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# **BDO CANADA CLIENT SEMINAR**

**Orangeville – June 3, 2015**

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## **BASIC LEGAL RISK MANAGEMENT FOR CHARITIES AND NON-PROFITS**

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**By Terrance S. Carter, B.A., LL.B., TEP, Trade-mark Agent**

[tcarter@carters.ca](mailto:tcarter@carters.ca)  
1-519-942-0001


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 BARRISTERS SOLICITORS TRADEMARK AGENTS	<b>BDO CANADA CLIENT SEMINAR</b> Orangeville – June 3, 2015
<b>Basic Legal Risk Management for Charities and Non-Profits</b>  <b>By Terrance S. Carter, B.A., LL.B., TEP, Trade-mark Agent</b>  tcarter@carters.ca 1-519-942-0001  © 2015 Carters Professional Corporation	
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2	
<b>OVERVIEW OF PRESENTATION</b> <ul style="list-style-type: none"><li>• The Need for Due Diligence in Addressing Risk Management Issues</li><li>• Identifying the Differences Between Charities and Non-Profit Organizations</li><li>• Organizational and Legal Documentation</li><li>• Board Management Issues</li><li>• Utilizing Multiple Corporations</li><li>• Real Property Issues</li><li>• Third Party Use of Property</li><li>• Insurance Considerations/Risk Transfers</li></ul>	
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3

- Intellectual Property Issues
- Privacy Issues
- Anti-Spam Issues
- Employment and Volunteer Issues
- Maintaining Charitable Registration
- Donor Restricted Trust Funds Issues
- Investment Issues

Note: For more details see Legal Risk Management Checklist at <http://www.carters.ca/pub/checklist/nfpchklistJan15b.pdf>

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## A. THE NEED FOR DUE DILIGENCE IN ADDRESSING RISK MANAGEMENT ISSUES

- Charities and non-profits (“NPs”) collectively make up an essential part of Canadian society and its economy
- Charities and NPs constitute the third sector of the economic engine of Canada
- However, charities and NPs are facing fundamental changes and challenges in delivering their services to the public, in part because of a more litigious environment and the higher degree of regulated compliance required



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- In facing these challenges, charities and NPs must become familiar with a vast array of legal requirements ranging from corporate law and trust law to tax and international structures and agreements
- In order for charities and NPs to comply and avoid exposure to legal liability, it is essential that they exercise due diligence in addressing compliance issues with legal obligations that they are subject to
- Why do charities and NPs often experience difficulties in complying with legal requirements?



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- Complicated corporate and charitable requirements at both the federal and provincial level
- Incomplete corporate records
- Interrelationships between multiple corporate structures
- Increasingly complicated tax issues
- Expanding fundraising requirements
- Due diligence needed in the management of gifts and charitable receipting
- Inherent risks in operations, such as sexual abuse of children
- Determining appropriate investment policies



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- Receiving and managing donor-restricted gifts (including endowments)
- Privacy issues involving donors, employees and volunteers
- Frequently inadequate contractual documents
- New compliance requirements under anti-spam legislation
- Possible consequences arising from non-compliance and deficiencies in organizational structure and operations:
  - Revocation of charitable status
  - Liability for exceeding corporate authority
  - Allegations of breach of trust

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- Inquiries by the public under the *Charities Accounting Act (Ontario)*
- Legal actions by donors and/or the Public Guardian and Trustee (Ontario) (“PGT”)
- Court supervised audit of accounts
- Confusion in corporate operations
- Loss of corporate status
- Due diligence in addressing compliance issues involves the charity or the NP asking the following basic questions:
  - What are they legally?



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- What are their legal obligations?
- How can they effectively comply with those legal obligations?
- Due diligence should be undertaken in a pro-active manner in order to manage risks and avoid legal problems before they occur
- The approach should change from benign passivity to pro-active legal risk management
- What follows is a series of key considerations and issues that charities and NPs should address in order to identify and comply with basic legal requirements



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## B. IDENTIFYING THE DIFFERENCES BETWEEN CHARITIES AND NON-PROFIT ORGANIZATIONS

### Charities

- What is a charity?
  - At common-law a charity includes
    - Relief of poverty
    - Advancement of education
    - Advancement of religion
    - Other purposes beneficial to the community recognized by the courts

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- Under the *Charities Accounting Act* - “charitable purpose” is defined
  - 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 donees” concept was introduced
  - Includes a “registered charity”
    - Defined as “charitable organization”, “public foundation” and “private foundation”

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- No definition of a “charity” but reflects the common law definition
- Includes extended statutory list of “qualified donees”
  - Registered Canadian amateur athletics associations
  - Low-cost housing corporations for the aged
  - Municipalities
  - Municipal or public bodies performing a function of government in Canada
  - Prescribed universities outside Canada
  - Her Majesty in right of Canada or a province
  - The United Nations and its agents



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- Foreign charitable organizations that received funding from the Canadian government in the past two years under limited situations
- 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 charity can receive gifts from other registered charities
- What are the legal forms available for a charity?
  - Unincorporated associations
  - Charitable trusts
  - Non-share capital corporations
  - Internal divisions of another charity

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## Non-Profit Organizations

- 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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- 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
  - However, a non-profit organization cannot issue charitable receipts for income tax purposes for gifts received
- CRA is currently reviewing the status of non-profit organizations under the ITA

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- What are the legal forms available for non-profit organization?
  - Unincorporated associations
  - Non-profit corporations
- Examples would include
  - Recreational clubs
  - Service clubs
  - Trade associations
  - Professional associations
  - Some day cares
  - Some housing corporations
  - Fairs and festivals



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## C. ORGANIZATIONAL AND LEGAL DOCUMENTATION

- General overview of organizational & legal documentation
  - Identify the existence and the location of key organizational and legal documents
    - Develop an inventory of key documents
    - Maintain central location for key documents
  - Identify key organizational documents for an unincorporated association
    - Constitution and amendments, if applicable
    - Policies and procedures, if applicable

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- Identify key organizational documents for an incorporated organization
  - Letters patent (articles of continuance) and supplementary letters patent (articles of amendment), if applicable
  - Membership covenant and mission statement, if applicable
  - By-laws and resolutions
  - Directors, members and debt registers
  - Copies of government filings



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- Identify other key legal documents
  - Leases, deeds and mortgages
  - Agency, partnership, association and joint venture agreements, contracts for service
  - License agreements
  - Business name, trade-marks, domain names, and s. 9 (*Trade-marks Act*) official marks
  - Charitable registration number, T3010s and correspondence from CRA
  - Operational policy statements, e.g. sexual abuse and volunteer policy statements
  - Privacy policy
  - Investment policy



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- Review of key documents for an unincorporated association
  - Are the objects clearly stated in the constitution and are they non-profit in nature or are they exclusively charitable in nature?
  - Do constitutional documents correctly reflect how the organization is actually structured and operated?
  - For charitable organizations, is a copy of the constitution filed with the appropriate government agencies, i.e. with Canada Revenue Agency (“CRA”) and the Ontario Public Guardian and Trustee (“OPGT”)?

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- For corporations, has the organization reviewed the *Canada Not-for-profit Corporations Act* or Ontario *Not-for-Profit Corporations Act* to assess what changes will need to be made to its constating documents to comply?
  - Existing federally incorporated charities had until October 17, 2014, to continue under the *Canada Not-for-profit Corporations Act* or face dissolution
  - The Ontario *Not-for-Profit Corporations Act* is expected to be proclaimed in force in 2016. Once proclaimed, corporations incorporated in Ontario will have three years to amend their corporate documents to transition under the new legislation

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- Review of key documents for an incorporated organization
  - Review of letters patent/articles of continuance
    - Is the name in the letters patent/articles of incorporation the correct name of the organization and is it consistent with the objects/purposes?
    - Are its objects/purposes appropriate for a non-profit organization, i.e. are they not charitable, or for a charity, are they exclusively charitable in nature?
    - Are the activities of the organization authorized by its corporate objects/purposes?



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- For a non-profit organization, is the dissolution clause complementary to the objects/purposes?
- For a charity, is the dissolution clause complementary to the charitable objects/purposes?
- Review of supplementary letters patent/articles of amendment (SLP/AA)
  - Have all SLP/AAs been identified
  - Has there been a change of corporate name?
  - Has there been a change of corporate objects/purposes?



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- Letters patent of amalgamation/articles of amalgamation:
  - Are the objects the same or similar?
  - What are the terms of the amalgamation agreement?
  - For charities, is the existing charitable property held in trust for the charitable objects of the previous charitable corporations?
- Does the organization have historical records of all the by-laws?
- Need to review the current corporate by-law for basic terms, such as:
  - Do provisions conflict with letters patent/articles of incorporation concerning objects/purposes or dissolution?

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- Do the provisions reflect the actual organization and operational structure of the organization?
- Does the by-law reflect recent changes to applicable corporate legislation?
- Is there an adequate indemnification provision for the directors?
- For charities, has the indemnification provision been authorized in accordance with the *Charities Accounting Act* (Ontario)?
- Are the by-law amendment procedures consistent with corporate legislation?
- Was initial corporate organization of the corporation properly done?

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- Was there a documented transfer of assets and liabilities at the time of incorporation?
- Are the records of board decisions and/or membership meetings complete?
- Is there adequate board and/or members' authorization for indebtedness, if applicable?
- Have corporate records generally been properly maintained, such as consent to be directors and applications for membership?
- Where are the corporate records kept?
- Have necessary corporate filings and registrations been kept up to date?
  - Ontario Corporations
    - Initial Notice and Notice of Change - Form 1

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- *Business Name Act* (Ontario) registrations
- Mandatory reporting to the Ontario Public Guardian and Trustee for charitable organizations
- Federal Corporations
  - Annual Return (Form 4022) - *Canada*
  - *Extra-Provincial Initial Notice (Form 2)* - *Ontario*
  - *Business Name Act* (Ontario) registrations
  - *Mandatory reporting to the Ontario Public Guardian and Trustee for charitable organizations*



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- Does the organization operate and/or fundraise in any other provinces? If so, there may need to be registration as extra-provincial corporations (and/or fundraiser for charities) in other provinces, together with applicable business name registrations
- Has there been loss of corporate status for failure to maintain government filings?
- Is the organization aware of the importance of proper use of corporate name and operating names?



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- Has the organization developed and implemented risk management policy statements concerning, e.g.:
  - Bullying
  - Child and vulnerable person protection
  - Sexual harassment
  - Protocol for foreign volunteer projects
  - Safety in the workplace
  - Volunteer recruitment management
- Is the content and effectiveness of policies evaluated and reviewed on an annual basis, or as appropriate?
- Has the organization conducted an up to date inventory of its assets?



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## D. BOARD MANAGEMENT ISSUES

- Who is a director?
  - Have the qualifications and procedures to be elected a director and been met by each director?
  - Are there conflicting qualifications to be a director in the by-laws, articles and board policies?
  - Is the register of directors being maintained at least on an annual basis and are any changes among the directors or in their addresses being sent to the relevant government authority?
- Is the organization able to identify who is in charge of the organization?
  - Where does the de facto control of the organization lie? Is it with a board, a committee or executive staff?
  - Is board authority recognized by the membership?

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- Is there liability exposure for defacto directors?
- Are there clearly defined lines of authority between the board and the executive staff?
- Does the board meet on a regular basis and do all directors regularly attend?
- Has an independent audit committee been established by the board to review financial statements and the auditors' report?
- Has the board delegated too much responsibility to executive staff by restricting itself to policy development only without a careful and ongoing monitoring and review of policy implementation?
- Are there policies in place to address board succession planning, recruitment, and orientation?

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- Are the individuals who are authorized to enter into contracts as signing officers on behalf of the charity clearly identified in their officer capacity instead of as individuals?
- Is there adequate communication of board responsibilities to existing, new and future board members?
  - Need to create a board binder of all organizational documents and inventory of assets, as well as an explanation of the general operations of the organization and the board of directors' legal duties and liabilities
  - Need to provide regular updates on changes in the law to board members

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## E. UTILIZING MULTIPLE CORPORATIONS

- Should the organization consider utilizing multiple charitable corporations for its high risk activities in order to contain future liability exposure?
- Should a provincial or national organization that consists of member organizations be structured as an umbrella association of multiple corporations or as a single corporation?
- Should the charity consider establishing and utilizing a parallel foundation for either fundraising or management of charitable assets?



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34

## F. REAL PROPERTY ISSUES

### Deeded land

- Has an environmental assessment been conducted to determine the extent of liability exposure for the organization for future acquisitions as well as existing property?
- If the organization has fuel oil tanks, either above or below ground, has there been compliance with mandatory provincial fuel oil tank regulations?
- Are there trust provisions in old title documents that may impact real property held by a charitable organization that should be varied by a court?
- Has the organization addressed and rectified encroachments with neighbouring lands?

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- Are municipal zoning and legal non-conforming uses being complied with?
- Has the organization reviewed its municipal property tax assessment to determine both classification and valuation and, if so, has there been a request for reconsideration or appeal of assessment?
- Have the requisite policies and plans been enacted for people with disabilities in accordance with the most recent compliance date (January 1, 2015) for the *Accessibility for Ontarians with Disabilities Act, 2005* (Ontario)?
- Does the charity own property with a cultural heritage value or interest and is therefore subject to the Ontario Heritage Act (Ontario)?

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36

## Leased Land

- Avoid personal guarantees on lease document as much as possible
- Avoid clauses requiring restoration of leased premises at the end of the lease
- Ensure access to adequate parking
- Need to limit the extent of tenant expenses under a net lease arrangement
- Ensure the right to sub-let and assign the lease, with a release, if possible
- Need to address issues of environmental liability for both the landlord and the tenant

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- Need to carefully monitor the date by which an option to renew the lease needs to be exercised
- The amount of rent on renewal should be made subject to arbitration
- Try to obtain a covenant from the landlord to prohibit offensive uses of adjoining leased premises
- Does the lease need to be registered on title?
- Try to obtain a right of first refusal to lease adjoining leased premises



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## G. THIRD PARTY USE OF PROPERTY

- Is the organization aware of potential liability exposure in permitting third parties to use its property?
- Has the organization developed and implemented a facility use policy and facility use agreement with appropriate releases and indemnification?
- Does the organization require evidence of liability insurance from third party users of its facilities?
- Has the organization provided written notice to its insurer concerning the use of its property by third parties?
- Does the organization charge appropriate fair market rental fees to users of these properties?



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- Charitable property requires fair market value for rent charged to non-charities
- Non-charitable properties have more flexibility in the amount of rent that it can charge
- Does the organization have implicit corporate authority to allow third party use of its property?
- For organizations that are charities, does the third party use constitute an unrelated business prohibited by the ITA?
- For charities with lifestyle requirements, has consideration been given to compliance with the *Human Rights Code* (Ontario)?

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## H. INSURANCE CONSIDERATIONS/RISK TRANSFERS

- Has the organization maintained a historical record of its insurance coverage in the event of a future claim?
- Has the charity provided full written disclosure annually of all risks to its insurer to avoid denial of coverage?
- Does the charity request regular written reports from its insurance broker on existing coverage, exclusions from coverage and recommendations to enhance coverage?
- Is there a regular review of the adequacy and extent of general liability coverage and property insurance, as well as employment benefits and practices liability?
- Is there directors' and officers' liability coverage in place? Is it reviewed regularly to ensure its adequacy?



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- Do there need to be special insurance endorsements to extend insurance coverage to “out of the ordinary” activities?
- Is there occurrence-based or claims-made insurance coverage for sexual abuse?
- Has the charity considered obtaining the services of an independent insurance consultant or specialist to conduct a risk management review of the charity’s operations and policies from an insurance perspective to determine the adequacy of insurance coverage?
- Has the charity developed and administered effective liability shields in the form of informed consents, disclaimers, releases, waivers and indemnities for program participants as necessary?

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42

## I. INTELLECTUAL PROPERTY ISSUES

- Intellectual property is an essential asset of an organization and consists of both trade-marks and copyright
- Trade-marks need to be identified, licensed and enforced
- Trade-marks can be lost if they are not properly protected
- An organization needs to be pro-active in protecting its trade-marks or risk losing its trade-mark rights by default
- Registration of a corporate name or business name does not by itself give trade-mark protection



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- Trade-mark rights exist at common law but those rights are limited and should be protected by trade-mark registration under the *Trade-marks Act*
- There is enhanced trade-mark protection available for those organizations that qualify as public authorities under the *Trade-marks Act* for official marks
- Separate trade-mark registration must be done in each country in which the organization is operating
- It is essential that a trade-mark be properly marked with either a <sup>TM</sup> for an unregistered trade-mark or a ® for a registered trade-mark



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- It is essential to properly use and license trade-marks, otherwise the trade-mark can be lost
- An infringement of a trade-mark by others, even if done unintentionally, must be immediately challenged
- The board members and executive staff of an organization need to be informed of the importance of trade-mark rights
- The organization should develop a portfolio management approach to identifying, registering, using and protecting trade-marks, both in Canada and in other jurisdictions as applicable



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- In addition to obtaining a trade-mark registration, an organization should secure multiple domain names such as the new .ngo domain name, as soon as possible using its trade-mark as part of the domain name
- Has the designer of the organization's website assigned the copyright for the website design?
- Who owns the copyright for publications of the organization and is it properly identified with a notice of copyright protection, i.e. ©?
- Should the copyright material of the organization be registered, assigned or licensed?



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## J. PRIVACY ISSUES

- Under the Personal Information Protection and Electronic Documents Act ("PIPEDA") organizations must obtain "knowledge and consent of the individual [...] for the collection, use, or disclosure of personal information, except where appropriate"
  - Consent can be either opt-in or opt-out
- PIPEDA applies to commercial activities, including "the selling, bartering or leasing of donor, membership or other fundraising lists"
- Charities and NPs that engage in limited commercial activities ancillary to their primary functions may likely be subject to PIPEDA
- Does the charity have a privacy policy in place to protect donors' rights?

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47

## K. ANTI-SPAM ISSUES

- Canada's Anti-Spam Legislation ("CASL") came into force on July 1, 2014, impacting how charities and NPs communicate with donors, volunteers and members
- CASL prohibits the sending of commercial electronic messages unless the sender has express or implied consent and the message contains prescribed information
- Regulations include a specific exemption for select messages sent by or on behalf of registered charities primarily for fundraising purposes
  - This does not provide a full exemption from all commercial electronic messages from charities
  - This exemption only applies to registered charities (i.e., NPs are not exempt)

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## L. EMPLOYMENT AND VOLUNTEER ISSUES

- Are individuals being paid as independent contractors or employees? If it is as independent contractors, is it in accordance with CRA requirements?
- Has the organization developed appropriate policies and practices for hiring, disciplining and terminating employees and volunteers, including employment contracts?
- Does the organization have a policy in place concerning accommodation for employees who are members of a disadvantaged group identified in the Ontario *Human Rights Code*?
- Does the organization have a policy concerning sexual harassment?
- Is there a need to develop and adopt statements and/or manuals for employees as well as volunteers in relation to conduct and performance structure?

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- Do employees and volunteers who deal with children need to be screened and supervised in accordance with an appropriate sexual abuse policy statement?
- Is the organization aware of and addressing ownership issues regarding intellectual property created by the employees and volunteers?
- Is the organization aware of and complying with applicable statutory requirements, such as pay equity, employment standards, human rights legislation, privacy legislation and occupational health and safety legislation?
- Is the organization and the board exposed to potential criminal liability under section 217.1 of the *Criminal Code* (Westway Mining Disaster) by directing how another person performs a task and neglecting to take reasonable steps to prevent bodily harm to that person?

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## M. MAINTAINING CHARITABLE REGISTRATION

- Do all of the charity's receipts include the name and website address ([www.cra-arc.gc.ca](http://www.cra-arc.gc.ca)) of the CRA?
- Has the charity ensured that its charitable activities are being undertaken in accordance with its charitable objects/purposes?
- Is the legal name of the charity and/or its operating name consistent with the records of CRA?
- Has the charity filed all of its governance documents with CRA, including supplementary letters patent/articles of amendment and by-laws?
- Does CRA have the current head office address of the charity?
- Has the charity obtained Québec charitable status for fundraising in Québec?



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- Does the charity submit its annual information return (Form T3010) within six months of the financial year end of a charity in order to avoid deregistration?
- Does the board of directors, the charity's accountant and legal counsel review and approve the annual information return (Form T3010) for the charity before it is filed each year?
- Is the charity aware of the amendments to the ITA concerning the disbursement quota?
  - The 3.5% disbursement quota extends to charitable organizations
  - Expanded anti-avoidance provisions concerning receipting
- Is the charity aware of the intermediate sanctions and penalties for minor and unintended infractions?



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- Is the charity aware of the CRA Fundraising by Registered Charities Guidance and the need to calculate and track its fundraising ratio each year?
- Is the charity involved in political activities within CRA requirements as amended by the 2012 Federal Budget?
- Is the charity involved in related business activities within CRA Guidance?
- Are charitable funds being used to fund separate business operations of the charitable organization?
- Is the charity aware of the applicable rules concerning the issuance of donation receipts?
- Is the charity aware of the rules on split receipting and anti-tax shelter provisions?



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53



- Are agency relationships, joint venture relationships, or contractual transfer arrangements with non-qualified donees, both inside and outside of Canada, properly documented and implemented?
- Are the charity's books and records maintained in accordance with the requirements of the ITA Is the charity aware of the need to avoid partaking in donation tax shelter schemes?
- Is the charity prepared for an audit by CRA?
- Is a member of the board of directors, a trustee, officer or equivalent official, or any individual who otherwise controls or manages the operation of the charity an "ineligible individual" under the ITA?

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54

## N. DONOR RESTRICTED TRUST FUND ISSUES

- Donor restricted trust funds only apply to charities
- Are there donor restricted trust funds being held by the charity?
  - Building funds
  - Endowment funds
  - Special project funds
  - "Ten year gifts" that may have been given in the past under the ITA
- Are restricted funds used only in accordance with applicable restrictions?



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55

- Are restricted funds being used in whole or in part for general operational purposes or are they being borrowed against? In either event there would be breach of trust
- Are restricted funds segregated from operating funds?
- If not, is there compliance under the *Charities Accounting Act* (Ontario) to co-mingle restricted funds for investment purposes?
- Is the board of the charity aware of the consequences of breach of trust for failing to comply with restricted funds?



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56

## O. INVESTMENT ISSUES

- What investment powers apply to investment of surplus funds of the organization?
  - Investment power may be found in the letters patent/articles of incorporation or supplementary letter patent/articles of amendment
  - Investment power may be found in incorporating legislation
  - Investment power may be found in the *Trustee Act* (Ontario), particularly for a charity



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- Does the organization need and/or have an investment policy?
  - Documenting compliance with prudent investor rule
  - Establishing requirements for delegation of investment decision making, particularly for a charitable organization
  - Proper management of endowed funds
- For charities, are charitable funds being used to fund separate business operations of the charitable organization?



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TOLL FREE: 1-877-942-0001

Toronto Ottawa Orangeville Mississauga  
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