

The New Canada Not-for-profit Corporations Act

An Overview

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The current legislative regime governing the federal not-for-profit sector has not undergone any significant modification since 1917. On November 15, 2004, following much public consultation, the federal government introduced An Act Respecting Not-for-profit Corporations and Other Corporations Without Share Capital (Bill C-21) (the "*Canada Not-for-profit Corporations Act*") (hereinafter "the Act") which provides a modern system of corporate governance for federal not-for-profit corporations and special act corporations without share capital currently regulated by the *Canada Corporations Act*. The federal government has predicted that it will take more than a year for the new legislation to be passed, and amendments and changes to its current provisions remain likely as it proceeds through the legislative process. The following summary highlights some of the most important aspects of this highly detailed and comprehensive piece of legislation.

1. Transitional Procedures for New Corporations

Once the legislation is enacted, all corporations that are currently governed by Part II of the *Canada Corporations Act* will be required to apply for a certificate of continuance in order to achieve corporate status under the new regime. No fees will be required for this application, but if an existing corporation fails to take this step within three years after the coming into force of the Act, it may be subject to dissolution. Existing corporations therefore have a significant incentive to comply with the new legislation, as well as a lengthy period in which to do so.

2. Incorporation

The new legislation will replace the current system of federal incorporation (i.e., the discretionary "letters patent" system) with the faster and more efficient system of incorporation "as of right." In addition, the new legislation will no longer require that three individuals incorporate new corporations. Instead, one or more individuals or corporations will be able to incorporate by sending signed articles of incorporation and other specified documents to the Director, who upon receipt will issue a certificate of incorporation. The Director is a position created by the new legislation that is somewhat similar to that of the Director under the *Canada Business Corporations Act*, in that the Director's role is to exercise regulatory powers and act as a public registrar of corporations.

3. Capacity and Powers of the Corporation

The new legislation provides not-for-profit corporations with the capacity, rights, powers and privileges of natural persons, and it does not require the passage of by-laws in order to confer any power on a corporation or its directors. Corporations will still be required, however, to refrain from carrying on activities or exercising powers in a manner contrary to their mission as articulated in their articles. As a result of these new provisions, directors should be less exposed for actions that are ultra vires the corporation's powers.

4. Financial Accountability and Disclosure

The new legislation introduces a distinction between two different types of corporations: "soliciting corporations"

and “non-soliciting corporations.” When a corporation requests donations or gifts of money from the public, receives a grant or similar financial assistance from a government or government agency, or accepts money or other property, then such corporation is considered to be “soliciting”, according to the new legislation.

With a view to enhancing and protecting the rights of members, the new legislation will impose additional financial disclosure obligations on corporations by requiring that they make financial statements available to members on request. Soliciting corporations will also be required to file their financial statements with the Director, who will then make them available to the public.

Different levels of financial accountability will be imposed on different types of corporations depending on their level of annual revenue and whether they are a soliciting corporation. Soliciting corporations with annual revenues greater than \$250,000 require an audit, whereas non-soliciting corporations are required to have an audit only where their annual revenues are greater than \$1 million. Members of both soliciting and non-soliciting corporations with annual revenues below these prescribed annual revenue levels will have some limited choice in the level of financial scrutiny they wish to impose on the corporation – an audit engagement, a review engagement with a lesser scope of examination or no review or engagement whatsoever.

5. Administrative Obligations

The new legislation requires all corporations to file annual returns and keep registered offices. Corporations will also be required to maintain corporate records for specific periods of time. Required records will include registers of directors, officers, members and debt obligations, minutes of members' meetings, adequate accounting records and important corporate documents such as articles and by-laws. The new legislation requires corporations to grant access to these corporate records for certain groups, depending on the type of record involved.

6. Directors

Under the new legislation, directors of non-profit corporations will be subject to modern governance rules, bringing their duties and responsibilities more in line with those of their for-profit counterparts.

a) Composition of Board and Meeting of Directors

A corporation, pursuant to the new legislation, has more flexibility in determining the number of directors required to manage its affairs. Non-soliciting corporations must have at least one director, whereas soliciting

corporations must have a minimum of three directors, at least two of whom are not officers or employees of the corporation or its affiliates. In addition, the Act makes provision for directors' written resolution in lieu of holding a meeting, a flexible and rotating board and a maximum term of three years.

b) Duties

Under the current legislative regime, the standard of care to which non-profit directors and officers are subject is determined by a fluctuating common law. The new legislation specifically provides directors with a duty of care that requires them to act honestly and in good faith with a view to the best interests of the corporation, to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances and to comply with the new legislation and any governing corporate documents. The legislation also gives directors other express duties, including the duty to manage or supervise the activities and affairs of the corporation, and a duty to disclose all conflicts of interest.

c) Defences

The current non-profit regime provides no explicit defence for directors facing liability claims. The new legislation rectifies this by providing a due diligence defence for directors who can demonstrate that they exercised the care, diligence and skill that reasonably prudent persons would have demonstrated in comparable circumstances, including the reliance in good faith on corporate financial statements or reports made by professionals. The introduction of this defence clarifies and limits the potential liabilities of directors, and may encourage recruitment of directors in this sector. Recruitment may also be encouraged by provisions in the new legislation that allow corporations to indemnify present and former directors and officers in certain circumstances and to purchase and maintain insurance for the benefit of such individuals.

d) Potential Liabilities

The new legislation outlines specific potential liabilities of directors, including the provision that directors can be liable to employees of the corporation for all debts (not exceeding six months' wages) for services performed during their directorship. In addition, directors who authorize, permit or acquiesce to an offence committed by the corporation under the new legislation will be party to and guilty of the offence as well, unless they establish that they exercised due diligence in preventing its commission.

7. Members' Rights

The new legislation expands the rights of members, as well as the corresponding duties that a corporation owes to these members. Further, the new legislation provides more details and includes matters previously dealt with only by policy guidelines or by by-law.

a) Member Meetings

Directors are required to call annual meetings of members within specific time periods under the new legislation, which also regulates the manner in which corporations must notify members of such meetings. New provisions also give members the right to requisition the directors to call meetings, a right not provided under the current legislative regime. The requirements of what constitutes a proper meeting are now clearly outlined in the new legislation by the inclusion of such matters as the conduct of electronic meetings, voting in absentia (which now includes voting by telephone or other electronic means) and the replacement of meetings by written resolution of the members in lieu of a meeting.

b) Voting and Member Proposals

Under the new legislation, at least one class or group of members must have the right to vote at any meeting of members. Voting members will be able to submit to the corporation notice of a proposal that they wish to raise at a members' meeting, and subject to some broad exceptions, the corporation will be required to include the proposal in the notice of the meeting.

c) Unanimous Member Agreements

The mechanism of a "unanimous member agreement" will become available to members under the new legislation. Through this instrument, all members of a non-soliciting corporation can restrict the powers of the directors to manage or supervise the activities and affairs of the corporation.

d) Member Remedies

Derivative actions, rights and the oppression remedy are made available to members, as well as other complainants, under the new legislation. The derivative action can be used by members to launch actions in the name of the corporation, and the oppression remedy allows members to bring claims seeking relief from the oppression of their rights. The new legislation gives courts wide latitude to order remedies and impose obligations on corporations when satisfied of the merits of a derivative or oppression action, although a faith-based defence for religious non-profit organizations is available.

8. Fundamental Changes to the Corporation

The new legislation outlines specific circumstances in which special resolutions (two-thirds vote) of members are required in order to make fundamental changes to the corporation. Such fundamental changes include altering the conditions and rights of membership, the number of required directors and/or the distribution of assets upon dissolution. Detailed provisions also govern occasions where two or more corporations wish to amalgamate and continue as one corporation, situations in which corporations are liquidated and dissolved, and circumstances where corporations wish to continue under the laws of another legal jurisdiction.

9. Special Issues

a) Debt Obligations

There are numerous and detailed provisions regarding debt obligations in the new legislation that are similar to those that apply to share capital corporations. There are provisions regarding the proper form, delivery, registration and enforcement of debt obligations, the duties and rights of purchasers, guarantors and issuers and the use of trust indentures for debt obligations. These provisions may have special significance for those corporations that borrow money from their members, and therefore should be examined closely by organizations engaging in such activities.

b) Receivers and Receiver-Managers

The new legislation specifically provides for the appointment of receivers and receiver-managers of non-profit corporations, thereby clarifying the uncertainty that exists under the current legislative regime as to whether this is possible.

10. Conclusion

This proposed legislation will have tremendous impact on the conduct and affairs of the not-for-profit sector in Canada, specifically the over 18,000 corporations that currently fall under the federal non-profit regime. Although it will be some time before this legislation becomes law, federal non-profit corporations would be well advised to monitor the status of the legislation and govern their planning and affairs accordingly. **L&G**

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