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**ASSOCIATION OF TREASURERS OF RELIGIOUS INSTITUTIONS  
(ATRI) 19<sup>TH</sup> ANNUAL CONFERENCE**

**Winnipeg – October 1, 2006**

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**CHARITIES UPDATE 2006  
SELECTED TOPICS**

**Consideration in Utilizing Multiple Corporate  
Entities to Protect Charitable Assets**

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**By Terrance S. Carter, B.A., LL.B.**  
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**Offices / Bureaux**  
Ottawa (613) 235-4774  
Mississauga (416) 675-3766  
Orangeville (519) 942-0001  
**Toll Free: 1-877-942-0001**

**By Appointment / Par rendez-vous**  
Toronto (416) 675-3766  
London (519) 937-2333  
Vancouver (877) 942-0001  
**www.charitylaw.ca**

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**Considerations in Utilizing Multiple Corporate  
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Offices in Ottawa, Mississauga & Orangeville  
Locations also in Toronto, London & Vancouver  
Toll Free: 1-877-942-0001  
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**OVERVIEW**

- 1. RESOURCE MATERIALS**
- 2. THE PURPOSE OF MULTIPLE CHARITABLE CORPORATIONS**
- 3. DIFFERENT TYPES OF MULTIPLE CHARITABLE CORPORATIONS**
- 4. ISSUES TO ADDRESS IN ULTIZING A MULTIPLE CORPORATE STRUCTURE**
- 5. INDIRECT CONTROL OF MULTIPLE CHARITABLE CORPORATIONS**
- 6. AVOIDING CROSS-OVER LIABILITY**
- 7. CRA DRAFT POLICY ON UMBRELLA ORGANIZATIONS**

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**1. RESOURCE MATERIALS**  
See the following publications available at [www.charitylaw.ca](http://www.charitylaw.ca) for more information

- **Effective Asset Protection Through Multiple Corporate Structures, November 9, 2005 at**  
<http://www.carters.ca/pub/seminar/chrchlaw/2005/index.html>
- **“Pro-Active Protection of Charitable Assets”**  
– A Selective Discussion of Liability Risks and Pro-Active Responses, November 20, 2001
- **“National and International Charitable Structures: Achieving Protection and Control”, November 26, 1998**  
<http://www.carters.ca/pub/article/charity/1998/natlstruct.pdf>

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- **“Cross-over Liability: Principles from the Residential Schools Cases (Charity Law Bulletin #19 – January 31, 2003)**  
<http://www.carters.ca/pub/bulletin/charity/2003/chylb19-03.pdf>
- **Update on Christian Brothers (Charity Law Bulletin #24 – September 30, 2003)**  
<http://www.carters.ca/pub/bulletin/charity/2003/chylb24-03.pdf>
- **New CRA Policy on Umbrella Organizations (Charity Law Bulletin #78, October 12, 2005)**  
<http://www.carters.ca/pub/bulletin/charity/2005/chylb78.pdf>

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## 2. THE PURPOSE OF MULTIPLE CHARITABLE CORPORATIONS

- Multiple corporations have long been used by the for-profit sector to contain liabilities and protect assets
- Similar use of multiple corporations by the charitable sector is now increasing
- The board of a charitable corporation has a fiduciary obligation at common law to protect charitable assets

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- There is a similar duty at canon law (canon 1284, §2, 2° – i.e. “ensure that the ownership of ecclesiastical goods is safeguarded in ways which are valid in civil law”)
- The use of multiple charitable corporations can accomplish these fiduciary and canon law obligations

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### 3. DIFFERENT TYPES OF MULTIPLE CHARITABLE CORPORATIONS

#### Parallel Operating Charities

- Used when an incorporated charity (e.g. either a generalate/provincialate or a local house) has one or more operating divisions with a greater degree of liability exposure (e.g. a religious institution, such as a school or a AIDS-HIV clinic)
- The liabilities associated with an operating division (such as a school or a AIDS-HIV clinic) is moved to a separately incorporated entity to contain liability and protect the assets of the main charity

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#### Parallel Foundations

- Parallel foundations can be used for:
  - Protection of donor restricted funds as a result of the *Christian Brothers* case
  - Establishment and management of endowment funds
  - Protection of surplus funds from governments for religious health care institutions
  - Separation of capital campaigns from operating campaigns
  - The encouragement of *inter vivos* gifts, testamentary gifts and planned giving

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- Also a parallel foundation can be used as a form of holding corporation for a charity's assets, e.g. land and buildings, intellectual property or specialized libraries
- Compliance with creditor protection legislation, though, is important. As a result, only existing assets not subject to past or present claims can be transferred without residual claims remaining
- Consideration needs to be given to *Assessment Act* (Ontario) for land holding parallel foundations in order to maintain the municipal tax exemption of church property
- Development of a license or lease agreement and possibly seek a pre-ruling from MPAC

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#### Umbrella Associations

- Involves structuring a national or provincial charity that consists of member organizations into multiple legal entities
- The governing organization (e.g. the generalate/provincialate), is separately incorporated that acts as the umbrella organization, with each member organization (e.g. local houses) possibly being separately incorporated under the auspices of the governing organization (e.g. generalate/provincialate)
- While a single corporate entity can provide simplicity in administration and operations, the disadvantage is that all the assets of the various divisions (e.g. the local houses) are left in one single legal entity

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- This may result in the loss of all of the assets of the national or provincial charity in the event of a claim being made against any one of the divisions or chapters of the charity
- The advantages of utilizing an umbrella association model include:
  - Reduced overall liability exposure in operating a national or provincial charity by containing the liability associated with a member organization within a separate corporate entity

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- Where one member organization owns real estate that is subject to toxic contamination, the costs associated with the clean up of the contamination will generally be limited to only the assets of the incorporated member organization
- Similarly, the operations of the umbrella association that are carried on outside the province of Ontario through separate corporations in other provinces would not be subject to the provisions of the *Charities Accounting Act* (Ontario)

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**4. ISSUES TO ADDRESS IN UTILIZING A  
MULTIPLE CORPORATE STRUCTURE**

**Matching Civil Law and Canon Law Entities**

- In order to avoid confusion at civil law and with government regulators, it is advisable that each separate juridical person should have a matching separate corporate entity at civil law as much as possible

**Potential for Loss of Control**

- The authority that the governing organization (e.g. the generalate/provincialate) has at canon law over its members must not be lost through the use of multiple corporations

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**Trade-mark Protection and Licensing**

- The use of the name and/or the trade-mark of a governing organization by either an incorporated division (e.g. religious institution, such as a school or a AIDS-HIV clinic), parallel foundation, or local division or chapter (e.g. a local house) should be as much as possible protected and licensed

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**5. INDIRECT CONTROL OF MULTIPLE  
CHARITABLE CORPORATIONS**

**The Need for Indirect Control**

- Unlike business corporations, charities cannot control subsidiary corporations through the ownership of shares
- As separate and autonomous legal entities at civil law, a governing organization and a member organization have to carefully structure their relationship from the inception to avoid having to “rewrite the rules” later
- Letters patent and by-laws of an incorporated entity should provide reserve powers at canon law to the generalate/provincialate over matters such as:
  - Change of corporate objects in by-law

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- Approval of election of board of directors or trustees
- Approval over appointment of a chief executive officer
- Approval over leasing, selling or encumbering real estate
- Approval over merger or dissolving the corporation

- In addition to reserve powers at canon law, there are other types of indirect control models at civil law that can be considered, such as:
  - The ex officio control model
  - The franchise control model

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**Ex Officio Control Model**

- Historically, the ex officio control model has been the more common method of indirectly controlling member organizations by a governing organization
- The by-laws of the member organization provide for ex officio directors who are either directors or officers of the governing organization
- The number of ex officio board members can vary from one all the way up to all of the board members of the member organization

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- Both the *Canada Corporations Act* and the *Corporations Act* (Ontario) permit the establishment of ex officio directors in the form of corporate by-laws
- A variation involves having all the board members or corporate members of the governing organization being deemed to be the corporate members of the member organization ex officio
- However, the ex officio model results in serious concerns about cross-over liability and does not address other expectations between a governing organization and its member organizations or related intellectual property licensing considerations

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**Franchise Control Model**

- A practical parallel can be drawn between the relationship of a franchisor and a franchisee in a business context and the relationship between multiple charitable corporations
- The Franchise Control Model involves a contractual relationship by way of a franchise agreement which establishes a control mechanism between a governing organization (e.g. a generalate/provincialate) and its member organization (e.g. a religious institution, a parallel foundation or a local house)

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- Key factors in the contractual relationship include the requirements for an ongoing relationship in the governing organization and the consequences of losing that relationship
- The franchise agreement can also be used to authorize the licensing of trade-marks and copyrights owned by the governing organization

**Basic Features of the Franchise Control Model**

**a) Overview**

- The Franchise Control Model works well with all types of multiple charitable corporations, e.g. generalate/provincialate and member organization, including religious institutions, parallel operating foundations and umbrella organizations

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- Basic components include an association agreement including, appropriate control provisions within the incorporating documents of member organizations, and implementing a licensing arrangement to protect the applicable intellectual property

**b) Association Agreement**

- The association agreement sets out the contractual relationship between the governing organization and its member organizations

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- An association agreement should include:
  - Recognition that the governing organization and the member organizations have similar charitable purposes, but are separate and distinct corporate entities at civil law with separate boards of directors, and that they are to remain independently responsible for their own management and governance
  - Set term for the association agreement (e.g. five years) and renewal provisions
  - Basic requirements of the association relationship include:

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- § The contents of the letters patent of the member organization
- § Governing organization to review and approve the general operating by-law for the member organization, as well as other fundamental changes (e.g. standard reserve powers)
- § The parameters under which the name and trade-marks of the governing organization can be utilized by the member organization
- The rights that flow from the association relationship
- How the association relationship is terminated and the consequences of termination

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- c) Incorporating Documentation for Member Organizations
  - The incorporating documents for a member organization should be drafted or amended in accordance with the requirements set out in the association agreement
  - The governing organization must be given an opportunity to review the final form of the application for letters patent and general operating by-law for the member organization before it is filed for incorporation

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**d) Trade-mark Considerations**

- The most important asset of a charity is the goodwill associated with its name as a trade-mark. In the context of a governing organization, its name as a trade-mark and associated logo constitute the basis by which the public will identify the organization and activities that it carries on
- The corporate name and various operating names and logos of the governing organization should be separately registered as trade-marks

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- The registered trade-marks should then be licensed to each member organization by a separate trade-mark license agreement to include:
  - Recognition of the ownership of the trade-marks
  - How the trade-marks can be used and controlled
  - How the trade-marks are to be protected and enforced
  - What constitutes default and the consequences of termination of the trade-mark license

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**e) Copyright Considerations**

- Copyright issues can also be an important part of establishing control by a governing organization
- It may be prudent for the governing organization to register the copyright for materials used in the public domain
- Examples of copyright materials belonging to the governing organization that are used by member organizations include resource materials, audiotapes, videotapes, training manuals, checklists, brochures, fundraising documentation, etc.
- A copyright license should be prepared and entered into similar to a trade-mark license

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**6. AVOIDING CROSS-OVER LIABILITY**

- A fundamental aspect of utilizing multiple charitable corporations is the need to maintain the integrity of the limited liability protection of the various incorporated entities
- While the concept of limited liability protection is still the general rule for corporate entities, there are instances where the governing organization or an operating charity might be found to be liable for the actions of a member organization or affiliated corporation as a result of the equitable doctrine known as “piercing the corporate veil”

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- The *Christian Brothers* decision was a landmark case on the application of cross-over liability for charitable and not-for-profit organizations
- Based on a review of recent residential school case law, cross-over liability may result where governing organization has a significant degree of control over the actions of the members or employees of associated incorporated entities

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- The following are practical steps to reduce a finding of cross-over liability between multiple charitable corporations:
  - Ensure separate incorporation of each entity
  - Expressly define the limits of power and authority of the entities
  - Keep up-to-date records of activities in separate corporate minute book

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- Some of the factors suggesting “central control”:
  - Having the governing organization involved in the licensing, hiring, disciplining, payment or general day-to-day direction and supervision of employees of the member organization
  - Having common bank accounts or investments
  - Making explicit or implicit representation that the governing organization is responsible for the operations of the member organization

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- Having both organizations occupy the same location for either operational or administrative activities
- Using the same officers or employees unless it is clear that one organization is invoicing the other organization for the services provided by its employees
- Using the land, buildings or property of the other organization without an arm’s length lease agreement

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- Having the same individuals serve on the board of directors or key committees of both entities where there is a significant overlap in membership
- Indicating on letterhead, signs, brochures, or other documentation that the member organization is an operating division of the governing organization
- Having the governing organization and a member organization use the same lawyers or accountants on a regular basis

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**7. CRA DRAFT POLICY ON UMBRELLA ORGANIZATIONS**

**Overview**

- CRA released a new draft policy on umbrella organizations in July 2005, entitled “Guideline for the Registration of Umbrella Organizations”, which is available at its website: [www.cra-arc.gc.ca](http://www.cra-arc.gc.ca)
- The Guidelines define a charitable umbrella organization as one that “works to achieve a charitable goal by supporting, improving and enhancing the work of groups involved in the delivery of charitable programs”

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- The Guidelines make it clear that an umbrella organization can now qualify for registration

**Types of Umbrella Organizations**

**a) Charities Established to Assist Other Registered Charities**

- These are organizations that support the charitable sector by promoting the efficiency and effectiveness of registered charities
- The beneficiaries of the services of an umbrella organization must be predominantly other registered charities
- The objects of these charities must clearly reflect that the purpose of the organization is to improve the efficiency and effectiveness of other registered charities

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**b) Umbrella Organizations Advancing a Recognized Charitable Purpose**

- These are organizations which are established to further a particular charitable purpose, i.e. other than assisting charities, which may convey benefits on constituent groups as ancillary to the achievement of that purpose
- It is also acceptable for such umbrella organizations to increase the capacity and ability of member organizations as a secondary result of their work
- This would apply to the umbrella relationship of a general/provincial to its local house

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**c) Charities Established to Hold Title to Property**

- It is now possible for charities, as foundation, to incur debts in taking title to property, thereby increasing the availability of asset protection arrangements by including both foundations and charitable organizations
- The beneficiaries of this third type of umbrella organization must only be registered charities
- Its formal purpose must be to provide a charitable service or benefit to the tenant charity and not merely to hold title to property
- The activities of these title holding organizations can vary from merely title-holding entities to ones that provide a more comprehensive range of services, e.g. property management services

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- The land holding charity must show that it provides some benefit to the tenant charity, although it is not clear why
- The Guidelines then address the requirements of these title holding entities with regard to reporting expenses
- CRA takes the position that a mere permission to occupy the premises does not constitute an expenditure, nor does it constitute a gift to the tenant charity
- However, there is no reason why the fair market value of the provision of the premises to the tenant charity should not also constitute a charitable expenditure for a title-holding charity

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