

LEGAL RISK MANAGEMENT CHECKLIST FOR CHARITIES

By Terrance S. Carter, B.A., LL.B. and Jacqueline M. Connor, B.A., LL.B.

A. INTRODUCTION

The operations of charities have become complex and the possibility of litigation against charities occurring as a result of their operation is greater than ever before. The exposure of charities to liability goes further than the loss of charitable assets and/or the insolvency or winding up of a charity. Directors of charities may also face possible legal action against them personally by donors, members, third parties and governmental authorities for breach of their fiduciary duties or even breach of trust in failing to adequately protect or apply the assets of a charity. Given the increased risks to both charities and their directors, there is an increasing need to protect charitable assets from lawsuits and creditors on a pro-active basis.

The purpose of this legal risk management checklist is to provide a brief outline of some of the more important issues that directors and/or executive staff of a charity, whether incorporated or not, may need to consider in ensuring due diligence in the operation of the charity, as well as an overview of liability exposure faced by charities in Canada and some of the steps available to protect charities against such risks. As it is impossible to adequately address all aspects of liabilities being faced by charities and the pro-active steps which need to be taken to protect against such risks, this checklist provides only a general overview of some of the considerations that charities and their board of directors may need to be aware of to both identify and manage legal risks. Some of the comments and recommended procedures contained in this legal risk management checklist may also be applicable to not-for-profit non-charitable organizations.

B. IDENTIFICATION AND MANAGEMENT OF LEGAL RISKS

1. Is charitable status needed?
 - a) Do charitable receipts need to be issued?
 - b) Can the organization work under the auspices of an existing charity?
 - c) Business donors may not require charitable receipts.

2. General overview of organizational & legal documentation
 - a) Identify the existence and location of key organizational documents
 - Develop an inventory of key documents
 - Maintain central location for key documents
 - b) Identify key organizational documents for an unincorporated charity
 - Constitution and amendments, if applicable
 - Policy statements, if applicable
 - c) Key organizational documents for a corporate charity
 - Letters patent and supplementary letters patent, if applicable
 - Membership covenant and mission statement, if applicable
 - By-laws and resolutions
 - Directors, members and debt registers
 - Copies of government filings
 - d) Determining other key legal documents
 - Leases, deeds and mortgages
 - Agency, association and joint venture agreements
 - License agreements
 - Business name, trade-marks, Section 9 official marks and domain names
 - Charitable registration number
 - Policy statements, i.e. sexual abuse and volunteer policy statement
 - Insurance policies
 - Privacy policy
 - Investment policy

3. Review of key documents for unincorporated charity
 - a) Are the objects clearly stated in the constitution and are they exclusively charitable?

- b) Do constitutional documents correctly reflect how the organization is actually structured and operated?
 - c) Is a copy of the constitution filed with the appropriate government agencies, i.e. with Canada Revenue Agency (“CRA”) and the Public Guardian and Trustee (“PGT”)?
4. Review of key documents for an incorporated charity
- a) Review of letters patent
 - Is the name in the letters patent the correct name of the charity consistent with the charitable objects of the charity?
 - Are its objects exclusively charitable?
 - Are the activities carried out by the charity authorized by its charitable objects?
 - Is the dissolution clause complementary to the charitable objects?
 - b) Review of supplementary letters patent
 - Has there been a change of corporate name?
 - Has there been a change of corporate objects?
 - What is the effect of a change of objects upon existing charitable property?
 - c) Letters patent of amalgamation (only for Ontario corporations)
 - Are the charitable objects the same or similar?
 - What are the terms of the amalgamation agreement?
 - Is the existing charitable property held in trust for the charitable objects of the previous charitable corporations?
 - d) Need to review corporate by-law for basic terms, such as
 - Do provisions conflict with letters patent?
 - Do provisions reflect changes to applicable corporate legislation?
 - Is there an adequate indemnification provision?
 - Has the indemnification provision been authorized in accordance with the *Charities Accounting Act* (Ontario)?
 - Are the by-law amendment procedures consistent with corporate legislation?
 - e) Was the initial corporate organization of the charity properly done?
 - f) Was there a documented transfer of assets and liabilities on incorporation?
 - g) Are the records of board decisions and/or membership meetings complete?
 - h) Was there adequate board and/or members’ authorization for indebtedness?
 - i) Have corporate records been properly maintained?
 - j) Have necessary corporate filings and registrations been kept up to date?
 - Ontario Corporations:

- ◆ Initial Notice and Notice of Change - Form 1
 - ◆ *Business Name Act* (Ontario) registrations
 - ◆ Mandatory reporting to Public Guardian and Trustee
 - Canada Corporations:
 - ◆ Annual Summary (Form 3) – Canada
 - ◆ Extra-Provincial Initial Notice (Form 2) – Ontario
 - ◆ *Business Name Act* (Ontario) registrations
 - ◆ Mandatory report to Public Guardian and Trustee
 - Does the charity operate and/or fundraise in any other provinces? If so, there may need to be registration as an extra-provincial corporation and/or fundraiser in other provinces, together with applicant business name registrations.
- k) Does the charity need to continue itself under the proposed new *Canada Not-for-profit Corporations Act*? (Note: To be proclaimed into force in approximately June 2006).
- l) Has there been loss of corporate status for failure to maintain government filings?
- m) Is the charity aware of the importance of proper use of corporate name and operating names?
- n) Has the charity developed and implemented risk management policy statements on:
- child abuse
 - sexual abuse
 - sexual harassment
 - bullying
 - volunteer conduct
 - safety in the workplace?
- o) Has the charity conducted an inventory of its charitable assets?

C. UTILIZING MULTIPLE CHARITABLE CORPORATIONS

1. Should the charity consider utilizing multiple charitable corporations for its high risk activities in order to reduce liability exposure and protecting assets?
2. Should the charity consider establishing and utilizing a parallel foundation for either fundraising or protection of charitable assets?
3. Has consideration been given to balancing indirect control of multiple corporations with issues involving cross over liability?
4. Has consideration been given to implementing effective indirect control through contracts and/or licensing agreements as an alternative to overt corporate control?

D. BOARD MANAGEMENT ISSUES

1. Is the charity able to identify which group is in charge of the charity?
 - a) i.e., Where does the de facto control of the charity lie? Is it with a board, a committee or executive staff?
 - b) Is board authority recognized by the membership?
2. Are there clearly defined lines of authority between the board and the executive staff?
3. Does the board meet on a regular basis and do all directors regularly attend?
4. Has an independent audit committee been established to review financial statements and the auditors' report?
5. Is there adequate communication of board responsibilities to existing and future board members?
 - a) Need to create a board binder of all corporate documents, as well as an explanation of the general operations of the corporation as a charity and the board of directors' legal duties and liabilities
 - b) Need to provide regular updates on changes in the law to board members

E. REDUCING BOARD LIABILITY

1. Do any directors receive direct or indirect remuneration or other financial benefit from the charity in contravention of their fiduciary duties?
2. Has the charity adequately indemnified its directors and officers in accordance with the *Charities Accounting Act* (Ontario)?
3. Is there corporate authority to acquire directors' and officers' liability insurance in accordance with the requirements of the *Charities Accounting Act* (Ontario)?
4. Has the board delegated too much responsibility to executive staff by restricting itself to policy decisions only without careful and ongoing monitoring and review?
5. Should the charity consider reducing the size of the board to limit the number of people who are exposed to liability as directors?
6. Is the charity effectively making use of committees as an alternative to a large board of directors?
7. Do the board members on occasion need to receive independent legal advice due to the possibility of liability exposure?

8. Should the charity consider implementing an advisory board to complement the board of directors without a corresponding exposure to liability?
9. Has the charity established a comprehensive due diligence review procedure by establishing and utilizing the appropriate legal risk management checklist?
10. Has a legal risk management committee of the board been established?

F. INSURANCE CONSIDERATIONS

1. Has the charity maintained a historical record of its insurance coverage in the event of a future claim?
2. Is there occurrence-based or claims-made insurance coverage for sexual abuse?
3. Has the charity provided full written disclosure of all risks to its insurer to avoid denial of coverage?
4. Does the charity request regular reports from its insurance broker on existing coverage, exclusions from coverage and recommendations to enhance coverage?
5. Is there a regular review of the adequacy and extent of general liability coverage and property insurance?
6. Is there directors' and officers' liability coverage in place and is it reviewed on a regular basis?
7. Do there need to be special insurance endorsements to extend insurance coverage, e.g. activities of agents in foreign countries?

G. THIRD PARTY USE OF CHARITABLE PROPERTY

1. Is the charity aware of the potential liability exposure in permitting third parties to use its property?
2. Has the charity developed and implemented a third party property use agreement with appropriate releases and indemnification?
3. Does the charity require evidence of liability insurance from third party users of its facilities?
4. Does the charity charge appropriate fair market rental fees to non-charities?

H. REAL PROPERTY ISSUES

1. Has an environmental assessment been conducted to determine the extent of liability exposure for contaminants?

2. Are there trust provisions in old trust deeds or title, and if so, are they being complied with?
3. Has the charity addressed and rectified encroachments with neighbouring lands?
4. Are municipal zoning and legal non-conforming uses being complied with?
5. Could the charity be forced to sell off surplus land under *Charities Accounting Act* (Ontario) if it has been held for more than three years?
6. Has the charity reviewed its entitlement to possible exemption from municipal property taxation, or reviewed its assessment for accuracy, or its entitlement to a possible rebate of property taxes?

I. INTELLECTUAL PROPERTY ISSUES

1. Does the charity need to register any of its key names and/or logos as trade-marks?
 - a) Identify trade-marks
 - b) Protect trade-marks by registration
 - c) Use trade-marks in conjunction with appropriate markings
 - d) Ensure that any third parties using trade-marks enter into a trade-mark licensing agreement
2. Has the charity protected its trade-marks by multiple corresponding domain names?
3. Who owns the copyright for publications of the charity?
4. Should copyright be registered, assigned or licensed?

J. EMPLOYMENT AND VOLUNTEER MATTERS

1. Is the individual an employee or an independent contractor?
2. Has the charity developed appropriate hiring policies and practices for its employees?
3. Is there compliance with applicable human rights legislation?
4. Is there need for an employment contract with employees?
5. Is there a need to develop and adopt policy statements and/or manuals for employees as well as volunteers?
6. Do employees and volunteers who deal with children need to be screened and supervised, together with criminal record checks, in accordance with an appropriate sexual abuse policy statement?
7. Is there need for a discipline procedure for employees and/or volunteer members?

8. Has the charity developed appropriate policies and practices regarding the termination of employees and complied with appropriate provincial and/or federal legislation?
9. Is the charity aware of and complying with applicable statutory requirements, such as pay equity, employment standards, human rights legislation, privacy legislation and occupational health and safety prerequisites?
10. Are the charity and board exposed to criminal liability under the *Criminal Code* i.e. Bill C-45 (Westray Mines)?

K. CHARITABLE AND FUNDRAISING ACTIVITIES

1. Has the charity ensured that its charitable activities are done in accordance with its charitable objects?
2. Are fundraising and/or administrative costs kept within the 80/20 disbursement quota?
3. Has provincial fundraising legislation, where applicable, been complied with?
4. Have fundraising programmes been reviewed by legal counsel?
5. Are donors' rights to require accountability respected, particularly rights under the *Charities Accounting Act* (Ontario)?
6. Does the charity have a privacy policy in place in order to protect donors' rights?
7. Are sponsorship arrangements properly documented?

L. FISCAL MANAGEMENT ISSUES

1. Are all salaries, benefits and statutory deductions being paid by the charity on a timely basis with appropriate reports to the board of directors?
2. Is the charity operating with a deficit and, if so, for how long?
3. How is the deficit being funded?
4. Has a sinking fund been established to retire debt of the charity?
5. Are investments being offered to the public without full disclosure to potential investors?
6. Is there an audit committee in place?
7. Are charitable funds being used to fund separate business operations of the charity?

8. Is there a violation of the *Charitable Gifts Act* (Ontario) by the charity owning more than 10% of a business?

M. INVESTMENT ISSUES

1. What investment powers apply to the investment of surplus funds of the charity?
 - a) Prudent investor rule under the *Trustee Act* (Ontario) will generally apply
 - b) However, specific investment powers may sometimes apply as contained in
 - Letters patent or supplementary letters patent
 - Endowment and gift agreements
 - Testamentary gifts
2. Does the charity need and/or have an investment policy?
 - a) Documenting compliance with prudent investor rule
 - b) Establishing requirements for delegation of investment decision making
 - c) Prohibition on sub-delegation

N. DONOR RESTRICTED TRUST FUNDS

1. Are there donor restricted trust funds being held by the charity?
 - a) Building funds
 - b) Endowment funds (perpetual)
 - c) Ten year gifts under the *Income Tax Act*
 - d) Special project funds
2. Are restricted funds being used only in accordance with applicable restrictions?
3. Are restricted funds being used in whole or in part for general operational purposes or are they being borrowed against?
4. Are restricted funds segregated from operating funds?
5. Is there compliance under the *Charities Accounting Act* (Ontario) to co-mingle restricted funds for investment purposes?
6. Is the board of the charity aware of the consequences of breach of trust for failing to comply with restricted funds?

O. MAINTAINING CHARITABLE REGISTRATION

1. Is the legal name of the charity and/or its operating name consistent with the records of CRA?
2. Does CRA have the current head office address of the charity?
3. Has the charity obtained Quebec charitable status for fundraising in Quebec?
4. Does the charity submit its annual charity information return (Form T3010A) within 6 months of the financial year end of a charity?
5. Has the charity complied with its disbursement quota?
6. Can the charity comply with the new disbursement quota rules as of December 2004?
7. Is the charity involved in political activities within CRA limits?
8. Is the charity involved in related business activities within CRA guidelines?
9. Is the charity aware of the applicable rules concerning the issuance of charitable receipts including the new rules on split receipting and anti-tax shelter provisions?
10. Are agency and/or joint venture relationships with non-qualified donees properly documented and implemented?
11. Does the board of directors review the annual return (T3010A) for the charity before it is filed each year?
12. Is the charity prepared for a spot audit by CRA?

P. NATIONAL AND/OR INTERNATIONAL RELATIONSHIPS

1. Are relationships with national organizations and/or subsidiary chapters adequately documented with specific reference to controlling trade-marks?
2. Are relationships between national and international organizations adequately documented in order to effect an international operation?
3. Has the ownership of trade-marks and/or copyrights been determined and documented?
4. Have trade-marks and copyrights been adequately protected and licensed in Canada and in other countries as necessary?

Q. ANTI-TERRORISM LEGISLATION

1. Does the charity carry on operations that may require it to be in compliance with anti-terrorism legislation?
 - a) International operations
 - b) Domestic operations
2. Has the charity undertaken appropriate due diligence procedures in complying with anti-terrorism legislation?
 - a) Development of an anti-terrorism policy statement
 - b) Development of resource materials on anti-terrorism legislation
 - c) Requiring disclosure statements for board members and staff
 - d) Evaluating all charitable programs for compliance
 - e) Requiring disclosure statements from affiliated charities, third party agents and/or partners and conducting appropriate inquiries
 - f) Determining when to make inquiries of donors
 - g) Conducting due diligence internet searches on directors, officers and agents
3. Are directors aware of risks associated with failing to comply with anti-terrorism legislation?
 - a) Loss of charitable status
 - b) Personal liability in civil law
 - c) Possible criminal law sanction