

Corporate Governance Principles for Non-Profit Entities

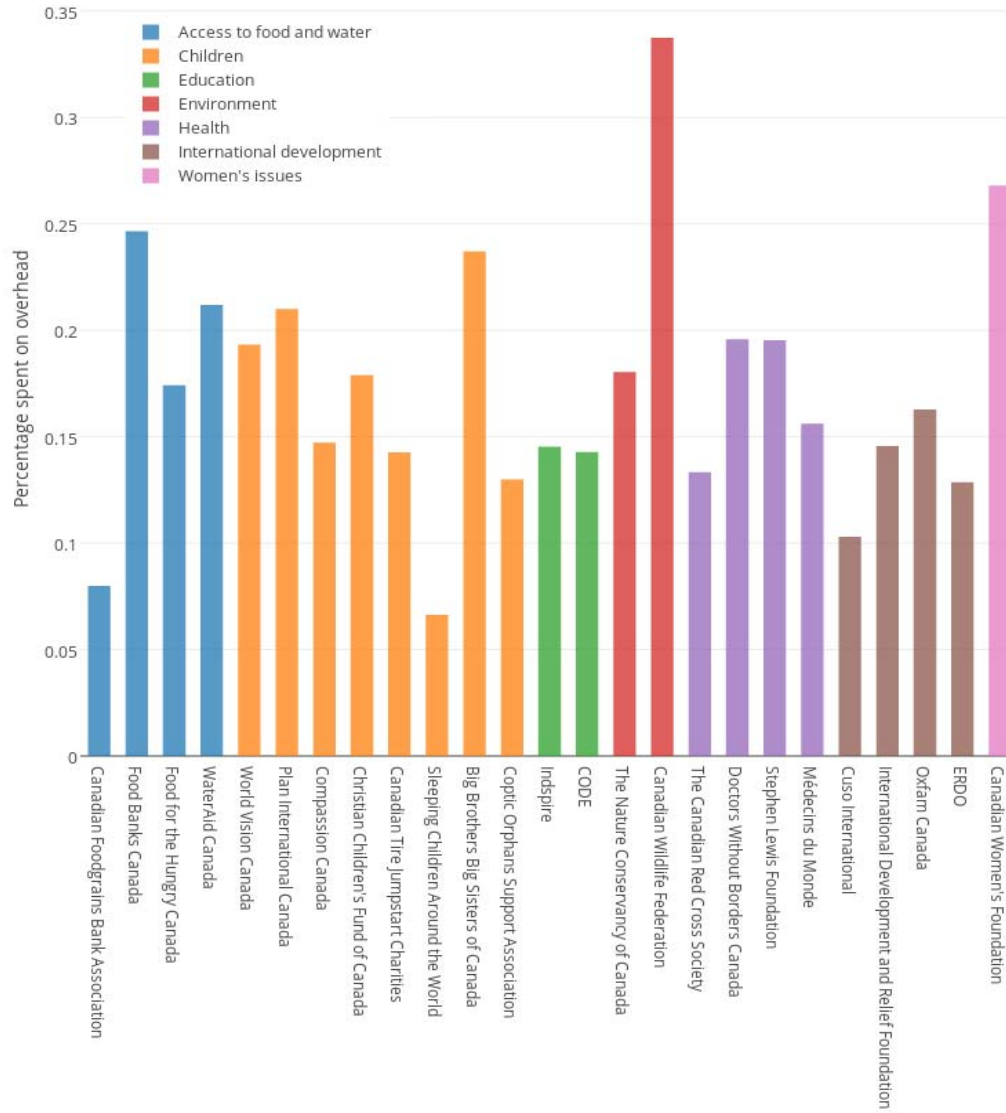
Presented by: Kenneth Jull
May 23, 2019



Non-Profit Sectors

- Canada has one of the largest and most vibrant nonprofit and voluntary sectors in the world.
- It accounts for 6.8 percent of the nation's gross domestic product (GDP) and employs 12 percent of Canada's economically active population.
- With the significant role nonprofit organizations play in Canadian life and the increasing demand for accountability in nonprofit organizations, more attention is being drawn to governance issues.

The Financial Post's 25 Charities of the Year: Percentage spent on overhead



Thesis: Four Points for Non-Profit Governance



1. Good faith and best interests of the corporation parallel but are not identical to the tests articulated for profit corporations;
2. Non-profits are subject to corporate criminal liability which may be an ethical blind spot;
3. There are risks of being a victim of fraud but also risks of non-compliance on a corporate level;
4. Matrix risk management is essential

Thesis: Four Points for Non-Profit Governance



1. Good faith and best interests of the corporation parallel but are not identical to the tests articulated for profit corporations;

Canada Not-for-profit Corporations Act (S.C. 2009, c. 23)



148 (1) Every director and officer of a corporation in exercising their powers and discharging their duties shall

(a) act honestly and **in good faith** with a view to the **best interests of the corporation**; and

(b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

(2) Every director and officer of a corporation shall comply with

(a) this Act and the regulations; and

(b) the articles, the by-laws and any unanimous member agreement.



Guide to the Not-for-Profit Corporations Act, 2010



- When ONCA comes into effect(target of early 2020), it will:
- make the incorporation process for new not-for-profit corporations more efficient
- make a new distinction between public benefit corporations and other not-for-profit corporations
- clarify that not-for-profit corporations can engage in commercial activities if the activities support the corporation's not-for-profit purposes
- a not-for-profit corporation may be subject to restrictions on its activities imposed by other legislation such as the Income Tax Act

Guide to the Not-for-Profit Corporations Act, 2010



- provide clearer rules for governing the corporation and increasing accountability
- ONCA will provide a statutory duty of care for directors, which will require them to act honestly and in good faith with a view to the best interests of the corporation, and to exercise reasonable care, diligence and skill
- set out a due diligence and good faith reliance defence for directors
- a director will not be legally liable in certain circumstances if they acted with the care, diligence and skill a reasonably careful person would have acted in similar circumstances
- list specific requirements for directors and officers to report a conflict of interest in certain circumstances

Good Faith



Beattie v. Women's College Hospital 2018 CarswellOnt 18570, 2018 ONCA 872,

The appellants are both doctors who practiced for many years in the respondent hospital's urgent care centre. The respondent closed the urgent care centre and, as a consequence, terminated their privileges.

The trial judge dismissed the appellants' action for damages for wrongful dismissal on the ground that it was barred by s. 44(5) of the Public Hospitals Act, R.S.O. c. P.40. That provision provides that if the board of a hospital decides to cease to provide a service:

No action or other proceeding for damages or otherwise shall be instituted against [the hospital] for any act done in **good faith** in the execution or intended execution by a board of its authority [to cease to provide the service] or for any alleged neglect or default in the execution in good faith by a board of such authority.



Objective Criteria versus local agendas



Ottawa Humane Society v. Ontario Society for the Prevention of Cruelty to Animals 2017 CarswellOnt 14316, 2017 ONSC 5409,

- A few affiliates then loaded the board with their own executive directors and she states that it became difficult to govern because the directors or executive directors of the affiliates were more interested in advancing their local agendas rather than success of the OSPCA
- She adds that under the **new governance model**, the board will vote for their own replacements pursuant to a broader set of criteria based on **skills, competencies experience and diversity** rather than merely being affiliate member. The stated goal is to seek more diverse and qualified individuals, including, for example, an indigenous representative.

Non-Profits and the Business Judgment Rule



Ottawa Humane Society v. Ontario Society for the Prevention of Cruelty to Animals 2017 CarswellOnt 14316, 2017 ONSC 5409,

- In *Hadjor v. Homes First Society*, 2010 ONSC 1589, 70 B.L.R. (4th) 101 (Ont. S.C.J.), Justice Belobaba reviewed the law with respect to the **Business Judgment Rule** this way:

48 First, the Business Judgment Rule. In *UPM-Kymmene Corp. v. UPM-Kymmene Miramichi Inc.*, this Court explained the Business Judgment Rule as follows:

The Business Judgment Rule protects boards and directors from those that might second-guess their decisions.

The Court looks to see that the directors made **a reasonable decision, not a perfect decision**. This approach recognizes the autonomy and integrity of a corporation and the expertise of its directors.

Non-Profits and the Business Judgement Rule



Ottawa Humane Society v. Ontario Society for the Prevention of Cruelty to Animals 2017 CarswellOnt 14316, 2017 ONSC 5409,

- Having reviewed the material filed by both sides, I have no difficulty coming to the conclusion that the decision of the board, acting in the best interests of the OSPCA, was to put in place a modern "best-practices" governance structure and is entitled to deference under the Business Judgment Rule.

Public Sector Boards



DUAL LOYALTIES ON NON-PROFIT BOARDS: SERVING TWO MASTERS

Clifford S. Goldfarb

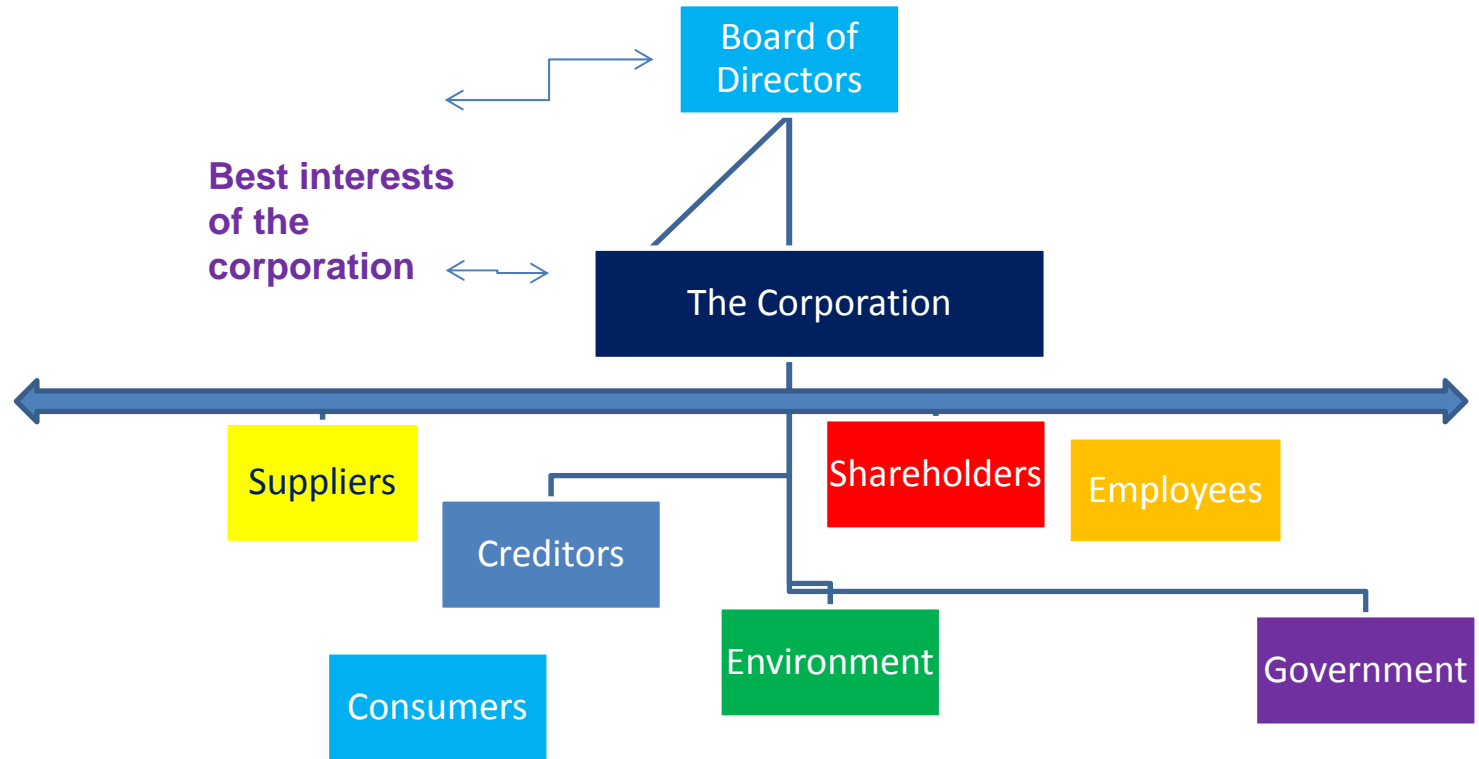
CBA-OBA National Symposium on Charity Law

- It is extremely common for the boards of non-profit organizations to consist in whole or in part of representatives of the constituent bodies, stakeholders or members. For example, invariably a hospital support foundation will have on its board the president of the hospital and the chair of the board of the hospital. Hospital boards have representatives of the medical and nursing staff.



Peoples v. Wise: Moving in the Direction of Overlapping Models

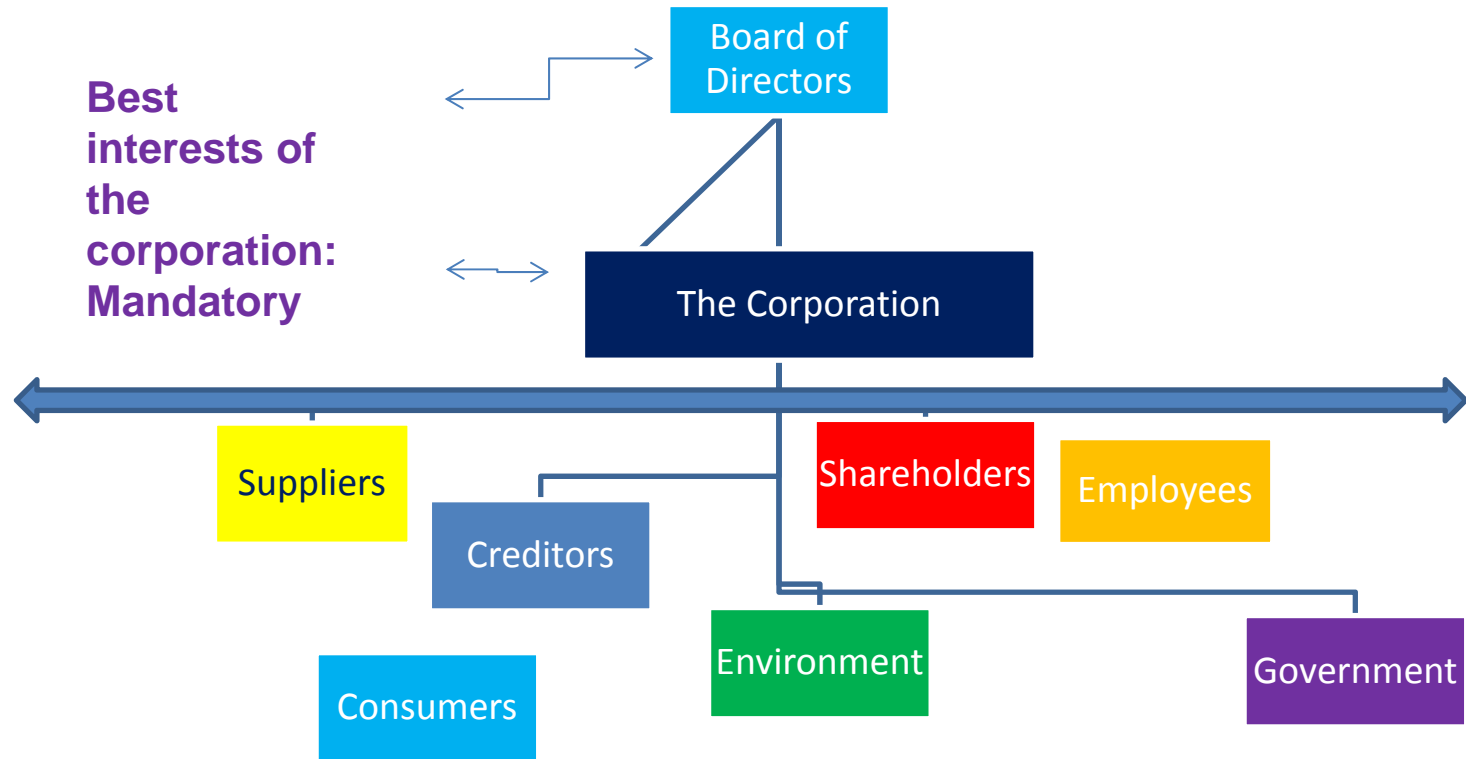
- We accept as an accurate statement of law that in determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, inter alia, the interests of **shareholders**, **employees**, **suppliers**, **creditors**, **consumers**, **governments** and the **environment**.



BCE Inc. v. 1976 Debentureholders, 2008
CarswellQue 12595, 2008 SCC 69 at paragraph 39

- In *Peoples Department Stores*, this Court found that although directors **must** consider the best interests of the corporation, it may **also be appropriate**, although **not mandatory**, to consider the impact of corporate decisions on shareholders or particular groups of stakeholders. As stated by Major and Deschamps JJ., at para. 42:
- "We accept as an accurate statement of law that in determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, *inter alia*, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment."





- Discretionary consideration of other stakeholders

Thesis: Four Points for Non-Profit Governance



2. Non-profits are subject to corporate criminal liability which may be an ethical blind spot;

Each of us tends to believe that we see the world objectively; to see ourselves as more fair, unbiased, competent, and deserving than average; and to be overconfident about our abilities and prospects. This tendency to view the self in positive terms is heightened when the characteristic at issue is socially desirable—as is the case with ethical behavior. Indeed, attorneys tend to believe that their own ethics and their firm’s ethical standards are more stringent than those of other attorneys and other firms. (Robbennolt and Sternlight, “Behavioral Legal Ethics” (2013) 45 Ariz. St. L.J 1107. at 1116.)



Westray and Criminal Negligence



Senior Officer

“**Senior officer**” is now defined in s.2 of the *Criminal Code* as follows:

“**Senior officer**” means a representative who plays an important role in the establishment of the organization’s policies *or*

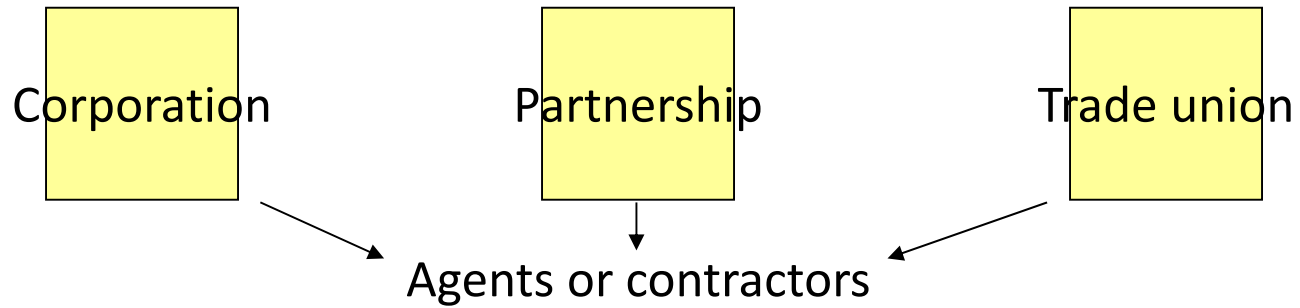
>> policy

>> operational

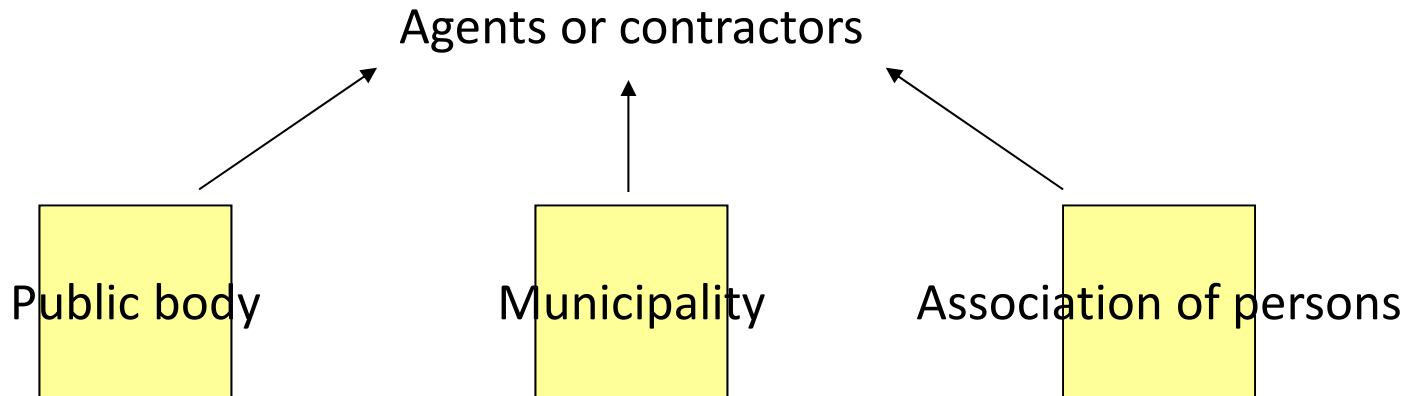
is responsible for managing an important aspect of the organization’s activities and, in the case of a body corporate, includes a director, its chief executive officer and its chief financial officer.

C-45: Wider Organizations

Private

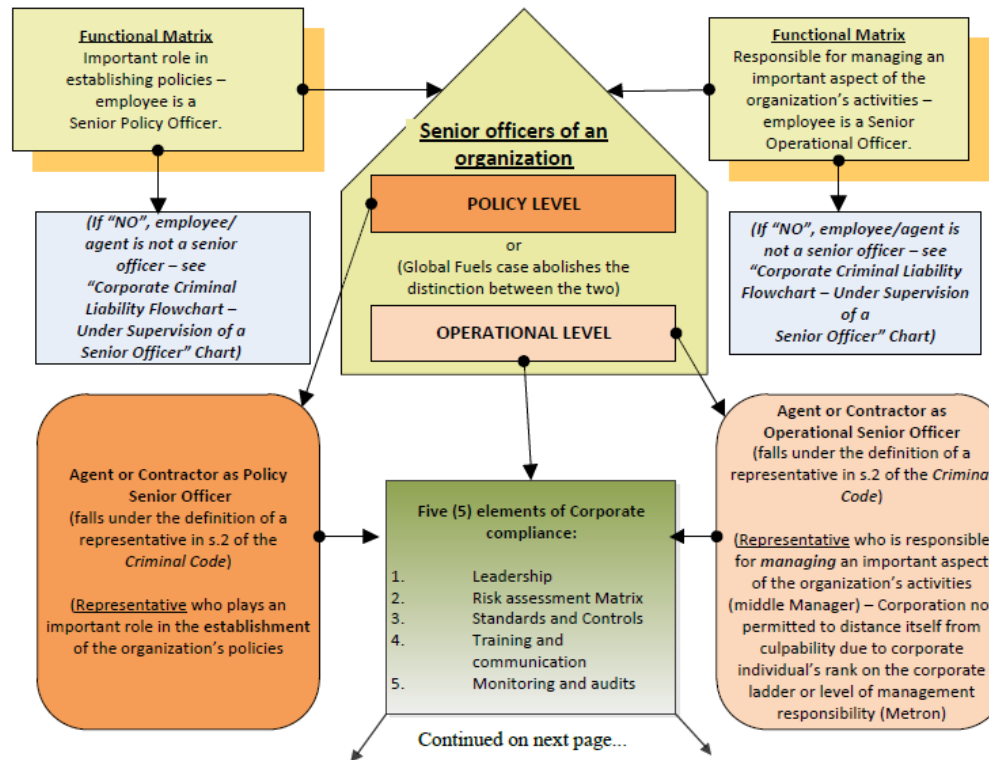


Public



Corporate Criminal Liability Flowchart

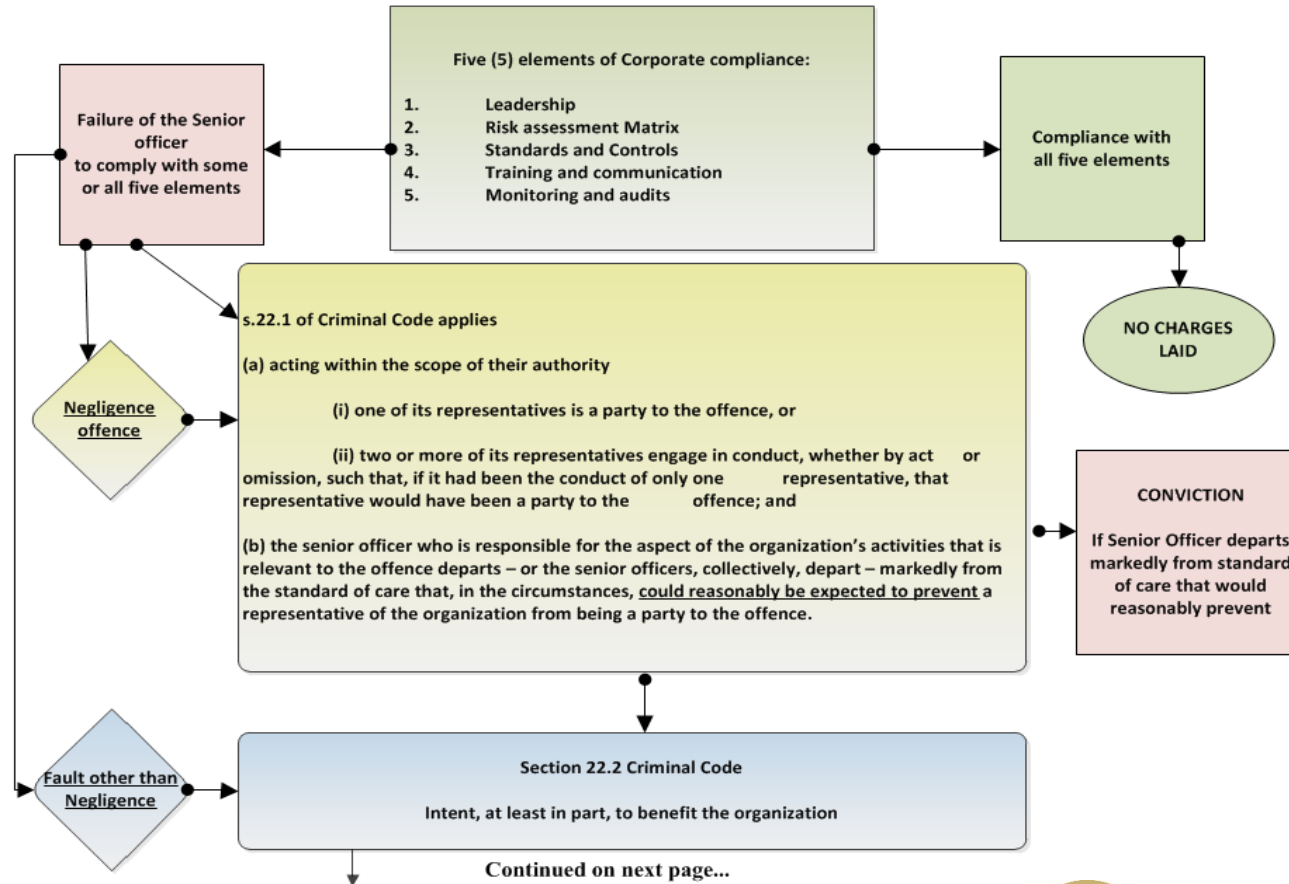
Senior Officer Level



Corporate Criminal Liability Flowchart

Senior Officer Level

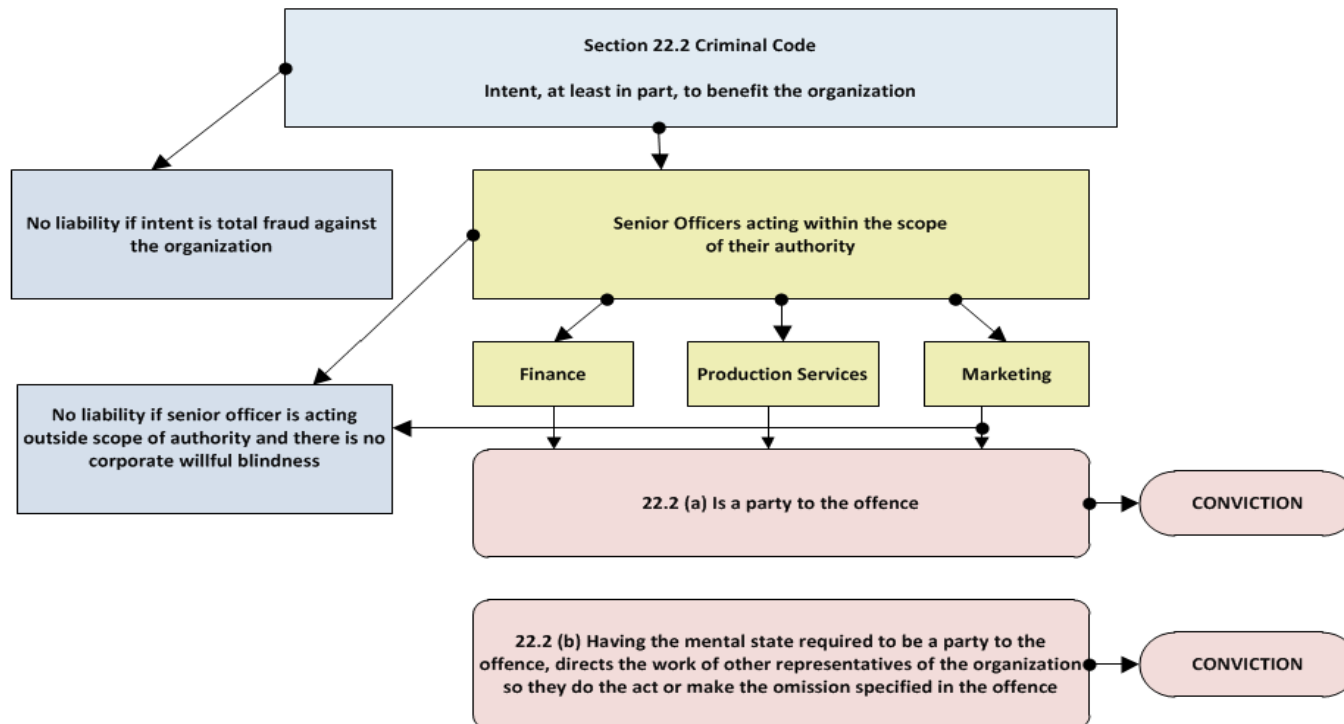
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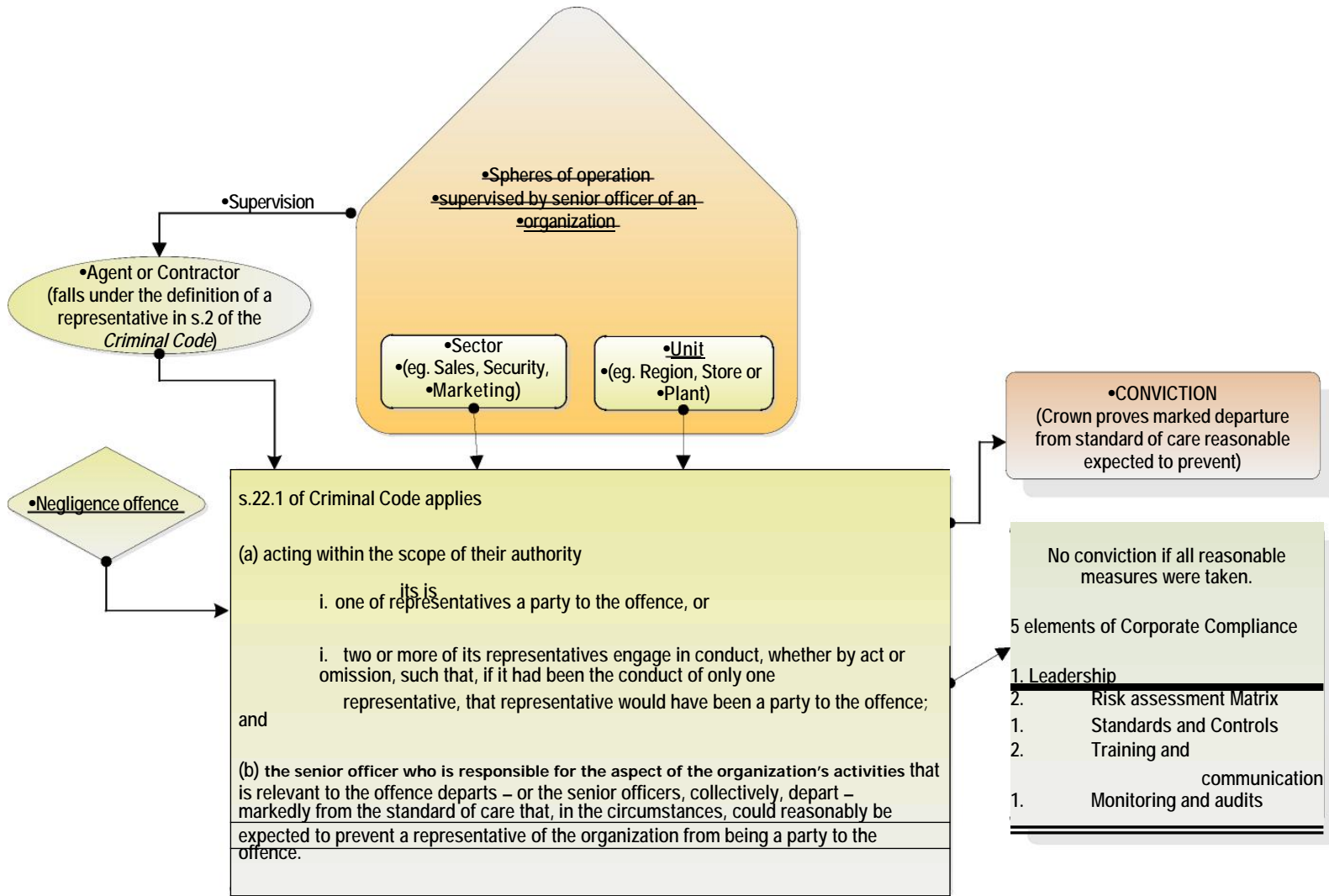
Corporate Criminal Liability Flowchart

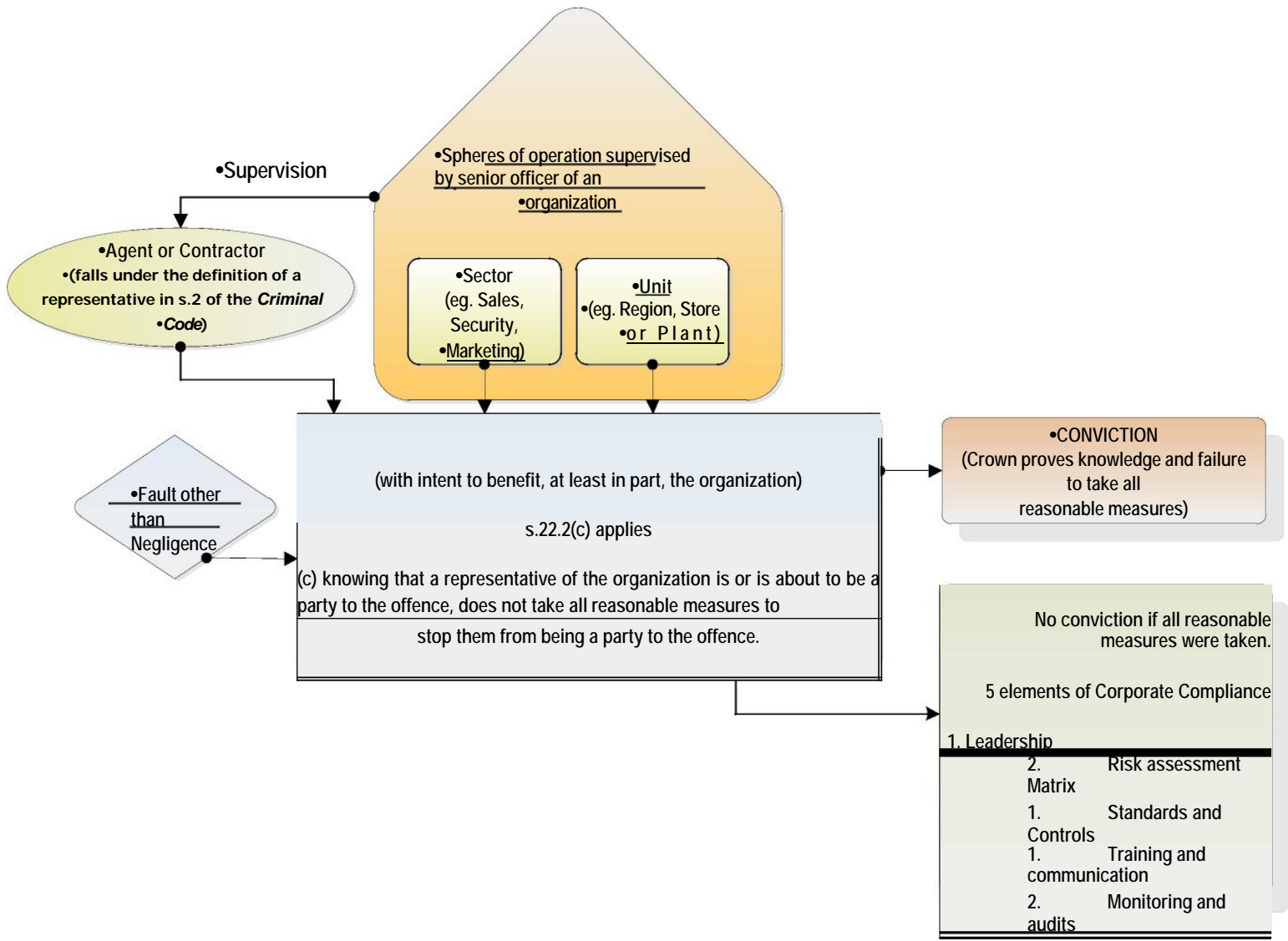
Senior Officer Level

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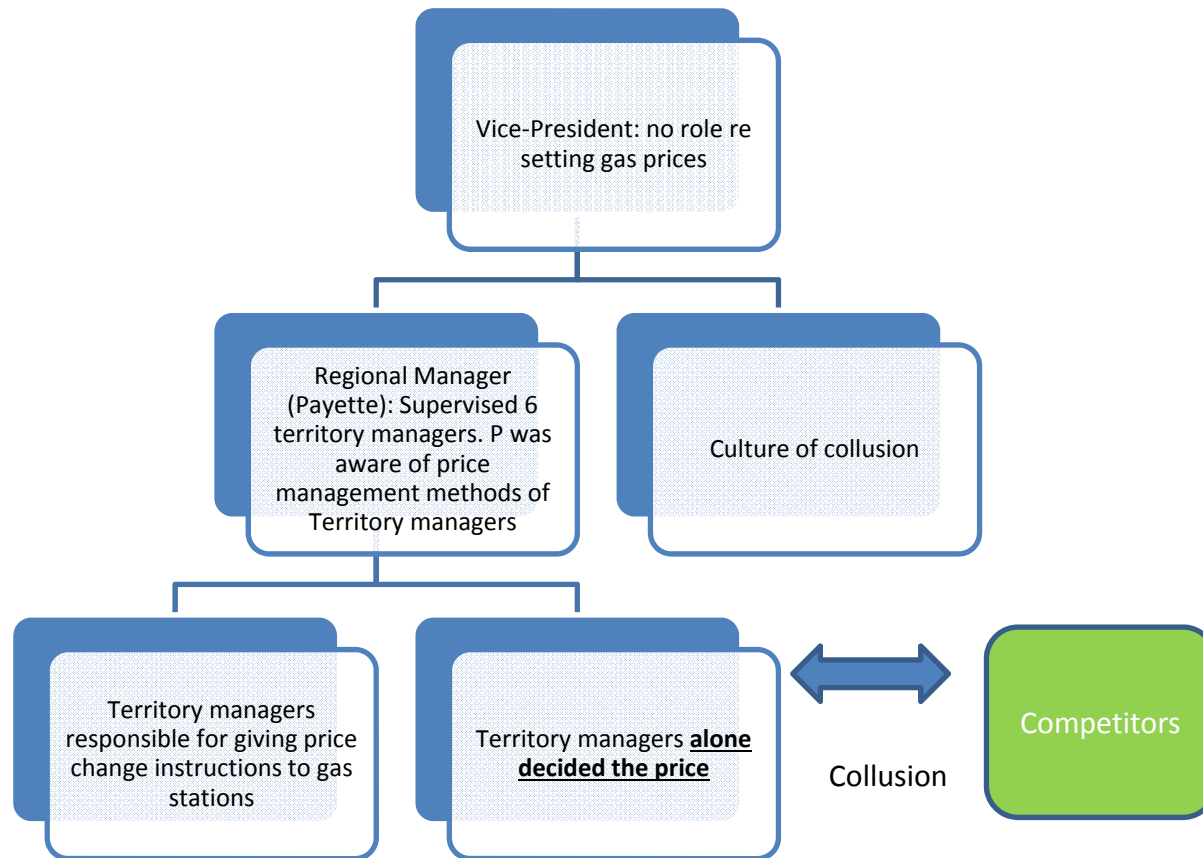


Corporate Criminal Liability Flowchart – Under Supervision of a Senior Officer

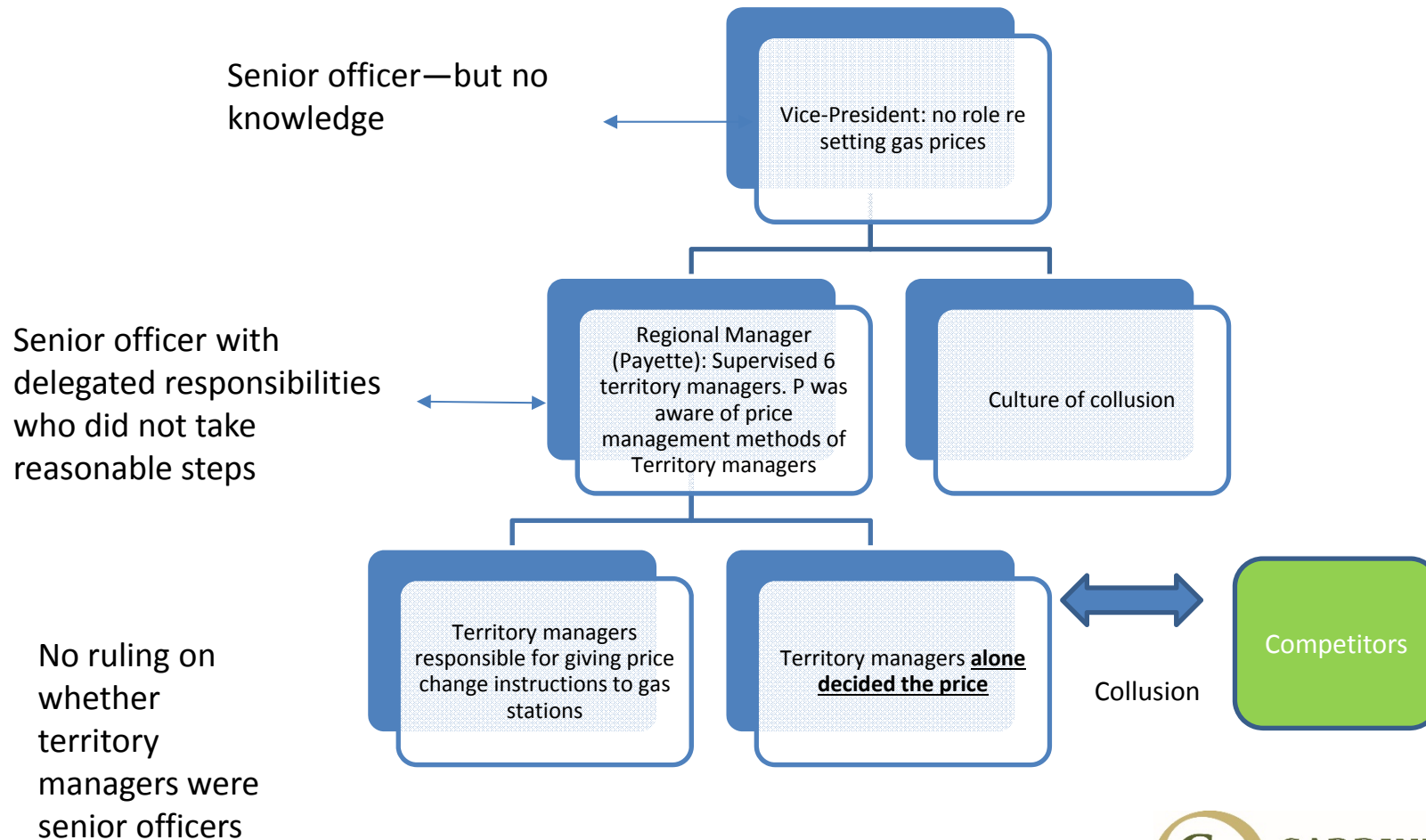


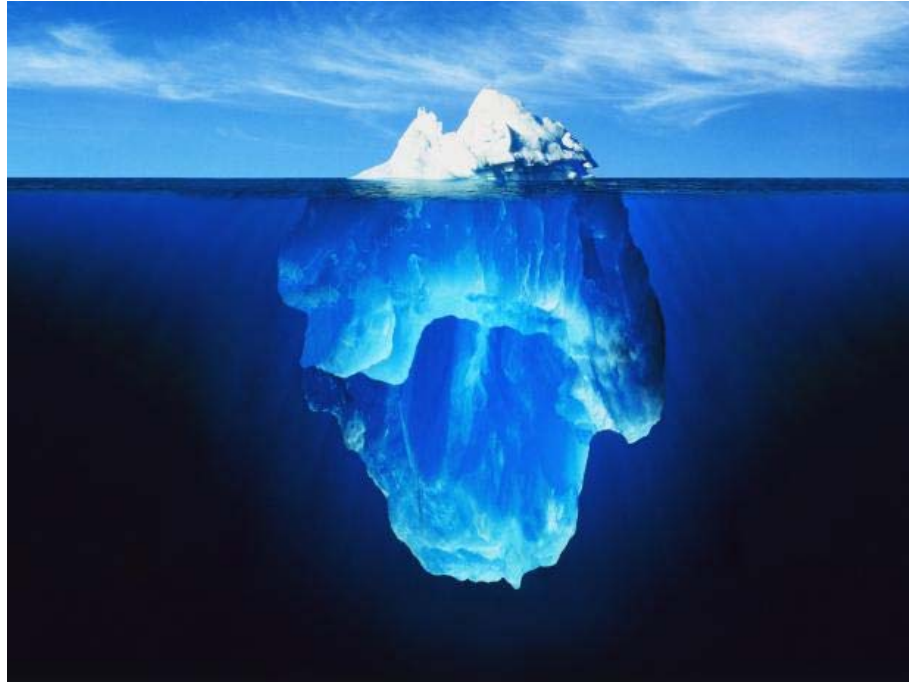


The New Law of Expanded Organizational Criminal Liability



The New Law of Expanded Organizational Criminal Liability





(3) There are risks of being a victim of fraud but also risks of non-compliance on a corporate level

Risk from Fraud

Fraud in Canadian nonprofit organizations as seen through the eyes of Canadian newspapers, 1998–2008 Qiu Chen, Steven Salterio, & Pamela Murphy Queen's University, Kingston, Ontario

- We found that the median loss from fraud within Canadian nonprofit organizations was \$27,244, significantly smaller than the median loss of US\$100,000 for nonprofits in the United States in 2004 (Greenlee, Fischer, Gordon, & Keating, 2007).
- However, the median fraud loss in Canada represents about 5% of annual revenues, quite close to the Association of Certified Fraud Examiners (ACFE) estimate of 7% of annual revenues for all U.S. organizations (ACFE, 2008).
- Smaller nonprofit organizations—those employing fewer than 50 people and/or having annual revenues of less than \$100,000—experienced the most number of fraud cases and the highest losses relative to their annual revenue.

Risk

Fraud in Canadian nonprofit organizations as seen through the eyes of Canadian newspapers, 1998–2008 Qiu Chen, Steven Salterio, & Pamela Murphy Queen's University, Kingston, Ontario

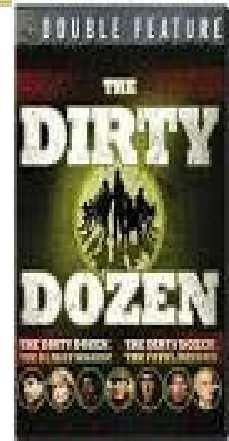
- We found that fraudsters within Canadian nonprofit organizations had a slightly different face than those in the rest of the world along one dimension: gender.
- The typical Canadian perpetrator is almost as likely to be a woman as a man (46% were women and 54% were men), whereas perpetrators worldwide are overwhelmingly male (85%) (PricewaterhouseCoopers, 2007).
- The gender breakdown in the U.S. is closer to that of Canada (60% of U.S. perpetrators were male; ACFE, 2008), but the Canadian literature still points to more female perpetrators than most other fraud literature. We posit this difference might reflect the greater percentage of women employed by nonprofit organizations in general.



IRS's Dirty Dozen scams — 2019 edition

<https://www.journalofaccountancy.com/news/2019/mar/2019-irs-dirty-dozen-tax-scams-201920830.html>

- **Abusive tax shelters, trusts, and conservation easements (IR-2019-47):** The IRS warned taxpayers to stay away from abusive schemes that tax cheats often promote. They include abusive trusts, abusive micro-captive insurance shelters, and abusive syndicated conservation easements. This is the first year that the IRS has included abusive trusts and conservation easements on the list. In earlier years, only abusive tax shelters were included.



Guindon v. Canada 2015 SCC 41 ("*Guindon*")

Agreed Facts before the Tax Court:

- The Settlor was going to acquire timeshare units called Biennial Vacation Ownership Weeks ("VOWs") from TDL, which held the property of [Hawkes Nest Plantation Resort/Arawak Inn in Turks and Caicos Island](#) [sic];
- After acquiring the VOWs the Settlor would gift the VOWs to the Trustee, who in turn would exchange the VOWs to the beneficiaries of the Trust, in return for the payment of a vendor take-back charge;
- The amount of the vendor take-back charge that was to be paid by beneficiaries of the Trust was **\$3,248** per VOW;
- It was anticipated that the beneficiaries would donate the VOWs to a registered Canadian charitable organization for a receipt for the fair market value of the donated VOWs; and
- The VOWs were valued at **\$10,825** per VOW.

Turks and Caicos: Providenciales



Guindon v. Canada 2015 SCC 41 ("*Guindon*")

- Ms. Guindon agreed, for a fee of \$1,000, to provide an opinion letter on the tax consequences of this program on the basis of a precedent provided by the promoters. She recommended that the promoters have a tax lawyer and an accountant review her opinion to ensure its accuracy, as the opinion did not fall within her field of expertise, but nonetheless provided the letter knowing that it was intended to be part of the promotional package for the scheme. She wrote that the transactions would be implemented based on supporting documents that she had been provided with and had reviewed. She had not reviewed the supporting documents.

Guindon v. Canada 2015 SCC 41 ("Guindon")

- Ms. Guindon was also the president and administrator of a registered charity, Les Guides Franco-Canadiennes District d'Ottawa. In November 2001, this charity agreed to become the recipient of the donated timeshares. The promoters would then sell the timeshares on behalf of the charity which would receive a minimum of \$500 per unit sold.

Guindon v. Canada 2015 SCC 41 ("*Guindon*")

- The scheme was a sham: no timeshare units were created and no transfers from the donors to the charity occurred. The promoters prepared 135 tax receipts, which were issued by the charity and signed by Ms. Guindon and the treasurer of the charity. The total receipted amount was \$3,972,775. The Minister of National Revenue disallowed the charitable donation tax credits claimed by the donors. On August 1, 2008, the Minister assessed Ms. Guindon for penalties under s. 163.2 of the ITA for each of the tax receipts issued on the basis that she knew, or would have known but for wilful disregard of the ITA, that the tax receipts constituted false statements.

Hawkes Nest Plantation Development Parcel



Hawkes Nest Plantation Development Parcel



Grand Turk Cruise Centre



Guindon v. Canada 2015 SCC 41 ("*Guindon*")

- The Appellant, Julie Guindon, was assessed penalties totaling **\$546,747** under subsection 163.2(4) of the Income Tax Act (the "ITA"). Ms. Guindon is a lawyer practicing mainly in the areas of family law and wills and estates. She was retained to provide a legal opinion on a charitable-donation plan called "The Global Trust Charitable Donation Program" (the "Program").
- Ms. Guindon provided a legal opinion vouching for the plan. She provided a signed copy of her legal opinion without having reviewed all of the documents referred to in the opinion.
- Ms. Guindon accepted a retainer of one thousand dollars (\$1,000) to prepare an opinion letter and advised that the area of tax law did not fall within her field of expertise.

Thesis: Four Points for Non-Profit Governance



4. Matrix risk management is essential

Matrix Analysis and Levels of Audit

Impact trumps likelihood where equal

MATRIX WHERE GRAVITY OF HARM TRUMPS PROBABILITY

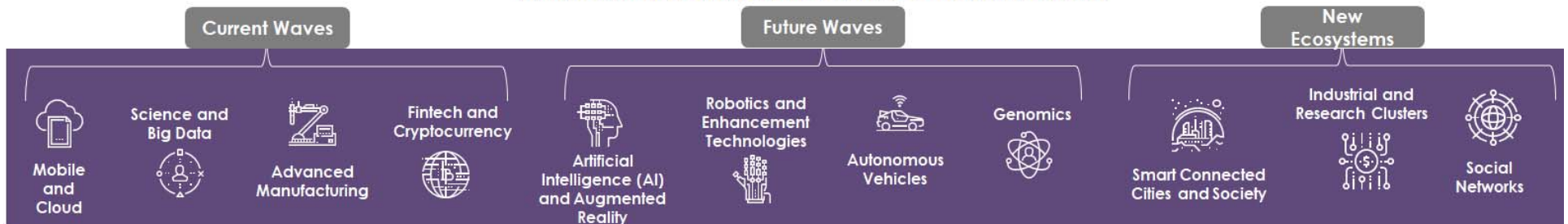
Impact			
<i>Significant</i> ↑	Significant Management effort required	Internal investigations with external counsel and retained experts and significant remediation	Act now: immediate and comprehensive remediation and self-report to the Regulator
<i>Moderate</i>	Management effort worthwhile	Extensive management essential	Internal investigations and remediation commenced
<i>Minor</i>	Accept risks	Accept risks with monitoring	Management effort required
	<i>Low</i>	<i>Medium</i>	<i>High</i>
			Likelihood →

The Essential Elements of Corporate Compliance

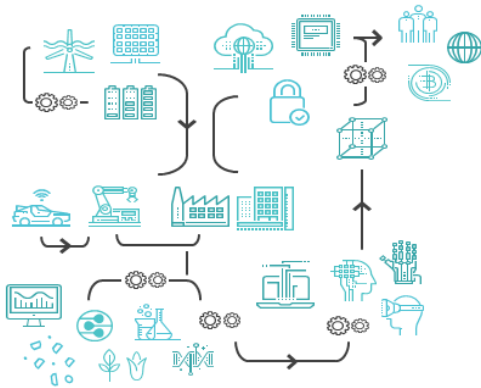
USSG's 7 Elements of an Effective Compliance Program	13 Good Practices by the OECD on Internal Controls, Ethics, and Compliance	UK's 6 Principles for "Adequate Procedures"
1. Standards and procedures to prevent and detect criminal conduct	1. Risk assessment as basis for effective internal controls and compliance program	1. Proportionate procedures
2. Leaders understand / oversee the compliance program to verify effectiveness and adequacy of support; specific individuals vested with implementation authority / responsibility	2. Policy that clearly and visibly states bribery is prohibited	2. Top level commitment
3. Deny leadership positions to people who have engaged in misconduct	3. Training – periodic, documented	3. Risk assessment
4. Communicate standards and procedures of compliance program, and conduct effective training	4. Responsibility – individuals at all levels should be responsible for monitoring	4. Due diligence
5. Monitor and audit; maintain reporting mechanism	5. Support from senior management – strong, explicit and visible	5. Communication
6. Provide incentives; discipline misconduct	6. Oversight by senior corporate officers with sufficient resources, authority, and access to Board	6. Monitoring and review
7. Respond quickly to allegations and modify program	7. Specific risk areas – promulgation and implementation programs to address key issues	
	8. Business partners due diligence	
	9. Accounting – effective internal controls for accurate books and records	
	10. Guidance – provision of advice to ensure compliance	
	11. Reporting violations confidentially with no retaliation	
	12. Discipline for violations of policy	
	13. Re-assessment – regular review and necessary revisions	
NOTE: A general provision requires periodic assessment of risk of criminal conduct and appropriate steps to design, implement, or modify each element to reduce risk		

Minister Bains announces Canada's Digital Charter

MAKING CANADA A COMPETITIVE, DATA-DRIVEN, DIGITAL ECONOMY NATIONAL DIGITAL AND DATA CONSULTATIONS



Technologies are reshaping the way people live and connect, the nature of work and industrial production



- Big Data: 90% of the world's data created in the last 2 years
- 80B connected devices by 2025
- Industrial robots to reach 3M by 2020
- AI – Global GDP 14% higher in 2030
- Nearly 10% of jobs automated
- 2B active Facebook users
- 4B Google search per day – 1.2T annually
- Cybercrime to cost \$6T annually by 2021



Digital Charter

- Requiring organizations to provide individuals with the information they need to make informed decisions, including requiring specific, standardized, plain-language information on the intended use of the information, the third parties with which information will be shared, and prohibiting the bundling of consent into a contract.



Questions?



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