

The New *Canada Not-For-Profit Corporations Act* – questions for directors to ask

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ARE YOU A DIRECTOR OF A FEDERALLY INCORPORATED CHARITY OR NOT-FOR-PROFIT?

IF SO, DO YOU KNOW THAT THE CORPORATE LEGISLATION WHICH GOVERNS THAT CHARITY OR NOT-FOR-PROFIT HAS CHANGED AND THAT THE CORPORATION WILL BE REQUIRED TO TRANSITION BY OCTOBER 17, 2014?

I. Introduction

The new *Canada Not-for-profit Corporations Act*² (the “**CNCA**”) provides for the phased in repeal of the *Canada Corporations Act*³ (the “**CCA**”) and, specifically, will replace Part II of the CCA, the section which governs federal corporations without share capital (commonly referred to as not-for-profit corporations). The CNCA received Royal Assent on June 23, 2009 and was proclaimed in force effective October 17, 2011.

Every not-for-profit corporation (including charities) currently governed by Part II of the CCA will have three years to formally make the transition to the CNCA. In order to be governed by the CNCA, a corporation will have to apply for a certificate of continuance by **October 17, 2014** or face dissolution. There will be no government fee for the filing of articles of continuance if they are filed within the prescribed three years. If a corporation does not complete the transition by **October 17, 2014**, the corporation may be dissolved. If a corporation is dissolved for failure to file the transition articles, it will be eligible for revival under the CNCA, subject to a prescribed fee.

Action Items:	Review letters patent – additional information is required to be included in articles of continuance
	Review and amend by-laws – requirements under the CNCA are different from the requirements under the CCA and supporting government policy
	Be proactive – take immediate steps to comply with the CNCA and to determine the necessary and desirable changes to your corporation’s governance structure

Some of the issues that directors of federal not-for-profit corporations will need to consider when transitioning to the CNCA are discussed in this Director Alert.

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² S.C. 2009, c. 23.

³ R.S.C. 1970, c. C-32.

II. Members and Membership Rights

The CNCA changes some of the rules regarding members and memberships rights. For example, the new legislation grants voting rights to non-voting members. Specifically, the CNCA provides that where a proposed amendment to articles or by-laws will affect a particular class of members, the amendment must be approved by that class by way of a separate class vote. This voting right is granted to both voting and non-voting members and a corporation may not opt out except in limited circumstances.

In addition, the CNCA changes the requirements regarding the placement of membership provisions in a corporation's governance documents. Some provisions must be contained in the articles and others in the by-laws:

Articles:	Classes of members
	Voting rights of each class if more than one class
	Whether a separate class vote is withdrawn (permitted only in certain circumstances)
By-laws:	Condition required for being a member in each class
	Process by which a member may withdraw or transfer to another class
	Conditions under which a membership can be terminated
Articles or By-laws:	Whether membership is transferable (default rule is that membership is not transferable unless specified to be transferable in the articles or by-laws)

Questions for Directors:

1. Do the corporation's articles and by-laws need to be amended to contain the required information regarding membership classes?
2. Does the corporation currently have one or more classes of non-voting members? If so, will these members remain non-voting members and be permitted to vote in the circumstances specified in the CNCA or should they be reclassified as something other than members prior to continuance under the CNCA?
3. Should the corporation, through its articles, opt out of class voting in the circumstances permitted by the CNCA?
4. Will membership interests be transferable or non-transferable? If transferable, will it be reflected in the by-laws or the articles?

III. Directors

In addition, some of the rules regarding directors have changed. For example, the CNCA provides that the directors may appoint additional directors in between annual meetings of members (if permitted by the articles). The number of directors appointed by the directors may not be more than one-third of the number of directors elected at the previous annual meeting and any directors so appointed may only hold office until the next annual members' meeting.

Number:	Some corporations may have one director (but likely not registered charities) and others are required to have a minimum of three directors, at least two of whom may not be officers or employees of the corporation or any of its affiliates
Ex-officio:	Ex-officio directors (that is, directors by virtue of their office) are not permitted under the CNCA
Appointment:	The directors may appoint additional directors in between annual meetings of members (if permitted by the articles)
Nominations:	Nominations are entitled to be made from the floor at members' meetings or by proposals submitted by members for the election of directors in advance of the meeting

Questions for Directors:

1. Is the corporation subject to a minimum required number of directors?
2. Does the corporation currently have any ex-officio directors? If so, how should they be dealt with?
3. Should the articles include a provision permitting directors to appoint additional directors in between annual meetings?
4. Does the corporation's nomination process permit nominations from the floor at annual members' meetings or by members' in advance of meetings?

IV. Soliciting vs. Non-Soliciting Corporation

Under the CNCA, each not-for-profit corporation is classified as either a soliciting or a non-soliciting corporation. While most charities will be soliciting corporations that may not always be the case. For example, a charity that does not receive any donations in a fiscal year may be a non-soliciting corporation. Similarly, a non-charitable not-for-profit corporation will not necessarily be a non-soliciting corporation. Corporations that receive sufficient government contributions will be a soliciting corporation whether or not charitable. The following chart sets out the guidelines for how to differentiate between soliciting and non-soliciting corporations:

Soliciting Corporation	Non-Soliciting Corporation
<p>More than \$10,000 requested and received by the corporation from one or more public donors, that is, a person <u>who is not</u>, at the time of the request:</p> <ul style="list-style-type: none"> • A member, director, officer or employee of the corporation • The spouse of a member, director, officer or employee of the corporation • A child, parent, brother, sister, grandparent, uncle, aunt, nephew or niece of a member, director, officer or employee of the corporation (or a spouse of such person) 	<p>More than \$10,000, whether or not requested by the corporation, from one or more persons <u>who is</u>, at the time of the request:</p> <ul style="list-style-type: none"> • A member, director, officer or employee of the corporation • The spouse of a member, director, officer or employee of the corporation • A child, parent, brother, sister, grandparent, uncle, aunt, nephew or niece of a member, director, officer or employee of the corporation (or a spouse of such person)
<p>More than \$10,000 by way of grant or similar financial assistance from a government or a government agency</p>	<p>\$10,000 or less from any source whether or not requested by the corporation</p>

More than \$10,000 by way of donation or gift from other entities that have themselves received in excess of \$10,000 in the previous financial year from public donors or from the government – it will be a corporation’s responsibility to inquire from these other entities whether, in the last financial year, they have requested and received funds from public donors or whether they have received money from government and if so, in what amounts

A not-for-profit corporation will need to determine annually whether or not it meets the criteria for a soliciting corporation. The test must be applied on the last day of the corporation’s financial year and if the corporation meets the criteria, it will become a soliciting corporation as of the next annual members’ meeting. A soliciting corporation will retain this status until the third annual meeting of members following the meeting at which it became a soliciting corporation, that is to say, a soliciting corporation will remain a soliciting corporation for roughly three years from the date it obtains such status. If, however, a corporation receives funds meeting the above criteria in a year during this three year period, the three year period will begin anew.

A soliciting corporation will be subject to additional requirements such as the following:

	Soliciting Corporations	Non-Soliciting Corporations
Number of directors:	Minimum of three directors, at least two of whom are “independent”, that is, not officers or employees of the corporation or its affiliates ⁴	Can have one director and have no restrictions on the independence of their directors (unless a registered charity)
Dissolution:	Remaining property must be distributed to one or more “qualified donees” as defined in the <i>Income Tax Act</i> (Canada) ⁵	No restrictions

Questions for Directors:

1. How much money does the corporation anticipate that it will receive from public donors and government?
2. Is the corporation likely to be classified as a soliciting corporation in more years than not?
3. What would be the consequences to the non-soliciting corporation of being reclassified as a soliciting corporation?
4. Knowing the consequences of reclassification, should the corporation continuously adhere to the rules governing soliciting corporations or alter its governance structure and documents as needed depending upon its annual classification?
5. Does the corporation need to change the dissolution clause in its by-laws?

V. Financial Disclosure and Review

Designated and Non-Designated Corporations

In addition to the distinction between soliciting and non-soliciting corporations, the CNCA creates a distinction between “designated” and “non-designated” corporations.

⁴ Note that there may be other legal restrictions on officers or employees of a charity being directors of the charity.
⁵ R.S.C., 1985, c. 1 (5th Supp), subsection 248(1).

A designated corporation is any soliciting corporation having gross annual revenues of less than \$50,000 or any non-soliciting corporation having gross revenues of less than \$1,000,000. A non-designated corporation is a soliciting or non-soliciting corporation that does not fall within those parameters. This classification will affect the corporation's financial reporting requirements as set out in the chart below:

	DESIGNATED CORPORATION		NON-DESIGNATED CORPORATION	
	Soliciting Corporation	Non-Soliciting Corporation	Soliciting Corporation	Non-Soliciting Corporation
Gross annual revenues for last fiscal year	\$50,000 or less	\$1 million or less	More than \$50,000	More than \$1 million
Accountant – required to appoint public accountant* by ordinary (majority) members' resolution at each annual meeting	May dispense with appointment by unanimous members' resolution – valid for 1 year	May dispense with appointment by unanimous members' resolution – valid for 1 year	May NOT dispense with appointment	May NOT dispense with appointment
Financial statements – must be prepared in accordance with GAAP & must send summary of financial statements to members within prescribed timelines	Must submit to Industry Canada not less than 21 days prior to each annual members' meeting	Not required to submit to Industry Canada unless Industry Canada expressly requests them	Must submit to Industry Canada not less than 21 days prior to each annual members' meeting	Not required to submit to Industry Canada unless Industry Canada expressly requests them
Level of financial review	If appoints public accountant, the accountant must conduct a review engagement unless the members pass an ordinary resolution requiring an audit rather than a review - valid only until the next annual members' meeting	If appoints public accountant, the accountant must conduct a review engagement unless the members pass an ordinary resolution requiring an audit rather than a review – valid only until the next annual members' meeting	If gross annual revenues for last financial year are equal to or less than \$250,000 AND members pass a special resolution (two-thirds), public accountant may conduct a review engagement	Must have audited statements
	If has not appointed public accountant, financial statements must be compiled, but not reviewed or audited	If has not appointed public accountant, financial statements must be compiled, but not reviewed or audited		

* Pursuant to the CNCA, a public accountant is defined as:

- a) A member in good standing of an institute or association of accountants incorporated by or under an Act of the legislature of a province;

- b) Who meets any qualifications under an enactment of a province for performing any duty that the person is required to perform under the CNCA; and
- c) Who, subject to court order, is independent of the corporation, its affiliates or the directors or officers of the corporation or its affiliates.

Questions for Directors:

1. Is the corporation a soliciting or a non-soliciting corporation?
2. Is the corporation a designated or non-designated corporation?
3. To which level of financial review is the corporation subject?
4. If the corporation is a designated corporation, should the members be asked to pass a resolution to dispense with the appointment of a public accountant?
5. Based on the corporation's classification, is the corporation required to file its financial statements with Industry Canada?
6. If the corporation is a non-designated, soliciting corporation, should the members be asked to pass a resolution requiring a review engagement rather than an audit?

VI. Minimalist vs. Comprehensive By-Laws

Under the current regime, most not-for-profit corporations have lengthy by-laws essentially compensating for the lack of detail contained in the CCA. The CNCA, however, provides a much more comprehensive set of rules governing not-for-profit corporations. As a result, CNCA corporations will be able to choose between long, detailed by-laws or minimalist by-laws which include only the information that is required and any alternatives to default rules.

Questions for Directors:

1. Should a corporation use comprehensive or minimalist by-laws?
2. If transitioning to minimalist by-laws, what should be included and what can be excluded?

VII. Conclusion

The CNCA brings with it a new era of governance for federal not-for-profit corporations. As such, directors of these corporations will need to consider the differences between the CCA and the new legislative regime and the changes that will need to be made to the governance structures of the corporations on whose boards they sit.

Ontario will go through a similar process in the near future with the enactment of the *Ontario Not-for-Profit Corporations Act, 2010*. The CICA will issue another Director Alert when more details of the Ontario legislation are available.