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CHARITIES & NOT-FOR-PROFIT NEWSLETTER

September 2008

The Charities & Not-for-Profit Newsletter is published monthly 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 e-mail subscriptions are available by contacting charitieseditor@millerthomson.com.

Inside

MILLER THOMSON ADDS ANOTHER DEDICATED CHARITY AND NOT-FOR-PROFIT SPECIALIST

We are pleased to announce that Andrew Valentine has joined our Charities and Not-for-Profit group as a junior-level associate. Andrew, who has been called to the Ontario Bar this summer, will be practising in our Toronto office. He can be reached at 416-595-2980 or avalentine@millerthomson.com.

PETER LAUWERS APPOINTED TO THE BENCH

Miller Thomson is pleased to announce that Peter Lauwers has been appointed to the bench as a Judge of the Ontario Superior Court of Justice. As a member of the firm for the past 13 years and a senior partner in the litigation department, Peter has contributed significantly to Miller Thomson's success. We warmly congratulate Peter and wish him every success in his important new role.

VANCOUVER CHARITIES AND NOT-FOR-PROFIT SEMINAR

Miller Thomson's Vancouver Charities and Not-For-Profit Group will be hosting a complimentary breakfast seminar on Thursday, October 23, 2008 from 7:30 a.m. to 10:15 p.m., at the Sutton Place Hotel.

The seminar will cover the following topics:

- *Tax Update*
- *Employment Issues*
- *Immigration Issues*
- *B.C. Society Act and the Proposed Federal Act*
- *Recent Issues for Charities*

If you are interested in attending please R.S.V.P. via email to kchan@millerthomson.com or by telephone to Katherine Chan at 604.628.2905.

PROTECTION OF DIRECTORS: WHEN MAY AN INDEMNITY, OR A REIMBURSEMENT RIGHT, LAWFULLY BE WITHDRAWN?

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It is not often that local proceedings in the United States courts provoke a warning to us in Canada. One such instance is the decision of Vice-Chancellor Stephen Lamb of the Court of Chancery of the State of Delaware in the case of *Schoon and Bohnen v. Troy Corporation.*

At the time William J. Bohnen was elected as a director, and until the November following his February resignation for health reasons, the by-laws of the Troy Corporation provided that the Corporation was required to "pay the expenses incurred by any present or former director" in connection with certain claims made against any of them. The by-law also provided that the Corporation would advance funds to cover such director's ongoing costs in defending against such claims. In November, the by-laws were changed to remove these benefits from former directors. Two months later, the Corporation brought actions against Bohnen (and his successor director, Schoon), alleging breaches of fiduciary duty for their respective actions while directors. Based upon the by-law provision in force while he was a director, Bohnen then sought to obtain funds for the legal expenses he was incurring in defending against such allegations. Not surprisingly, the Corporation resisted such payment, based upon the change in the by-law provision that by then no longer extended to former directors. Bohnen countered by asserting that the Corporation could not change the by-law protection with retroactive effect, denying him the financial protection in place while he was a director. The Delaware Court concluded, however, that in order to have the right to such payments, the court proceeding against Bohnen would have had to arisen before the change in the by-laws.

This case has persuaded several legal commentators in the United States to encourage their readers and/or clients who serve as directors to review the arrangements under which directors have financial protection, particularly after they leave office, from claims and demands arising out of their service as directors. These concerns extend to provisions for indemnities and reimbursement rights for directors and officers that are typically found in by-laws of not-for-profit and business corporations alike. There are two separate, but related, issues:

1. the indemnification issue, that is, the right of the person to be indemnified by the corporation for any claim made against the person while the person was acting as a director; and
2. the advancement issue, that is, the right of the person to require the corporation to advance whatever funds are necessary to pay for the legal defence costs (including disbursements) of the person as the claim makes its way through the courts.

There are at least three kinds of arrangements that a person might seek to ensure that, during and after the person's term as a director or officer, the person has at least some financial protection against the costs of claims arising out of actions taken (or omitted) while serving in that position, on both the indemnification and advancement issues.

Firstly, the by-laws of the corporation could provide that the corporation is obliged to indemnify the person, and to advance defence costs while the claim is pending, commencing from the time that the person first takes office, and thereafter, in perpetuity - meaning forever. As long as the by-laws include such provisions, a person who serves as director or officer will have the resources of the corporation behind him or her to fund both of these obligations. Unless there is also something further, however, there are two potential problems with such a provision: the by-laws could be altered (as they were in the Delaware case) to remove the protection; and the resources of the corporation could be insufficient to cover all costs.

Secondly, to protect against a change in by-laws that removes the indemnification and advancement obligations, each director could, on appointment, seek a formal binding agreement between the director and the corporation by which the corporation binds itself to provide the indemnity and to agree to advance legal defence costs in the event of a claim. Such a contract could also include a prohibition against a termination of that obligation

by the corporation by any means without the prior consent of the director. It would be important that the corporation's by-laws at the time of the contract permit the indemnity and advancement obligations. With such a formal contractual obligation, a director or officer would be less concerned if the corporation subsequently tried to or did change the by-laws so as to remove such a benefit.

Thirdly, Directors & Officers insurance coverage ("D&O insurance") could be obtained in order to protect present and former directors and officers. This coverage is normally taken out by the corporation at its sole cost, so that the corporation would have sufficient resources to fund both the indemnity and the advancement obligations. The downside of this, of course, is that sufficient insurance coverage may not be in place by the corporation at the actual moment that the funds are needed. Directors while in office have the power to ensure that the corporation provides adequate D&O coverage. However, for former directors and officers, there is a risk that the current directors might not see fit to provide adequate coverage. To provide against this, the individual director or officer may wish to contract for D&O coverage specifically for that person, and such coverage (which, we are given to understand, can be made non-cancellable and non-rescindable) would continue regardless of the action (or inaction) of the corporation.

In the best of all worlds, the corporation will include in its by-laws extensive all-inclusive indemnity and full advancement provisions for the benefit of present and former directors and officers. The by-laws would also include a condition that the obligations in both cases come into force and are binding without further formality from the moment the person is elected or appointed as a director or officer, and a further condition that such by-law provisions are incapable of alteration or revocation without the prior consent of all persons who may be entitled to benefit thereunder. This would be fully funded by a D&O policy with generous limits. At the same time, the corporation would enter into individual indemnity and advancement contracts with all directors and officers at the time they are respectively elected or appointed, containing provisions that continue the protection indefinitely following the person's leaving of the office.

BRITISH COLUMBIA'S NAMING PRIVILEGES POLICY

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The naming of a building, part of a building, road, recreational area, collection or equipment of significant value is a serious matter for organizations such as hospitals, health authorities, colleges and universities. It can reflect the importance of a donor to the realization of a charity's objectives and can add prestige to the named physical asset, the entity itself or a program of the charity. In 2006, the government of British Columbia established a "Naming Privileges Policy" to govern the naming of physical assets such as those listed above, in recognition of donations made to any government ministries and government bodies as defined in the *Financial Administration Act*. Affected entities, including hospitals, health authorities, colleges and universities were required to bring their own naming recognition policies, if any, in line with this new policy when it was implemented in June 2007.

By the time the Naming Privileges Policy was rolled out in June 2007, it had been revised to streamline wording and incorporate recommendations from stakeholders. The current policy requires that all proposed naming recognitions (referred to as "naming privileges opportunities") be approved by a Naming Privileges Committee identified by the Minister of Labour and Citizens' Services (the "Minister"), or, in certain circumstances, by the British Columbia Cabinet, but the Minister can now appoint up to two *ad hoc* members to the Naming Privileges Committee from the entity submitting the naming opportunity. These *ad hoc* members are not permitted to vote and can only participate in the opportunity for naming recognition in which they are involved. Examples of proposals requiring Cabinet approval include those where the value of a contribution is greater than $5,000,000 or where the asset is or likely will be the object of media attention.

The government will not approve proposed naming recognitions that, among other things:

- may be inconsistent with the government's legal obligations;

- imply the government's endorsement of a partisan political or ideological position or of a commercial product;
- convey a message that might be deemed prejudicial to race, religion, gender or sexual orientation;
- present demeaning or derogatory portrayals of communities or groups or, in light of generally prevailing community standards, could reasonably be expected to cause offence to a community or group.

Between June 2006 and the end of January 2008, the British Columbia government's Intellectual Property Program ("IPP") facilitated 56 naming opportunity requests. IPP Officials are unable to provide more recent statistics relating to the Naming Privileges Policy, citing confidentiality reasons and fiscal restraints.

We are aware that some institutions consider the Naming Privileges Policy to be an infringement on their autonomy and question its legality. Others simply find it to be an annoying process of hurdles to overcome, while for some organizations, it is considered to be a reasonable and effective policy to which they fully adhere. If a charity requires assistance with respect to the Naming Privileges Policy, Miller Thomson's Charities and Not-For-Profit Group lawyers can provide assistance.

EXPOSURE TO LIABILITY FROM SERVICE OF ALCOHOL AT EVENTS

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Charitable and non-profit organizations often host functions for their members or for the public at which alcohol is served. Like almost all human interactions, there are legal implications arising from these events, but often these implications are not considered until it is too late.

The following provides an overview of the liability implications for charitable and not-for-profit organizations that hold functions at which alcohol is served. Legal liability in this context is governed by the nature of the relationship between the host and the guests. As a starting point, it is important to understand other relationships between host and guest, whether commercial, social or in an employment situation. This article does not address the very important licensing issues - charities and non-profit organizations should be sure to verify that the service or distribution of alcohol is even permitted in the circumstances.

Commercial hosts (bars and restaurants) have a positive duty to guests who consume alcohol in their establishments because it is foreseeable that an intoxicated patron has a high risk of suffering personal injury, or of injuring others, if allowed to leave the establishment while impaired. This high level of responsibility is driven by the fact that the commercial host is profiting from the consumption of alcohol, and has an interest in encouraging consumption.

Social hosts are held to a different standard than commercial hosts. In a recent landmark decision, the Supreme Court of Canada unanimously concluded that a social host will not generally be liable to people who are injured by guests who consume alcohol at a party hosted at his home.

The Supreme Court said that social hosts are not obligated to police the conduct of their guests unless the host encourages the over-consumption of alcohol, such as hosting drinking games. It further ruled that social guests are autonomous individuals who are responsible for their own conduct. An important distinction between a commercial host and a social host is that the commercial host is profiting from the sale of alcohol.

An employer, due to its unique relationship to its employees, can have a higher duty than a social host at company-hosted events. This is especially true when the employee has a job function to perform at the event.

A not-for-profit organization holding a function is unlikely to be considered a commercial host unless it is profiting from the sale of alcohol. The venue, such as a conference centre, where the event is held and which is actually serving the alcohol would fall into the category of commercial host. However, that does not relieve the organization of all responsibility. The scope of responsibility of a not-for-profit organization is illustrated in a decision of the Alberta Court of Queen's Bench.

In *Calliou Estate (Public Trustee of) v. Calliou Estate* (2002), the Court considered the liability of a volunteer organization that provided alcohol to its guests. A group of adult hockey players organized a friendly tournament. Each team paid a $350 entry fee, and was provided with a case of beer and coupons that could be exchanged for two pitchers of beer at a local tavern. Members of a visiting team consumed some of the beer provided to them and exchanged the coupons for two pitchers of beer. They bought a third pitcher and later purchased alcohol at two other locations. Members of the visiting team were killed when a drunken team-mate's vehicle collided with an oncoming truck. The families of the deceased sued, among others, the hockey team that provided the beer and coupons.

In assessing whether the host team had a duty to the deceased, the court confirmed that the existence of a duty of care does not depend solely on the formalities of the relationship between the parties (whether a commercial, social or employment relationship). Instead,

> *…the thread running through both the commercial host and the social host cases on the question of duty of care, is a knowledge of a state of intoxication on the part of the guest who drives and injures himself or a third party.*

The Court concluded that:

> *In this case, the relationship of the host to the guest is more than a mere social host situation, although it is also less than a full commercial relationship. I draw this conclusion because while the [host team] charged $350 for entry into the tournament and supplied beer to the teams from the proceeds of the entry fee, the [visiting] team members essentially bought the beer themselves through a volunteer intermediary.*

The Court went on to assess the knowledge of the host organization as to the degree of intoxication of the visiting team and whether they were likely to drive while intoxicated. On the facts of that case, there was no liability because the host organization had no indication that the visiting team was intoxicated or that they would drive while intoxicated.

While Canadian courts have identified categories of hosts for the purpose of describing relationships, the liability of a host is not determined solely by the classification of the type of relationship as social, commercial or employment. Those categories are important in the sense that they generally establish the degree of responsibility that the host has towards the guest. Ultimately, however, courts will assess whether the host knew the guest was intoxicated and had a reasonable expectation that the guest would drive (or engage in another dangerous activity) while intoxicated.

FOOTBALL CANADA RCAAA STATUS REVOKED

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On August 30, 2008, the Canada Revenue Agency published a notice in the Canada Gazette that it had revoked the status of Football Canada as a registered Canadian Amateur Athletic Association for improper issuance of official donation receipts. To the best of our knowledge, this is the first revocation of an RCAAA for cause.

RCAAA's are national amateur athletic organizations. Notwithstanding that they may carry out activities that do not demonstrate an exclusively charitable purpose, they are permitted to issue official donation receipts like a registered charity and gifts to RCAAAs give rise to the same tax credits or deductions as gifts to registered charities.

Football Canada apparently became involved in a tax shelter donation program whereby donors borrowed money to give to Football Canada. Football Canada then seems to have invested the gift proceeds in long term annuities arranged by the promoters of the donation program.

The position of the CRA is that the receipts by Football Canada were improper. As a result, CRA has revoked its RCAAA status. The revocation of Football Canada is consistent with the aggressive approach of CRA to donors and charities (even ones that did not participate in issuing official donation receipts) who have been involved in tax shelter arrangements. Any charity that has been involved in a shelter should obtain immediate legal advice. Miller Thomson charity tax lawyers can assist with responding to CRA audits.

WHAT'S HAPPENING AROUND MILLER THOMSON

Robert Hayhoe and **Andrew Valentine** published "Charity Suspension Postponements Available" in the *Canadian Tax Journal*, August issue.

Robert Hayhoe and **Amanda Stacey** published "The Continuing Saga of Charitable Donation Tax Shelters in Canada" in the August 2008 edition of *Exempt Organizations Tax Review,* published by.

Arthur Drache wrote "Redeemer Foundation - Another Win for the Minister" in the August-September issue of *The Canadian Taxpayer*.

Erin A. Viala's article "Employee Scholarships Who Reports to CRA?" was reprinted in the September issue of *The Canadian Taxpayer*.

Susan Manwaring and **Robert Hayhoe** made presentations at the Canadian Council of Christian Charities conference on September 23 and 24, 2008.

Arthur Drache wrote "Supreme Court Sanctions Fishing for Charity Donors Names", "Fundraising or Related Business" and "Feds Hit Arts Programs in Dog Days of Summer" in the September 2008, Vol. 16 No. 9 issue of the *Canadian Not-For-Profit News*.

Rachel Blumenfeld's article "Valuing Life Insurance for Donation Purposes" appeared in the September 2008, Vol. 16 No. 9 issue of the *Canadian Not-For-Profit News*.

Rachel Blumenfeld presented on "Charitable Remainder Trusts" at the Ontario Bar Association's Trusts, Trustees and Trusteeships III" conference on September 23, 2008.

David Chodikoff wrote "Tax Shelters: What Is Next For The Buyer/Participant" in the September issue of *It's Personal*.

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