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LEGAL ISSUES IN STARTING A CHURCH

**Part II – The Legal Duties of Directors
of a Church**

(Powerpoint Presentation)

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A. PRELIMINARY MATTERS AND OVERVIEW

Preliminary Matters

- The term “director” for this presentation refers to the members of the controlling board of a church, whether they are called board of directors, board of trustees, board of management, board of deacons, board of elders, etc., and whether the church is incorporated or unincorporated
- For a more detailed discussion of director’s duties, see summary at www.charitylaw.ca

Overview of Presentation

- Introduction
- Common Law Duties and Liabilities
- Statutory Duties and Liabilities

2

B. COMMON LAW DUTIES AND LIABILITIES

- Management of the church
 - Directors responsible for all aspects of church operations
 - To fulfill duties, directors must ensure:
 - Objects are properly carried out and activities comply with objects
 - Church’s financial stability and overall performance
 - Proper hiring and supervision of management and staff

3

- Duty of care
- Directors of all organizations, whether incorporated or not, must exercise certain standard of care in carrying out their duties
 - But standard of care for directors of corporations varies depending on the type of corporation
 - Business corporation
 - Statutory objective standard of care
 - Reasonably prudent person

4

- **Not-for-profit corporation (non-charity)**
 - Common law subjective standard of care
 - Director's own knowledge and experience important
- **Charitable corporation**
 - Additional expectations beyond subjective standard
 - Directors of charities also subject to fiduciary duties as quasi-trustees of charitable property

5

- **Liability risk for lack of constitutional authority**
 - Constitutional authority defined by objects in governing documents, i.e. letters patent for an incorporated church or the constitution for an unincorporated church
 - All church activities must fall within parameters of these objects
 - Liability results where directors act outside scope of this authority

6

- **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 church
 - However, need to have proper constitutional authority to sign contracts and ensure contractual terms are complied with

7

- **Liability risk for breach of fiduciary duty**
 - **Overview**
 - **Directors of a church are subject to fiduciary duty to act as quasi trustee of charitable property**
 - **Directors have primary obligation to exercise due diligence in overseeing corporation**
 - **Fiduciary duties owed to charitable objects, corporation, donors and creditors**

8

- **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 church**
 - **Director's interests not to be placed in conflict with those of church**

9

- **Duty of diligence/duty to act in good faith**
 - **Directors to diligently attend to duties by being familiar with all aspects of church**
 - **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 to be sought**
- **Duty to exercise power**
 - **Directors responsible for managing church**

10

- Delegation to management, staff and volunteers is possible, but directors must always supervise
- **Duty of obedience**
 - Directors must comply with applicable legislation and corporations governing documents
 - All valid church decisions must be implemented

11

- **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
 - Directors cannot receive any remuneration, whether directly or indirectly, without court approval

12

- **Duty of prudence**
 - Directors with special expertise must use it prudently to achieve best result for the church
- **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

13

- **Liability for breach of trust**
 - **Overview**
 - **In addition to fiduciary quasi trustee duties, directors of churches may also be actual trustees of charitable property**
 - **However, fiduciary duties and trustee duties essentially the same**
 - **Aids Society case emphasizes that directors have obligation to apply charitable property to charitable objects**

14

- **Where charitable property lost as a result of actions or inactions of directors, breach of trust could be found**
- **Potential liability risks**
 - **Remuneration of directors**
 - **In Ontario, directors of charities cannot receive direct or indirect remuneration, e.g. as employee or contractor, without court approval**
 - **Indemnification and directors' insurance now available**

15

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

16

- Dealing with special purpose charitable trusts
 - Directors of charities 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

17

- Liability can result from failure to comply with investment powers as well as bad investments, overly conservative decisions and missed opportunities
- Co-mingling of donor restricted funds
 - Are gifts subject to restrictions or limitations?
 - Co-mingling of donor restricted gifts now possible under *Charities Accounting Act* (Ontario) regulations
 - See Charity Law Bulletin #4 at www.charitylaw.ca
 - But cannot co-mingle with general funds

18

C. 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 is due diligence
 - Resigning as a director may not limit liability though there are generally limitation periods

19

- **Federal statutes**
 - *Canada Corporations Act*
 - **Wages and vacation pay**
 - **Conflict of interest**
 - **Reporting requirements**
 - **Books, minutes and records**
 - **Identification of corporation**
 - **Membership lists**
 - **Winding up**
 - **General penalty**

- *Income Tax Act (Canada)*
 - **Directors jointly and severally liable to pay employee income tax deductions for two years after term of office**
 - **Directors maybe personally liable if church fails to comply with numerous reporting requirements, e.g. annual charity information return or improper charitable receipts, or for giving improper tax advice**
 - **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***
 - **Avoid liability by showing positive steps taken to ensure compliance**

- *Excise Tax Act (Canada)*
 - **Directors jointly and severely liable for church's failure to collect & remit GST, if applicable**
 - **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**

– *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
- Failure to comply could result in prison terms and fines

– *Anti-terrorism Legislation*

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

23

- Risks include seizure of charitable property, loss of charitable status and criminal code charges
- See www.antiterrorismlaw.ca for details

– *Criminal Code*

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

- Ontario statutes
 - *Corporations Act (Ontario)*
 - Reporting requirements
 - Conflict of interest
 - General offence provision

24

– *Employment Standards Act (Ontario)*

- Fines imposed on directors for failure of churches to pay wages, vacation pay and severances
- 6 months liability for wages and 12 months liability for vacation pay, plus fines
- However, limitation periods are available

25

– *Retail Sales Tax*

- Directors jointly and severally liable where church fails to remit, where applicable

– *Workplace Safety and Insurance Board Act (Ontario)*

- Directors are not liable for church’s failure to remit premiums unless it can be shown they did not intend to pay them

26

– *Pension Benefits Act (Ontario)*

- Directors who fail to pay employer’s premiums for employee’s pension plans and to hold monies in trust may be ordered to make up contribution
- Failure to comply may subject directors to fines

– *Ontario Health Insurance Program*

- Directors will be held personally liable for premiums and health tax not paid by the church

27

– *Occupational Health and Safety Act (Ontario)*

- Directors required to take reasonable steps to comply with workplace health and safety requirements
- Failure to do so will result in fines to churches and their directors

– *Environmental Protection Act (Ontario) and related legislation*

- Directors required to take reasonable care to prevent unlawful discharge of contaminants

28

- Persons in control of contaminants are responsible for cleanup and related costs
- Appropriate environmental audits need to be obtained before purchasing or receiving land
- *Child and Family Services Act (Ontario)*
 - Failure to report child abuse is an offence
 - A church and its directors may be liable where employees fail to report abuse or where it occurs because of failure to monitor employees and operations

29

- *Trustee Act (Ontario)*
 - Act establishes that directors of churches have power and duty to invest assets of charity
 - Investments must be in accordance with prudent investor standard
 - See Charity Law Bulletin #8 at www.charitylaw.ca
- *Charities Accounting Act (Ontario)*
 - Act gives rights to donor and Public Guardian and Trustee (PGT) to call directors to account for improper use of

30

- Charitable property as well as fundraising practices
- Co-mingling of donor restricted funds is permitted provided there is strict compliance with the act's requirements
- Fundraising
 - Specific charitable statutes concerning fundraising:
 - *Income Tax Act (Canada)*
 - *Charities Accounting Act (Ontario)*
 - *Charitable Gifts Act (Ontario)*

31

- *Religious Organizations' Lands Act (Ontario)*
- *Charitable Fund-Raising Act (Alberta)*
- *Charitable Fund-raising Businesses Act (Saskatchewan)*
- *Charities Endorsement Act (Manitoba)*
- *Charities Act (Prince Edward Island)*
- General statutes affecting charitable fundraising:
 - *Competition Act (Canada)*
 - *Privacy Act (Canada)*

- *Insurance Act (Ontario)*
- *Loan and Trust Corporations Act (Ontario)*
- *Securities Act (Ontario)*
- *Trustee Act (Ontario)*
- *Business Name Act (Ontario)*

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