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CHARITIES & NOT-FOR-PROFIT NEWSLETTER

July 2005

The Charities & Not-for-Profit Newsletter is published periodically by Miller Thomson LLP's Charities & Not-for-Profit Group as a service to our clients and the broader voluntary sector. We encourage you to forward the e-mail delivering this newsletter to anyone (internal or external to your organization) who might be interested. Complimentary French and English e-mail subscriptions are available by contacting charitieseditor@millerthomson.com.

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MILLER THOMSON FOUNDATION SCHOLARSHIP AWARDS

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Since its formation in 1995, The Miller Thomson Foundation has awarded scholarships totalling $1,550,000 to 1,550 promising students pursuing post-secondary education in Canada. This program is an important part of Miller Thomson's commitment to the communities its lawyers live and work in. It is also a tangible example of the firm's desire to invest in Canada's future by supporting higher education opportunities.

A long term initiative, The Miller Thomson Foundation National Scholarship is funded by The Miller Thomson Foundation. Students throughout Canada, who are in their graduating year, are eligible to apply for The Miller Thomson Foundation National Scholarship and will be able to use the scholarship to pursue a course of study within Canada leading to a degree or diploma from the accredited community college or university of their choice.

Persons interested in information about the Scholarship (including lists of past recipients) or who wish to obtain an application may visit our website at www.millerthomson.com and link to MT Foundation or contact Mrs. Lesley A. Lawson, Executive Director, The Miller Thomson Foundation at llawson@millerthomson.com.

CIVIL MARRIAGE ACT INCLUDES PROTECTION FOR RELIGIOUS CHARITIES

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Concerns have been raised that Bill C-38, the *Civil Marriage Act* would indirectly restrict the right of religious charities to practice or promote religious tenets that are opposed to same-sex marriage. A purpose is not considered charitable if it violates public policy - if an official public policy accepted same-sex marriage, religious charities opposed to it might arguably cease to be charitable. There are strong charity law and *Charter of Rights and Freedoms* arguments for the continued recognition of religious charities regardless of their positions on same-sex marriage or other controversial social issues. Nevertheless, in response to those concerns, Parliament has added a specific provision to the *Income Tax Act* designed to confirm that religious charities will not lose charitable registration because of their opposition to same-sex marriage:

(6.21) For greater certainty, subject to subsections (6.1) and (6.2), a registered charity with stated purposes that include the advancement of religion shall not have its registration revoked or be subject to any other penalty under Part V solely because it or any of its members, officials, supporters or adherents exercises, in relation to marriage between persons of the same sex, the freedom of conscience and religion guaranteed under the Canadian Charter of Rights and Freedoms.

At the time of writing, Bill C-38 has passed the Commons and is on its way to the Senate. We expect that this provision will survive and be included in the *Civil Marriage Act* (and the *Income Tax Act*) when it comes into force.

NEW ONTARIO NOT-FOR-PROFIT CORPORATION ACT PROMISED

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On May 16, when speaking to the Ontario Bar Association, and again on June 23, when speaking to the Toronto Board of Trade, the Honourable James Watson, Ontario Minister of Consumer and Business Services, advised the audiences that Ontario is committed to three phases of law reform.

Third on the timetable (after the enactment of uniform securities transfer legislation and revision of the Ontario *Business Corporations Act* will be amendments to the Ontario *Corporations Act,* the primary piece of legislation for the incorporation of Ontario charities and not-for-profit organizations. Although no details were given about the changes proposed for the *Corporations Act*, we expect that the changes that will be proposed will be similar to those proposed in the new federal *Canada Not-for-Profit Corporations Act* (see the November 2004 issue of this newsletter for details).

The audiences were told that each phase will involve public consultation and the process may take a number of years. The best news however, is that after many years of no action, this timetable at least exists and the government has taken note that change is needed. We will keep you apprised as this timetable evolves.

GOODS DONATED FOR CHARITABLE PURPOSES MAY QUALIFY FOR DUTY FREE ENTRY AND RELIEF FROM GST

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Relief From Customs Duty

Every good imported into Canada must be classified under one of the 10-digit tariff classification numbers set out in Chapters 1 to 97 of the Canadian *Customs Tariff* (also known as tariff item numbers). Once the tariff item number is determined for a particular good, the rate of duty that applies on importation may also be determined.

However, some goods, including "charitable goods," may also fall within certain special classification provisions in Chapters 98 and 99 of the *Customs Tariff*. These provisions reduce or eliminate customs duty otherwise payable for qualifying goods that meet specific conditions.

Under tariff item no. 9815.00.00, clothing and books donated for charitable purposes by residents of Canada to any organization in Canada may be imported duty free. Any type of goods donated by non-residents of Canada to religious, charitable and educational institutions in Canada may also be imported duty free. The recipient is not required to be registered as a charity with the Canada Revenue Agency in order for the goods to qualify for duty-free entry.

According to the Canada Border Services Agency's written policy, goods will qualify for duty free importation under tariff no. 9815.00.00 even if the importer is required to pay an administrative fee and/or shipping

and handling charges to obtain the goods. For example, an organization that accumulates donated goods from multiple sources and then redistributes the goods to individual charities may require recipients to pay a registration or administration fee to cover the cost to the organization of maintaining inventory.

If, however, the charitable purpose of the donation or the *bona fides* of an organization or institution to which goods are donated is questioned by the Canada Border Services Agency, the CBSA may require the importer to pay full duties at the time of importation. The importer may subsequently request a refund of the duty paid.

Relief from GST

Generally speaking, goods imported into Canada are subject to GST payable at the time of importation.

For charitable goods falling within tariff item no. 9815.00.00, the importer is relieved from both customs duty and GST otherwise payable on importation. Section 1 of Schedule VII of the *Excise Tax Act* provides that goods classified under a number of tariff headings, including heading 9815, qualify as non-taxable importations for the purposes of the GST. However, certain types of goods may still be subject to excise duties which are not relieved by section 1 of Schedule VII.

Under the Charitable Goods Remission Order, P.C. 1997-2037, all customs duty, GST and excise taxes otherwise payable are eliminated in respect of goods donated by a non-resident of Canada to a religious, charitable, or educational institution in Canada.

Under section 4 of Schedule VII of the *Excise Tax Act*, donated goods that are imported into Canada by a charity or a public institution in Canada may also qualify as non-taxable importations for the purposes of the GST, even where they do not meet the specific conditions of tariff item no. 9815.00.00 or Charitable Goods Remission Order, P.C. 1997-2037.

However, to benefit from Section 4, the recipient importer must meet the definition of "Charity" or "Public Institution" as those terms are defined in the *Excise Tax Act*. Under section 123 of the *Excise Tax Act*, "charity" means a registered charity or registered Canadian amateur athletic association within the meaning of the *Income Tax Act*, but does not include a public institution. "Public institution" means a registered charity within the meaning of the *Income Tax Act* that is a school authority, a public college, a university, a hospital authority or a municipality. Accordingly, the recipient must be registered with the CRA as a charity to benefit from Section 4 of Schedule VII of the *Excise Tax Act*.

If you are a charitable organization considering the importation of donated goods into Canada, it is prudent to plan ahead and consult with a qualified customs professional. This will ensure that your organization makes the best use of all available duty and tax saving strategies under the applicable legislation.

NEW T3010A REGISTERED CHARITY INFORMATION RETURN

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In the April 2005 issue of this Newsletter, we noted that the Canada Revenue Agency (CRA) was currently revising the Registered Charity Information Return, form T3010A, to incorporate the recent changes to the *Income Tax Act* affecting the annual minimum expenditure requirements (i.e., the disbursement quota).

The CRA's new T3010A is now available online. This new form should be used by charities completing information returns for fiscal periods that begin after March 22, 2004. Registered charities are required to file an information return annually, within 6 months of the end of their fiscal period.

As a consequence of the delay in availability of the new T3010A, charities may, in some cases, have difficulty meeting the requirements to file this new return within 6 months of their fiscal year-end. In those cases, the affected charities will have until August 31, 2005, to complete the new T3010A.

TAX DETAILS FOR CHARITABLE BEQUESTS

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As planned giving becomes more popular in Canada, an increasing number of charities are beneficiaries of estates. Where the charity is a beneficiary of some or all of the *residue* of an estate (as opposed to a set amount), questions regarding the receipting of the gift often arise.

Assets of an estate are generally not distributed for at least a year following someone's death – longer if the assets are complex or if disputes arise. In the meantime, some of the assets may continue to accumulate income or to increase in value. In such cases, what should be the value of the donation receipt issued by the charity? How should the charity treat the income that arises on the assets of the estate for the period following the death but prior to the transfer of the assets to the charity?

The donation receipt is issued for the fair market value of the property donated on the date the donation was made. In the context of an estate, this generally means that the receipt should be for the value of the property on the date of death of the donor. Where the residue of an estate includes, for example, a principal residence valued at $500,000, GICs worth $350,000 and some mutual funds valued at $85,000 on the date of death, the amount of the receipt would be based on these values, less the amounts paid for taxes, probate fees, amounts paid to legatees, and other debts and expenses of the estate.

Following the date of death, the interest that accrues on the GIC, and any income and gains on the mutual funds "belong" to the charity (again, less certain expenses), and should be paid or transferred to the charity. The estate should issue a T-3 slip allocating these amounts out to the charity. The amounts are thereby not taxed in the hands of the estate. The charity should not issue donation receipts for these amounts, as they are income to the charity, not a further donation.

Lawyers in Miller Thomson's Charities and Not-for-Profit and Estates Groups would be pleased to assist your charity with any issues that may arise if it is the recipient of a bequest.

DISAPPOINTED BENEFICIARIES SUE LAWYER WHO DRAFTED WILL: *GRAHAM V. BONNYCASTLE*

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This case involves two disgruntled siblings who sued their father's lawyers for preparing a Will which did not name them the beneficiaries of their father's estate.

The facts of the case are that the father, Archie Graham, signed his first Will in 1984. After signing the first Will, Mr. Graham re-married. The marriage voided the first Will. In August 1994, Mr. Graham's accountant contacted the solicitors and advised them that Mr. Graham wanted to prepare a new Will. Two days later, one of Mr. Graham's sons obtained a trusteeship and guardianship order over his father, pursuant to the Alberta *Dependent Adults Act*. This gave the son the ability to manage both his father's financial and personal affairs.

Five days after the Order was granted by the Court, Mr. Graham met with his two lawyers. Both lawyers, after meeting with Mr. Graham, determined that he had capacity to sign a new Will in spite of his serious mental and physical illnesses. Prior to the meeting, the lawyers received instructions for the preparation of the new Will from Mr. Graham's sister, but confirmed those instructions with Mr. Graham and determined that, although the instructions came from his sister, the instructions reflected his intentions. Three days later, on August 26, 1994, Mr. Graham signed his new Will. His new Will was very different from his first Will which had named both of his children as equal beneficiaries of his estate. The new Will named his sister and his new wife as beneficiaries of his estate. On September 21, 1994, the children started an action with the Courts to challenge the marriage, alleging that their father did not have capacity to enter

into the marriage. Nine days later, on September 30, 1994, Mr. Graham died. On December 22, 1994, the sister and Mr. Graham's widow both applied for probate of his second Will. The children opposed the probate and on January 16, 1995, the Court directed that there be a trial to determine if Mr. Graham had testamentary capacity at the time that he signed the second Will. On November 26, 1997, the sister, the widow and the two children reached a settlement whereby the children were paid a portion of the estate. The children, however, did not receive the entire estate as they would have done if the first Will had been admitted to probate.

The children then sued the deceased father's lawyers for the difference between what they received from the settlement and what they would have received under the first Will had it been probated, as well as for all of their legal costs. The children claimed that they suffered losses as beneficiaries under the first Will because of the negligence of the lawyers. The children alleged that the lawyers had an obligation to them which was imposed upon the lawyers by their father.

The issue before the Court was whether the lawyers owed a duty of care to the beneficiaries of the first Will, to ensure that their father did not sign a second Will if he lacked testamentary capacity. After a thorough investigation of the law, the Court determined that a lawyer can only be liable to a beneficiary if, because of the lawyer's negligence in the preparation of the Will, the beneficiary does not receive a benefit which the deceased wanted them to receive.

The Court further held that a lawyer could never owe a beneficiary a duty because it would be inconsistent with the lawyer's duty to his client. In this case, Mr. Graham's wishes took precedence over what the children wanted their father's Will to say. The Court also stated that a lawyer could owe a duty to the children if the father imposed such a duty on his lawyers by virtue of his client-solicitor relationship. However, in this case, Mr. Graham had not imposed any such duty on his lawyers.

The children were not satisfied with the Alberta Court of Queen's Bench decision and appealed to the Alberta Court of Appeal. Their appeal was heard on March 2, 2004. The ground of appeal was that the Court of Queen's Bench Justice misapplied the law with respect to the duty of care owed by solicitors to third parties and acted without jurisdiction to find that the father had testamentary capacity to provide instructions for the preparation of the second Will.

The Court of Appeal held that the Court of Queen's Bench Justice correctly found that the lawyer's primary duty was to carry out the intentions of her client. With respect to Mr. Graham's testamentary capacity, the Court of Appeal stated that a lawyer has a duty to her client to make sufficient inquiries regarding testamentary capacity, and to record those observations. The Court of Appeal also stated that there were public policy reasons why the lawyer's duty should not be extended:

> The imposition of a duty to beneficiaries under a previous Will would create conflict of interest. A solicitor (lawyer) cannot have the duty to follow the instructions of his client to prepare a new Will and, at the same time, have a duty to beneficiaries under previous Wills, whose interests are likely to be affected by the new Will. The interests of the beneficiaries under a previous Will are inevitably in conflict with the interests of the testator who wishes to change the Will by revoking or reducing a bequest to that beneficiary.

The Court of Appeal also held that:

> A solicitor must be free to act in the best interests of her client when discharging her duties to make inquiries regarding the client's testamentary capacity without concerns about the interests of others. The decision as to testamentary capacity, which is a difficult one for the solicitor, should not be made more difficult by the unnecessary extension of duties to others.

The Court of Appeal concluded that if Mr. Graham had testamentary capacity at the time of making the new Will, then he was entitled to make a new Will, and that no loss could be caused by the lawyers. The Court could not find any justification for imposing a duty on lawyers taking instructions from a testator for a new Will to protect the interests of beneficiaries under a former Will. The Court held that "it is not fair, just and reasonable to impose such a duty."

The disgruntled children were dissatisfied with the decision of the Court of Appeal and sought leave to appeal to the Supreme Court of Canada. On April 14, 2005, the Supreme Court of Canada denied them leave to appeal. Charities may find themselves in situations similar to that described in this case and may take some comfort from the findings.

SUSPENSION OF NON-UNION EMPLOYEES

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A suspension without pay is a key element of the progressive discipline process in a unionized workplace. But what of a non-union environment? Can an employer suspend an employee not covered by a collective agreement without pay as a form of discipline?

The general rule is that an employer does not have the power to suspend a non-union employee. An employer who does suspend an employee may be exposing itself to a claim for constructive dismissal. There is, however, a large exception to this general rule.

A suspension can be used as a form of discipline where the right to suspend is an implied or express term of the employment contract. An express term is one which is specifically set out in the employment contract. Therefore, in order to have the express power to suspend an employee, the employment contract would have to actually state that the employer held such a power. In practice, very few employment contracts contain specific language giving the employer the right to suspend the employee.

The more common situation is where the right to suspend is an implied term of the employment contract. Terms may be implied into a contact based on custom and usage, or on the presumed intention of the parties to the contract. Thus, in workplaces where there is a history of suspending employees as a disciplinary tool, or where policies exist which indicate that suspensions may be used, the Courts have been inclined to find an implied power to suspend.

Terms may also be implied into a contract by law. Terms are implied by law where they are deemed necessary to the fair functioning of an agreement. Terms implied by law do not depend upon any agreement or understanding of the parties for their existence. For example, the right to reasonable notice of termination is a term implied by law into employment contracts. While to date, the power to suspend has not been implied into employment contracts by law, the Courts have hinted that this may be a possibility in the future

In any event, it should be remembered that even in workplaces were there is an express or implied right to suspend an employee, a constructive dismissal can still arise where the suspension imposed is not reasonable in the circumstances. We suggest that suspension not be used to discipline a non-union employee (particularly suspension based on an implied contractual term) without the employer first obtaining legal advice.

AROUND MILLER THOMSON

Miller Thomson hosted a complimentary client seminar on June 9 in Vancouver. Topics and presenters included **Peter Jarvis** "Managing Risk - Moving from fighting fires to growing the organization," **Debra Bell** "Charities and Gaming," **Peter MacDonald** "Anti-Terrorism, Charities and Due Diligence," **Sandra Enticknap** "Managing Risk – Protecting Special Purpose Assets," **Robert Hayhoe** "Update on New CRA Charities Sanctions," and **Arthur Drache** "Charities and Politics."

Susan Manwaring presented as part of a panel "Charities and Planned Giving" at the STEP Canada 7th National Conference on June 7 in Toronto. Her presentation concentrated on Donor Advised Funds.

Arthur Drache published "Budget gets an hour of committee's time" in the June 1 *National Post*. The article comments on the treatment by the Commons Finance Committee of the legislative amendments implementing the charity tax changes announced in the March 2004 federal budget.

Dragana Sanchez-Glowicki published "Secret Charitable Trusts" in the newsletter of the Canadian Cancer Society - Alberta.

Robert Hayhoe published "Update on Canadian Charities Operating Abroad" in the *Exempt Organization Tax Review* in June.

Susan Manwaring published "Collaboration With the Legislators: Can It Be Achieved?" in the 2005 *Canadian Donor's Guide*.

Robert Hayhoe published "New Charity Tax Regime" in the June issue of the Advisor, published by the Canadian Cancer Society.

Arthur Drache published "Klotz Appeal Upheld" in the June issue of the *Canadian Taxpayer*.

Arthur Drache published "What Are the Resources of a Charity?", "Roosting Chickens", "Charity Issues Not of Concern", "Federal Election" and "Tooting Their Own Horn" and **Stuart Rudner** published "Non-Competition Clauses Enforceable Against Former Employees?" in the June *Canadian Not-for-Profit News*.

Arthur Drache, **Robert Hayhoe** and **Susan Manwaring** have been re-elected to the executive of the Ontario Bar Association's Charities and Not-for Profit Section.

In mid-June, **Rachel Blumenfeld** was co-chair of a program entitled 'Planning for People with Special Needs: Legal, Tax and Financial Issues' for the Professional Advisory Committee of the Jewish Foundation of Greater Toronto. **Martin Rochwerg** is the Chair of the Professional Advisory Committee.

In early June, **Arthur Drache** presented to the Greater Vancouver Roundtable of the CAGP on "Tales from the Trenches".

Miller Thomson LLP was honoured to receive a special CAGP Greater Toronto Area Roundtable Recognition Award at the June 23rd Annual General Meeting of the Canadian Association of Gift Planners GTA Roundtable.

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