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5 Steps to Transition: the *Canada Not-for-Profit Corporations Act*

By Margot Patterson and Tom Houston

Introduction

The new *Canada Not-for-Profit Corporations Act* ("NFP Act") came into force on October 17, bringing with it a new framework for the governance and incorporation of associations, charities and other federal not-for-profit organizations. The NFP Act replaces Part II of the *Canada Corporations Act* ("CCA"), which has set the rules for not-for-profit organizations since 1917.

The new legislation is long and detailed, for a reason. It is intended to provide a comprehensive "rule book" that, among other things, replaces a great deal of the detail that was previously required in by-laws, and allows latitude for a corporation to either accept the default requirements in the legislation, or set rules to fit its own circumstances and practices. Overall, the NFP Act creates a more streamlined framework for Canadian not-for-profit corporations, which should be well worth the initial transition process.

As under the previous legislative regime, the rules respecting corporate governance and the rules respecting registered charities are kept separate. The NFP Act does not grant registered charity status under the *Income Tax Act*, nor does it directly address any other tax-related issues.

The Transition Period

Not-for-profit corporations currently incorporated under Part II of the CCA will have three years to transition to the NFP Act to avoid dissolution. Please see the "5 Steps to Transition" below.

By-laws

Industry Canada will no longer review and approve by-laws. Corporations are required, however, to file by-laws and amendments with Industry Canada within twelve months of member approval. The NFP Act gives corporations significant latitude to adopt by-laws that suit their specific needs.

Because the NFP Act sets broadly applicable default rules, a corporation's by-laws can be minimal, containing as little as the conditions for membership and notice of members' meetings.

It will therefore be up to each corporation to decide whether it will simply review and amend its by-laws to ensure compliance, or create new minimal by-laws and rely primarily on the NFP Act as its legal "rule book". The advantages and disadvantages for each corporation depend on its individual circumstances.

Directors' Fiduciary Duties

Directors are subject to the same duty and standard of care as directors of business corporations: an explicit duty to act honestly and in good faith, in the best interests of the corporation, and to exercise the care, diligence and skill of a reasonably prudent person in similar circumstances.

Members

Members have enhanced rights under the NFP Act, including:

- the right of voting members to submit **notice of a proposal** to the corporation of a matter to be raised at a members' meeting;
- the right to **requisition a meeting** for a specific purpose;
- the right of **non-voting members to vote separately from voting members** on matters that impact their membership rights, including certain fundamental changes; and

- the right to **access corporate records** to monitor the board's performance.

Remedies are available to members to enforce these rights. These include court-ordered investigations (to review alleged wrongdoing), compliance orders (e.g. to share information with members), and "business-style" derivative action and oppression remedies.

Meetings

Previously, under the CCA, directors' and members' meetings could not be conducted by way of a unanimous written resolution; however such meetings are permitted in certain circumstances under the NFP Act.

Corporate Obligations

1. Annual meeting

The NFP Act requires annual members' meetings to elect directors, appoint a corporate accountant and review financial statements. The NFP Act sets out options for providing notice of members' meetings and for absentee voting.

2. Reporting to Industry Canada

The new reporting obligations are designed to be simpler than the previous CCA requirements. The most significant of these is the requirement simply to file copies of by-laws, without the need for review and approval by the Minister of Industry. The following are the key ongoing filing requirements for a corporation operating under the NFP Act:

- annual return;
- changes in directors;
- copies of by-laws/amendments;
- articles and amendments made thereto;
- change of registered office address; and
- financial statements and accountant's report (soliciting corporations).

Financial Accounting and Disclosure

1. Soliciting or Non-Soliciting Corporation?

A “soliciting corporation” is one that receives more than \$10,000 in a financial year, in the form of donations from third parties, government grants or financial assistance, or donations from another soliciting corporation. Once acquired, “soliciting corporation” status lasts for three years. A corporation on the threshold of this status should therefore monitor its revenues annually to determine whether it has become a soliciting corporation, and to determine how long the status will apply to it. A non-soliciting corporation is – quite simply – not a soliciting corporation.

2. Review and reporting requirements

Soliciting corporations are subject to different rules for certain key matters. For example, while a non-soliciting corporation is permitted to have only one director, a soliciting corporation must have a minimum of three, two of whom must not be officers or employees of the corporation. Soliciting corporations are also subject to more stringent financial review and reporting requirements.

The level of corporate gross revenues is also relevant to these review and reporting requirements, as the following chart demonstrates. Note, for example, that the first category of corporations set out below (soliciting corporations with less than \$50,000 in gross annual revenues, non-soliciting corporations with less than \$1 million) is exempt from audits,

Type of Corporation / Gross Annual Revenues	Defaults and Options for Financial Review
Soliciting corporation < \$50,000 Non-soliciting corporation < \$1M	Members may unanimously vote not to appoint a public accountant; can have its financial statements reviewed or audited.
Soliciting corporation between \$50,000 and \$250,000	Must have a financial review by a public accountant; can have its financial statements reviewed or audited.
Soliciting corporation > \$250,000 Non-soliciting corporation > \$1M	Must have a financial review by a public accountant; must have its financial statements audited.

provided that the members have unanimously voted not to appoint an auditor, unless the articles or by-laws require otherwise.

3. Exemptive Relief

The NFP Act permits a corporation to apply for exemption from the financial reporting obligations where a case can be made that the potential detriment to the corporation outweighs the benefit to the members or, in the case of a soliciting corporation, to the public.

Fundamental Changes

The NFP Act sets out specific rules for the directors and members of the corporation to approve “fundamental changes”, which include such matters as:

- changing the name of the corporation;
- amending articles and by-laws;
- altering the corporation’s activities, or changing its mission statement or “statement of purpose”;
- changing conditions of membership, or the rights of any class or group of members; and
- changing the means of giving notice of a members’ meeting to voting members.

A director, or a member who is entitled to vote at an annual members’ meeting, may make a proposal for a fundamental change.

5 Steps to Transition under the NFP Act

The approach and the time each corporation takes to fulfill the following transitional steps will

depend on factors such as the type, size and complexity of the corporation, how familiar the Board and members are with its current procedures, and whether the corporation is combining its NFP Act transition with an overall governance review. While all corporations will have three years to transition, each one

should ensure that its transition plan can accommodate the consultation it will need with members, and legal and financial advisers as may be required.

1. **Review the current Letters Patent and By-laws**, consider the corporation's current structure and procedures, and determine whether the corporation will either retain or remove the provisions that are no longer required.
2. **Prepare Articles of Continuance (transition)** using Form 4031 made available online by Industry Canada.
 - If the corporation is also a registered charity, the draft Articles of Continuance should be sent to the Canada Revenue Agency for pre-approval before filing them with Industry Canada – note that CRA pre-approval can take 6-8 months.
3. **Revise the by-laws** following a review of the new requirements, default provisions, and choices open to the corporation under the NFP Act.
4. **Obtain member approval** at a members' meeting duly called under the existing rules, with approval by two-thirds of the members.
5. **File with Industry Canada** the Articles of Continuance (transition), Initial Registered Office Address, First Board of Directors and amended by-laws.

Your Choice: Corporate Housekeeping or a "Clean Sweep"

The NFP Act will affect some 19,000 not-for-profit associations, charities, and professional, cultural, and religious and other groups currently incorporated under a ninety year old Act. The old regime has become familiar territory.

The introduction of the new regime, however, provides an opportunity for thousands of not-for-profit corporations to revisit their governance structure and make important choices. The new

legislation is flexible enough to permit corporations to consider the transition as a form of good "corporate housekeeping", to tidy the rules up a bit, but to continue on with many of the rules they are currently accustomed to. On the other hand, some corporations may choose to do a "clean sweep", using the transition as an opportunity to change their names, mandates, and structures.

The entry into force of the NFP Act on October 17, 2011 starts the three-year transition clock. Get ready to review the legislation and ask questions – to get information, opinions, and advice – on how each not-for-profit corporation will respond to the new rules.

Contact Us

For further information, please contact [Margot Patterson](#) or [Tom Houston](#).