

**DUTIES AND RESPONSIBILITIES
OF DIRECTORS
OF NOT-FOR-PROFIT
ORGANIZATIONS**

Fourth Edition

WATSON Advisors Inc.

Published by:
Canadian Society of Association Executives
10 King Street East, Suite 1100
Toronto, Ontario M5C 1C3
www.csae.com

Copyright © 2015 by the Canadian Society of Association Executives.

All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means, electronic or mechanical, including photocopy, recording, or any information storage and retrieval system, without permission in writing from the publisher.

This book is published for informational and educational purposes only and should not be considered legal advice. Any use of the information contained in this publication is the sole responsibility and liability of the reader.

Library and Archives Canada Cataloguing in Publication

WATSON Advisors Inc.

Duties and responsibilities of directors of not-for-profit organizations, 4th edition / by WATSON Advisors Inc.

Includes bibliographic references.

ISBN: 978-1-927816-07-3

1. Directors of corporations—Legal status, laws, etc.—Canada. 2. Nonprofit organizations—Canada. 3. Risk Management—Canada

I. Canadian Society of Association Executives. II. Title. III. Title: Duties and responsibilities of directors of not-for-profit organizations.

Product Code: 1326

1 2 3 4 5 6 7 8

Printed in Canada



CANADIAN SOCIETY OF ASSOCIATION EXECUTIVES

SOCIÉTÉ CANADIENNE DES DIRECTEURS D'ASSOCIATION

Table of Contents

Preface	1
Important Note	2
Introduction	3
Purpose	3
Legislation.....	3
Not-for-Profit Corporations	4
Members, Directors, and Officers.....	6
Governance Framework	7
Legislation.....	7
Bylaws.....	7
Governance Policies	8
The Board of Directors’ Role	9
General	9
Organizational Stewardship	9
Board Stewardship.....	10
Duties of Directors	11
General	11
Fiduciary Relationship	11
Duty of Care	12
Duty of Skill.....	13
Duty of Diligence.....	14
Delegation by Directors.....	14
Reliance on Management and Advisors	14
Practice Points—Duty of Care	15
Higher Standard of Care Applicable to Directors of Charities	16
Fiduciary Duty	17
Duty to Avoid Conflicts of Interest.....	18
Specific Duties Under Statute of Incorporation.....	20
Liabilities Of Directors	21
General	21

Civil Liability.....	21
Contract	22
Statutory Liabilities	22
Employee and Workplace Liability.....	23
Tax Liability	24
Environmental Liability.....	25
Canada’s New Anti-Spam Legislation.....	26
Criminal Liability	26
Protection Of Directors	27
General	27
Due Diligence	27
Indemnification and Insurance for Directors.....	28
Effective Governance	31
Endnotes.....	35
About WATSON	45
Additional Resources.....	46
CSAE Bookstore	46
Sponsors	52

Preface



Over recent decades, there has been a dramatic growth in interest in corporate governance, both in the private and not-for-profit sectors. In 1999, the Canadian Society of Association Executives (CSAE) published a monograph entitled *Duties and Responsibilities of Directors of Not-for-Profit Corporations*, specifically aimed at helping directors of Canadian not-for-profit organizations. Co-authored by Hugh M. Kelly, Q.C., and Mark R. Frederick, this publication quickly became a bestseller for CSAE, with more than 10,000 copies sold. Its second and third editions, authored by Hugh Kelly and published in 2004 and 2011, have continued to be widely recognized as the primer for board directors and an invaluable resource for organizations in board orientation sessions.

Like previous versions, this new edition, edited and updated by WATSON, is designed to provide directors of not-for-profit organizations in Canada with information about potential liability they may face in their role as director. Informing directors of their responsibilities should be a key element of any annual orientation program.

Important Note

This publication provides general information only. It is not intended to provide legal or professional advice and should not be considered or relied upon as such. If legal or other professional advice is required regarding a specific issue or circumstance, the services of a professional should be sought.

Note also that with the increasing complexity of legislation and corporate activity in which not-for-profit organizations engage, it is not possible in a publication such as this to explore every requirement and nuance that a director or officer might face. This publication is intended to address the most frequent and common issues.



Introduction



Purpose

Governance is high on the agenda in all sectors—public, private, and not-for-profit. Voluntary organizations driven by community values and working for public benefit are increasingly expected to demonstrate how well they are governed. Aside from what is expected by members and stakeholders such as donors, government, and the public, there is growing recognition that good governance leads to better organizational performance. For these reasons, and due to the increasingly complex environment in which not-for-profit corporations operate, governance is high on the agenda of most boards. Directors are seeking guidance on their roles, responsibilities, and emerging governance practices.

The purpose of this publication is to highlight the important duties and liabilities of directors of not-for-profit corporations and to offer general practice points to help directors meet their obligations, reduce liability risk, and govern more effectively.

Further resources about board effectiveness are available from CSAE to build on the information set out in this publication.

Legislation

Not-for-profit corporations may be incorporated federally or provincially. In choosing the appropriate jurisdiction, consideration is typically given to the anticipated scope of the organization and applicable legal requirements or protection provided in each jurisdiction.

As the importance and complexity of the not-for-profit sector continues to grow in Canada, there is also a trend, both provincially and federally, to reform not-for-profit legislation. Generally, the legislative reforms strive to achieve accountability and transparency

in governance and at the same time afford reasonable protection to individual directors who conscientiously carry out their service to the organization and the community they serve.

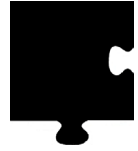
As a director of a not-for-profit corporation, it is important to understand the legislation pursuant to which your organization is incorporated and monitor any proposed changes. The Parliament of Canada and the Legislature of Ontario have recently completed an overhaul of their respective legislations governing not-for-profit corporations. At the date of publication, the *Canada Not-for-Profit Corporations Act*¹ (*Canada NFP Act*) is in force. Not-for-profits incorporated federally under the previous *Canada Corporations Act*² were required to transition by October 17, 2014. The Ontario *Not-for-Profit Corporations Act, 2010*³ (*Ontario NFP Act*), although given third reading and royal assent, is not yet in force. Not-for-profits incorporated under the previous *Corporations Act*⁴ in Ontario will be required to take action to transition to the new legislation upon proclamation. In 2008–2009, the government of British Columbia took steps to initiate public consultations and a formal review of the British Columbia *Society Act*⁵ (*BC Society Act*). In March 2015, an updated *Societies Act* was introduced in the BC legislature and could receive approval and royal assent in 2015, but would not likely come into force until regulations are finalized. There would similarly be a transition period and process for organizations to adopt changes to constitutions and bylaws.

In addition to legislation that provides for the incorporation of a not-for-profit corporation, there are many legislative and regulatory provisions that may affect the corporation and/or the directors. It is incumbent on directors to be familiar with all such provisions.

Not-for-Profit Corporations

This publication focuses on not-for-profit corporations.⁶ There is a wide range in size, mission, and activities of not-for-profit corporations, including: trade and community associations; sporting

Not-for-Profit Corporations



Not-for-Profit Corporations



and athletic organizations; social clubs; arts groups; neighbourhood and community organizations; health and social service organizations; human rights and civil liberties groups; and so on.

Some not-for-profit corporations may be designated as charities.⁷ Directors of charities will need to familiarize themselves with the specific legal obligations that apply to charities. (Some of these specific legal provisions are noted throughout this publication.)

Not-for-profit corporations have many characteristics in common with business or for-profit corporations. In both cases, there is a distinction in law between the corporation (a separate legal person) and the individuals who are directors, officers, and members. Not-for-profit entities formally incorporate for many of the same reasons as for-profit entities, including the benefit of limited liability that the corporate form provides for members, directors, and other persons connected with the organization.⁸

The main distinctions between for-profit and not-for-profit corporations include:

- a not-for-profit corporation has members (as opposed to shareholders),
- members of a not-for-profit corporation may not receive any financial gain, and
- the powers of a not-for-profit corporation are limited to what is written into its objects.

Because an entity is a not-for-profit corporation does not necessarily mean that it is not permitted to operate at a profit.⁹ The main difference that distinguishes a not-for-profit corporation from its commercial counterpart is that if the activities of a not-for-profit corporation produce a profit on its operations, the individual members of the corporation do not personally benefit as do the shareholders in a business corporation.

It should be noted that liability for income tax is not automatically excluded simply because the organization is incorporated as a not-for-profit corporation. The *Income Tax Act (Canada)* contains express provisions as to what tax is or is not payable.¹⁰

Members, Directors, and Officers

Like its business counterpart, a not-for-profit corporation is composed of:

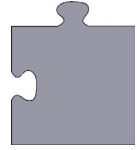
- members (the equivalent to shareholders in a business corporation),
- directors (elected by the members), and
- officers (appointed by the directors).

All not-for-profit entities that are incorporated are required to identify a membership base. Membership may be “closed” (restricted to the people who make up the board of directors)⁶ or “open” (a broad membership base). There are pros and cons with each model. In most cases, individuals become members by application to, and approval by, the existing board of directors.

Individuals become directors of a not-for-profit corporation in accordance with the corporation’s bylaws. Generally, the members elect directors. However, in some jurisdictions, individuals may become directors by virtue of holding another office (ex officio director) or by appointment (subject to restrictions).¹¹

While directors may also be officers of the corporation and fulfill certain corporate roles and functions (such as the duties of a president, treasurer, or secretary of the organization), it is more common today in larger not-for-profits for the officer roles to be fulfilled by paid staff appointed by the directors.

Members, Directors, and Officers



About WATSON



Since its foundation in 2005, WATSON has helped hundreds of organizations establish or improve their approach to governance, conduct board and director evaluations, implement board and CEO succession plans, and connect with value-adding directors. WATSON's clients include major trade and professional associations, governments (local, provincial, and federal), public sector entities of various models, not-for-profit organizations, private corporations, listed companies, and financial institutions.

WATSON is known for its leading edge approach to governance and for providing clear, practical, and cost-effective advice. We effectively bridge the disciplines of evaluation and governance with legal expertise. Our professionals are called upon regularly as trusted advisors to discuss foundational and emerging governance practices, and to help clients navigate difficult issues. Our clients appreciate our expertise in identifying key issues and providing creative solutions to meet a broad range of business objectives. Our system of situation analysis, together with our knowledge of governance practices worldwide, helps us identify each client's key concerns and develop an approach based on sound governance principles, yet handcrafted to address each client's unique legal and operating environment.

WATSON is proud to work with associations to help them shape how they practice governance, evaluate their performance, educate their boards, improve how they manage the board and find their directors.

Visit www.watsoninc.ca to find out more about WATSON or call us at 604.569.2071 to attend our association education course, Governing with Intention™.