

COMING SOON:

NEW FEDERAL NOT-FOR-PROFIT CORPORATIONS ACT

On June 23, 2009, the *Canada Not-For-Profit Corporations Act* (the “**NFPCA**”) received royal Assent. The **NFPCA** applies to federal not for profit corporations including those that are registered charities under the *Income Tax Act* (Canada) (the “**ITA**”). The enactment of the **NFPCA** marks a new era of modern governance for the not-for-profit sector since the current legislation has not been substantively amended since 1917. The **NFPCA** replaces the antiquated “letters patent” system of incorporation with an “as of right” system of incorporation.

The intent of the new regime is to modernize the legislation in the not-for-profit sector while maintaining a strong focus on good governance, accountability, disclosure and transparency. The new legislation will also allow such corporations to reorganize themselves in ways currently not available under the federal legislation.

While the **NFPCA** has received Royal Assent, it will only come into force by Order of Council which could occur as early as June 2011. Before this occurs the accompanying regulations (the “**Regulations**”) and user fees (the “**User Fees**”) have to be passed. The latest draft of the Regulations and User Fees were published in the Canada Gazette, Part I, on February 26, 2011.

This notice is intended to provide a high level summary of some of the key provisions of the **NFPCA** and provide guidance on the steps to continuing a not-for-profit organization under the **NFPCA**.

Key Provisions:

Incorporation

One of the most significant changes to the incorporation regime for federal not-for-profit corporations brought about by the **NFPCA** is that applicants will now be entitled to incorporate as of right. This will replace the former regime whereby applicants required ministerial review of their letters patent. Now incorporation will be granted upon the filing of articles of incorporation prepared in accordance with the **NFPCA** and the payment of a prescribed fee. Applicants will no longer be required to have “objects” (unless it is a charity in which case it will likely continue to be desirable to include them) or to list the powers of the corporation.

Soliciting v. Non-Soliciting Corporations

The **NFPCA** makes a clear distinction between soliciting and non-soliciting corporations. According to the **NFPCA**, a corporation becomes a soliciting corporation if, in a single financial year, the corporation received more than \$10,000 in gross annual revenues from public sources. Public sources include non-members, grants or other similar financial assistance received from a government body and donations or gifts received from a corporation that, in turn, would meet the definition of a “soliciting corporation”. A corporation that is found to be soliciting is a soliciting corporation for three years and if during that period there is another financial year over the \$10,000 threshold the three year period will start again. Soliciting corporations have five special requirements that non soliciting corporations do not have:

- (1) Soliciting corporations must have a minimum of three directors, two of whom are not officers or employees of the corporation;
- (2) Soliciting corporations must send a copy of the corporation’s financial statements and public accountant report to Corporations Canada;
- (3) On dissolution, soliciting corporations must ensure that the assets of the corporation go to a “qualified donee” as defined by the ITA;
- (4) Soliciting corporations may not have a unanimous member agreement; and
- (5) Soliciting corporations must follow specific rules for conducting their financial review.

Please note that if the corporation is or plans to be a registered charity, there will be additional rules and restrictions under the ITA.

Capacity

The **NFPCA** confirms that a not-for-profit corporation has the capacity, rights, powers and privileges of a natural person, although members may choose to limit a corporation's powers and activities in its articles. This will be required for charities. For not-for-profit corporations operating abroad, the **NFPCA** provides that the not-for-profit has the capacity to conduct its affairs "to the extent that the laws of that jurisdiction permit".

Registered Office and Records

Pursuant to the **NFPCA**, a corporation is required to maintain a registered office in the province specified in its articles. The directors may change the registered office within that province at any time by sending the Director a notice of registered office. The **NFPCA** also mandates that a corporation prepare and maintain, at its registered office or at any other place in Canada designated by the directors of the corporation, records containing the following:

- (a) the articles and the by-laws, and amendments to them, and a copy of any unanimous member agreement;
- (b) the minutes of meetings of members and any committee of members;
- (c) the resolutions of members and any committee of members;
- (d) if any debt obligation is issued by the corporation, a debt obligations register that complies with the Act;
- (e) a register of directors;
- (f) a register of officers; and
- (g) a register of members.

In addition, a corporation must prepare and maintain adequate accounting records and records containing minutes of meetings of the directors and any committee of directors and resolutions adopted by the directors or any committee of directors. These records must be open to inspection by the directors at all reasonable times. Members, members' personal representatives and creditors of the corporation also have the right to inspect these records, with the exception of the register of members, and may take extracts therefrom upon the payment of a reasonable fee. Members and creditors are only entitled to receive lists of members if they first deliver a statutory declaration stating a member list is required for one of the following purposes:

- (1) to attempt to influence how members vote;
- (2) to requisition a meeting of the members; or
- (3) any other matter relating to corporate affairs.

If the person receiving the list of members uses the list for an unauthorized purpose, he or she will be subject to certain penalties, which could include a fine of up to \$5,000, two years imprisonment, or both.

Corporate Finance

The **NFPCA** provides that any property that is transferred to or otherwise vested in the corporation is owned by the corporation. However, the corporation does not hold any property in trust unless that property was transferred to the corporation expressly in trust for a specific purpose. In addition the **NFPCA** specifically allows directors of a corporation to borrow money, issue debt obligations, provide guarantees and grant mortgages or security interests in the property of the corporation.

While a corporation will not generally be permitted to distribute any profits, proceeds or property, directly or indirectly to a member, director or officer of the corporation, the **NFPCA** does permit payments and reimbursements to members and directors as long as such payments are in furtherance of the corporation's activities or as otherwise permitted by the **NFPCA**. This allows corporations to reimburse directors for expenses and pay them for their services.

In terms of liability, members will not be liable for any liability of the corporation except to the extent that liability is assumed in a unanimous member agreement or to the extent that the member receives property on the liquidation of the not-for-profit corporation.

Directors of a corporation may require annual non-monetary contributions or dues as a condition of membership and the corporation may create a lien on a member's membership interest for a debt of that member to the corporation.

Debt obligations

The **NFPCA** includes extensive rules regarding the debt obligations of the corporation. These rules are similar to the provisions of the *Canada Business Corporations Act*, (the “**CBCA**”) for “for-profit” corporations. The rules codify among other things, the issuance of debt obligation certificates, the maintenance of debt obligation registers, the responsibilities of holders, brokers, purchasers, transferors and transferees of debt obligations, deliveries of debt obligations, the validity of debt obligations and the role of agents respecting debt obligations.

Directors

The **NFPCA** provides important mandatory and default provisions for the election and appointment of directors and officers and the regulation of meetings. It also deals with directors' and officers' duties, the limitation of their liability and directors' and officers' indemnity.

The **NFPCA** mandates that, except for soliciting corporations, a not-for-profit corporation must have a minimum of one director. A soliciting corporation must have a minimum of three directors, at least two of whom are not officers or employees of the corporation or its affiliates. Unless the by-laws of a corporation provide otherwise, a director of a corporation is not required to be a member of the corporation.

At each annual meeting of the corporation, members can, by ordinary resolution, elect directors to hold office for a term expiring within four years. It is not necessary that all directors elected at a meeting of members hold office for the same term. Members may, by ordinary resolution at a special meeting, remove any director or directors from office, with the exception of a director elected by a particular class of members, who can only be removed by an ordinary resolution at a meeting of members of that particular class. Naturally, a director will also cease to act when he or she dies or resigns.

Directors may fill vacancies on the board of directors provided that quorum is in existence and the by-laws do not mandate otherwise. The board may also, if the articles of the corporation so provide, appoint one or more additional directors, so long as the total number of directors so appointed may not exceed one third of the number of directors elected at the previous annual meeting of members.

Unlike the *CBCA* or the *Business Corporations Act (Ontario)*, there is no requirement that a majority of the directors be Canadian residents.

Directors are entitled to attend and be heard at every meeting of members, may appoint from their number a managing director or a committee of directors and may delegate to the managing director or committee any of the powers of the directors with some exceptions. Directors may also, subject to the articles, the by-laws and any unanimous member agreement, fix the reasonable remuneration of the directors, officers and employees of the corporation.

In terms of directors' and officers' duties and liabilities, directors and officers must act honestly and in good faith with a view to the best interests of the corporation; they must comply with the **NFPCA** and the regulations, articles, by-laws and any unanimous member agreement of the corporation; they must exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances; and they must disclose potential areas of conflict of interest. In addition to these duties, directors also have a general duty to manage and supervise the activities of the corporation and verify the lawfulness of the articles and the purpose of the corporation.

Where a director faces an action against him or her, he or she may raise a reasonable due diligence or good faith reliance defense. Directors may also be indemnified by the corporation for their actions while in office so long as they acted honestly and in good faith with a view to the best interests of the corporation.

Directors Meetings

The **NFPCA** provides a number of provisions regulating board meetings including notice, location, and quorum requirements.

Unanimous Member Agreements

Similar to unanimous shareholder agreements, members of a non-soliciting corporation are entitled to restrict the powers of the directors to manage and supervise the activities and affairs of the corporation and to take on these responsibilities themselves.

Conflicts of Interest

Similar to other corporate statutes, the **NFPCA** mandates that a director or an officer of a corporation disclose to the corporation the nature and extent of any interest that the director or officer has in a material contract or material transaction. A director that is required to make such a disclosure is not permitted to vote on any resolution to approve the contract or transaction unless the contract or transaction (a) relates primarily to the director's remuneration as a director, an officer, an employee, an agent or a mandatary of the corporation or an affiliate, (b) is for indemnity or insurance under s. 151 of the **NFPCA**; or (c) is with an affiliate of the corporation.

Officers

Subject to the articles, the by-laws and any unanimous member agreement, the directors of a corporation may designate the offices of the corporation, appoint officers, specify their duties and delegate powers to manage the activities and affairs of the corporation to the officers. The officers of a corporation may also receive reasonable remuneration and expenses for services to the corporation.

By-Laws

One of the most welcome changes brought on by the **NFPCA** is the fact that the by-laws of the corporation no longer have to be reviewed by the Director when created or amended. The **NFPCA** allows directors to unilaterally make, amend and repeal corporate by-laws relating to the activities and affairs of the corporation, so long as the articles, by-laws or unanimous member agreement does not provide otherwise. Standard amendments to by-laws by the directors of the corporation will have to require confirmation, rejection or amendment by the members at the next meeting of members. Fundamental amendments to the articles and by-laws of the corporation, however, require a special resolution of the members to be approved.

Members' Rights and Inputs

Unless otherwise provided in the articles, each member of a corporation is entitled to one vote at a meeting of members. Other members' rights include access to corporate records, the provision of standard corporate information (e.g. financial statements, public accountant's report), and access to membership lists (with special protections to prevent abuse of the information). The members of a corporation who hold the prescribed percentage of votes that may be cast at a meeting of members sought to be held, or a lower percentage that is set out in the by-laws, may also requisition the directors to call the meeting for the purposes stated in the requisition.

Meetings of Members

Meetings of members of a corporation must be held within Canada at the place provided in the by-laws or, in the absence of such a provision, at a place determined by the directors. Notwithstanding the foregoing, a meeting of members may be held outside of Canada if the place is specified in the articles or all the members entitled to vote at a meeting agree that the meeting is to be held at that place. In addition, unless the by-laws otherwise provide, any person entitled to attend a meeting of members may participate in the meeting electronically. The **NFPCA** also permits absentee voting/proxies and other forms of voting as may be approved by the Director.

The first annual meeting of members must be held within 18 months of the corporation coming into existence and subsequently within 15 months after the preceding annual meeting but no later than six months after the end of the corporation's preceding financial year. In addition, directors have the right to call a special meeting of members at any time.

The corporation must give members entitled to vote at a meeting of members notice of the time and place of the meeting in accordance with the by-laws and the regulations. A member entitled to vote at an annual meeting of members may submit to the corporation notice of any matter that the member proposes to raise at the meeting (a "proposal") and discuss at the meeting any matter with respect to which the member would have been entitled to submit a proposal.

All business transacted at a special meeting of members and all business transacted at an annual meeting of members, except consideration of the financial statements, public accountant's report, election of directors and re-appointment of the incumbent public accountant, is considered special business. Where special business is to be transacted at a meeting of members, the notice of the meeting must state the nature of that business in sufficient detail to permit a member to form a reasoned judgment on the business; and state the text of any special resolution to be submitted at the meeting.

Quorum at a meeting of members can be set in the by-laws of a corporation, failing which the **NFPCA** states that quorum is the majority of the members. Similar to other corporate statutes, all of the members may sign a resolution approving any business in lieu of having a meeting of members.

Financial Disclosure and Public Accountant

The financial disclosure requirements provided for in the **NFPCA** is a far departure from the old federal regime. The form of financial statements required to be delivered or made available to member varies depending on the level of the corporation's annual revenues and whether the corporation is a soliciting corporation or a non-soliciting corporation. Generally, the directors of a corporation must place before the members at every annual meeting:

- (a) prescribed comparative financial statements that conform to any prescribed requirements and relate separately to
 - i. the period that began on the date the corporation came into existence and ended not more than six months before the annual meeting or, if the corporation has completed a financial year, the period that began immediately after the end of the last completed financial year and ended not more than six months before the annual meeting, and
 - ii. the immediately preceding financial year;
- (b) the report of the public accountant, if any; and
- (c) any further information respecting the financial position of the corporation and the results of its operations required by the articles, the by-laws or any unanimous member agreement.

If the by-laws permit, the corporation may, as an alternative to sending copies of the financial statements to members, send notice to the members stating that the financial statements are available at the corporation's registered office or a copy can be sent to the members by prepaid mail upon request. Soliciting corporations are further required to submit their financial statements to the Director.

Fundamental Changes

In addition to incorporation as of right, the **NFPCA** also permits corporations to undergo fundamental changes and sets out how those changes are to be authorized by the directors and members. These include procedures for amalgamation, continuance, liquidation, and dissolution of a corporation.

Transition

The **NFPCA** contains provisions that guide how corporations incorporated under Part II of the *Canada Corporations Act* ("CCA") are continued under the **NFPCA**. There are no fees imposed by Corporations Canada for this continuance application, however, the application for continuance must be made within three years of the **NFPCA** coming into force (which could occur as early as June 2011). If a not-for-profit corporation fails to do so, it will be dissolved within six

months of the transition date. Until the Certificate of Continuance is issued to the corporation by Corporations Canada, Part II of the CCA will continue to apply to those corporations.

The transition process comprises five steps:

- (1) review of objects and by-laws;
- (2) preparation of Articles of Continuance, in the form provided by Corporations Canada;
- (3) create or amend by-laws;
- (4) obtain members' approval; and
- (5) file the required documents with Corporations Canada.

The Articles of Continuance require the following information: corporate name; province or territory where the registered office is situated; minimum and maximum number of directors or the fixed number of directors; statement of purpose of the corporation; restrictions on the activities that the corporation may carry on (if any); the classes, or regional or other groups of members that the corporation is authorized to establish; statement regarding the distribution of property remaining on liquidation; and any additional provisions that the corporation may want in its articles.

If a corporation wishes to change its name as part of the transition, a federal NUANS report will be required. Additional provisions that may be included in the articles include: non-profit clause for registered charities; remuneration of directors clause for registered charities; increase in the majority vote for members' ordinary or special resolutions; a corporate name to be used outside Canada; allow directors to fill vacancies on the board; allow directors to appoint one or more additional directors; and restriction on circumstances where members vote separately as a class or group.

With regards to the by-laws there are only two mandatory by-law provisions: conditions for membership; and notice of members' meetings.

Once the articles have been approved by the members, to obtain the Certificate of Continuance, a corporation must file the following, currently proposed, documents with Corporations Canada:

- Form 4031- Articles of Continuance (transition);
- Form 4002 – Initial Registered Office Address and First Board of Directors; and
- Federal NUANS report, only if the corporation's name is changing on transition.

Although by-laws do not have to be filed with Corporations Canada as a precondition to obtaining the Certificate of Continuance, they are required to be filed within twelve (12) months of member approval.

Charities

As noted above, where a corporation is a charity or wishes to become one, there will be more restrictive rules. Charities should consider sending their draft Articles of Continuance (transition) to the Charities Directorate of the Canada Revenue Agency (“**CRA**”) for review before filing them with Corporations Canada. CRA recommends that the “Additional Provisions” box in the articles include a statement that the corporation will be operated on a non-profit basis (i.e. a non-profit clause) and that directors may not be remunerated merely for acting as directors. CRA will provide examples of acceptable statements although such statements will not be mandatory. If CRA has not approved the purposes prior to Corporations Canada issuing the Certificate of Continuance, there is a risk that CRA will require the corporation to amend its articles under the **NFPCA**, which carries a \$200 fee.

*For more information on the new **NFPCA**, or for assistance in continuing your corporation under the **NFPCA**, please contact one of Wilson Vukelich LLP's Not-For-Profit group members: **Gwen Benjamin** (Tax) at 905-940-2647 or gbenjamin@wvllp.ca, and **Heather Whitten** (Corporate) at 905-940-8733 or hwhitten@wvllp.ca.*