
 - Prioritize legal issues to be addressed by the charity
 - Set out realistic time line for work to be done
 - Explain the nature of the legal work that is required

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