When should charities indemnify directors?

ROBERT HAYHOE

A recent decision of the Ontario Court of Appeal clarifies when a charity must indemnify its directors.

Pandher v. Ontario Khalsa Darbar, [2010] O.J. No. 1471, was an appeal of the costs portion of an Ontario Superior Court of Justice decision in what appears to have been a bitter governance dispute between groups of members of a Sikh temple. Relying on the indemnity provision in the temple's constitution, the appeal court decided that the costs of the successful minority directors were to be paid by the temple, not by the unsuccessful majority directors.

The Superior Court of Justice costs decision had found that "[t]o an extent it will be unfair to look to the Ontario Khalsa Darbar to pay costs. Surely the costs arose as a result of the action of its Board of Directors. In the end result it is appropriate that all defendants except the Ontario Khalsa Darbar be jointly and severally responsible to pay these costs" (of over $200,000).

However, the appeal court confirmed that absent *male fides*, it would give effect to the director's indemnity provision in the temple's constitution, and ordered that the costs of the successful directors be paid by the temple rather than the directors. The appeal court observed that "the primary purpose of indemnification is to provide assurance to those who become directors that they will be compensated for adverse consequences that ensue from well-intentioned acts taken on behalf of the corporation. This policy applies with force to not-for-profit organizations." It turned down a new argument that the court should rely on its inherent jurisdiction over charities to refuse to apply the indemnity, but went on to doubt that the court had such a power.

The court's willingness to apply the indemnity is an interesting conclusion that calls into question a long-standing position of the Ontario Public Guardian and Trustee (PGT). The PGT takes the position, consistent with the common law of trusts, that a director of a charity is not permitted to benefit directly or indirectly from the directorship. The PGT has traditionally extended its view of a director benefit to include director indemnities or insurance. As of 2001, a regulation under the Ontario *Charities Accounting Act* (O. Reg. 4/01, *Approved Acts of Executors and Trustees*) provides that it is not a breach of trust for a charity to indemnify its directors if it considers certain items prior to indemnifying:

- the degree of risk involved in administering the charity — how likely it is that the director, officer or trustee will suffer a financial loss through administering the charity;
- whether there are other practical means of significantly reducing the risk;
- whether the amount and cost of the insurance is reasonable given the risk to the director, officer or trustee of suffering a financial loss. If the risk of loss is low, the cost of insurance purchased by a charity should also be low;
- whether the cost of the insurance is reasonable given the revenue of the charity — it is not usually reasonable for a charity to spend a significant part of its income on liability insurance;
- whether the charity will benefit by giving the indemnity or buying the insurance. For example, the charity may attract better directors or be able to get more income if it buys the insurance.

This regulation confirms by implication the PGT's view that absent this regulation, indemnity is a breach of trust as a matter of common law. In principle, this would be the case in provinces other than Ontario, notwithstanding that no such analogous saving provision exists.

The decision of the Ontario Court of Appeal suggests that the purpose of giving a directors' indemnity is to assist the corporation by protecting directors, not to benefit the directors. After all, there would be no need for the indemnity absent being a director, so the indemnity is designed to put the director in the position that he or she would have been in without the office (a neutral position), not to provide a benefit. Thus, the court's decision should give charity directors in Ontario and in other provinces considerable comfort about the enforceability of director indemnities absent *male fides*. Nonetheless, Ontario charities should continue to comply with the *Charities Accounting Act* regulation out of an abundance of caution. ■

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Personal appearance by executor may be required

International

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times of the day during which effective communication between professional advisors can occur. Further, some jurisdictions require personal appearances by the executor or administrator to obtain probate. Unless this can be solved by delegating that requirement by power of attorney to an agent, travel by the personal representative will be required;

- While the personal representative will usually have the choice of professional advisor in international jurisdictions, in some cases the estate may be somewhat captive to the service provider with whom the deceased dealt during his or her lifetime, such as offshore corporate service companies;
- How does a personal representative resident in Canada take effective control of the personal residence of the deceased in another jurisdiction, particularly if that county is one beset by crime, extortion and/or natural disaster? Challenges with insurance, property management and the like will undoubtedly arise;
- Some financial institutions (even large ones) can take a very parochial attitude to the administration of the estates of their deceased customers. That could include imposing requirements for document production that simply cannot be met by persons who are not citizens and/or residents of the country in question.

Professional assistance in international jurisdictions will generally be required, particularly where foreign tax filings or formal probate/administration applications are made. The cost of these estate administration and compliance services, along with the extra time required to administer the estate, must be considered.

International estates can be extremely complex. The challenge is to solve the puzzle by putting the pieces together in the right way. ■

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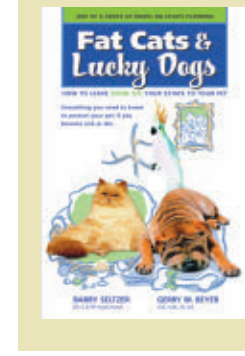
Passing it on to pets: Fat Cats & Lucky Dogs

MICHAEL RAPPAPORT

When Leona Helmsley, the billionaire hotel heiress nicknamed "the Queen of Mean" by the media, died at age 87 in August 2007, she left behind a heap of trouble when she left "Trouble" a $12-million trust fund, and nothing for two of her grandchildren. Trouble was Helmsley's little Maltese dog and her most loyal companion, as she was estranged from her grandchildren and had few friends.

The disinherited grandchildren challenged Trouble's trust fund in court, on the grounds that their grandmother was not of sound mind. The judge reduced the trust fund to $2-million — leaving Trouble considerably poorer, but still a pampered pooch by any measure — with the remainder divided between the grandchildren. (Helmsley left the bulk of her billions to a charitable trust for dogs, a matter that is still before the courts.)



Barry Seltzer and Gerry Beyer write about Trouble's legal travails in their book, *Fat Cats & Lucky Dogs: How To Leave (Some Of) Your Estate To Your Pet*, to highlight the difficulties faced by testators when they try to provide for their pets' feeding and care after they die. Barry Seltzer is a lawyer from Toronto, who practises estates law and is a frequent television and radio guest in Canada, the U.S., the U.K. and Australia. Gerry Beyer is a law professor from Texas Tech University and an expert on estate law.

Under common law, it is difficult to provide for a pet in a will. Pets are regarded as property, and property can't own property. Furthermore, in most jurisdictions, you can't make an animal a beneficiary to a traditional trust, because a beneficiary has to be able to enforce the trustee's duties, something an animal cannot do.

Even where a pet owner used proper legal instruments to provide for a pet — as Leona Helmsley did — the amount of money or property bequeathed may be challenged if it was excessive. Under judicial decisions or statutes, a court may have the power to reduce the value of a gift for the benefit of a pet to an amount it considers more reasonable.

The authors canvass in detail a wide range of options, both formal and informal, that pet owners may consider to ensure that Fido, Polly or Tabby are well provided for in the event that their owners become incapacitated or die.

Informal arrangements may involve finding a caregiver and making a handshake agreement. If pet owners want to give the arrangement some legal teeth, they may formally make a conditional gift to the caregiver in trust. In about 40 states in the U.S., they may set up a statutory pet trust. (The U.S. is the only country in the world which currently recognizes statutory pet trusts.)

The book's cover claims it contains "everything you need to know to protect your pet if you become sick or die." This is no idle boast. The book even devotes a chapter to providing for the future care of exotic and illegal pets. While the average person would not want to keep lions, tigers or bears as pets (Oh my!), there are an astonishing number who do. According to one estimate there are between 6,000 to 7,000 tigers held privately in the U.S., which is greater than the number of tigers left in the wild in Asia, estimated at 5,000.

As law texts go, *Fat Cats & Lucky Dogs* is entertaining reading. It is chock full of witty quotations about pets from famous people, unusual pet trivia and quirky briefs of cases concerning pets. But is there a serious reason for lawyers who do wills and estates to run out and buy this book? Indeed there is.

Chew on the following stats from the 2001 IPSOS-REID pet ownership study (Paws & Claws): More than half of all Canadian households own a cat or a dog, with one-third of households owning cats and one-third owning dogs. One in 10 households (13 per cent) own both cats and dogs. Eight in 10 pet owners (83 per cent) consider their pet to be a family member; only 15 per cent said they love their pet as a pet rather than as a family member.

So if you've drafted a will and you neglected to ask your client about provisions for pets, you may have committed a major oversight. And as anyone who has written wills knows, clients are often uncomfortable about discussing their mortality. Asking about pets is a great way to put your client at ease and build rapport. ■