The Ontario Not-For-Profit Corporations Act, 2010 and You

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HEALTHCARE PHILANTHROPY:
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OVERVIEW

• Current status of the Ontario Not-for-Profit Corporations Act, 2010 (“ONCA”)
• Overview of key features of the ONCA
• Continuance process and practical steps

RESOURCES

• Charity Law Bulletin “The Nuts and Bolts of the Ontario Not-For-Profit Corporations Act, 2010” on our website at www.charitylaw.ca
• To view ONCA in its entirety, see: http://www.ontla.on.ca/web/bills/bills%20_detail.do?locale=en&In tranet=&BillID=2347

A. CURRENT STATUS OF ONCA

• The Ontario Corporations Act (“OCA”) has not been substantively amended since 1953
• Bill 65 introduced the ONCA on May 12, 2010 to govern corporations under Part III of the OCA
• ONCA received Royal Assent on October 25, 2010
• ONCA is expected to be proclaimed in force in late 2012
• Draft regulations, default by-laws and plain language guides are expected to be released for public comment in early 2012
• Updated Not-For-Profit Incorporator’s Handbook is expected to be released
Advisory Committee comprised of industry and government representatives is involved in the ongoing process of implementing the ONCA and relevant documents. Ministry of Government Services – will be responsible for searches and filing. Ministry of Consumer Services – will be responsible for remaining areas, including policy and interpretation issues. Possible developments to watch for: New government might amend the ONCA. The degree to which the regulations might allow for the exercise of discretion (e.g., change amounts for financial audit).

B. OVERVIEW OF KEY ELEMENTS OF THE ONCA

1. Incorporation and Corporate Powers
   - Replaces the letters patent system with a statutory regime similar to Ontario Business Corporations Act
   - Removes ministerial discretion to incorporate, in that incorporation will be as of right
   - Obtain certificate of incorporation, not letters patent
   - Only one incorporator is needed
   - No requirement to file by-laws or financial statements with the government, but default by-law will apply if no by-law adopted within 60 days after incorporation
   - Import to and export from Ontario

   Corporation has the capacity, rights, powers and privileges of a natural person. Eliminates the concept of a corporation’s activities being ultra vires.
   - If a corporation acts outside of its purposes, then it has breached the ONCA but the act is valid
   - Makes little difference in practice, because directors have a duty to comply with the articles of the corporation, which may limit the purpose of the corporation and charities have to comply with the requirements in other statutes (e.g., Income Tax Act).
2. Public Benefit Corporations (PBCs)
   • All corporations categorized into PBCs and non PBCs
   • PBCs include
     – “charitable corporations” - uses common law definition
     – Non-charitable corporations that receive more than $10,000 in a financial year in funding from public donations or the federal or a provincial or municipal government or an agency of such government
   • When a non-charitable corporation reaches the $10,000 threshold in a financial year, it will be deemed to be a PBC in the next financial year, as of the date of the first annual meeting of members in that financial year

• Consequences of being a PBC
  – Not more than one third of the directors of a PBC may be employees of the corporation or its affiliates
  – Higher thresholds for dispensing with the default requirement to appoint an auditor or a person to conduct a review engagement requirements
  – Upon liquidation and dissolution, its net assets must be distributed in the following manner
    • If it is a charitable corporation, then to a charitable corporation with similar purposes or to a government or government agency
    • If it is a non-charitable corporation, then to a PBC with similar purposes or to a government or government agency

• Upon the liquidation and dissolution of a non-PBC, its net assets must be distributed in accordance with the articles, or if the articles do not address that issue, then rateably to the members
• A PBC may not distribute the fair value of a membership to a member upon termination of that member’s membership
• It is possible that some non-charitable corporations could oscillate between PBC and non-PBC because PBC/non-PBC status depends on the source and amount of funding in the previous year and the PBC status attaches for only part of a year
• Non-charitable corporations will need to monitor their funding sources
If a non-charitable corporation is concerned about oscillation, it can voluntarily be structured as a PBC:
- Ensure 2/3 of directors are not employees (but charities cannot have any directors who are employees)
- Ensure the articles provide that property will be paid to another PBC with similar purposes or to a government or government agency upon liquidation

For those years when it exceeds the $10,000 threshold:
- Follow audit and audit and review rules for PBC corporations – may not be an issue if the corporation's practice is to have its financial statement audited

### 3. Financial Review

Members are required to appoint by ordinary resolution an auditor or person to conduct a review engagement at each annual meeting

<table>
<thead>
<tr>
<th>Type of Corp/Gross Annual Revenues (GAR)</th>
<th>Requirements for an Auditor</th>
<th>Audit/Review Engagement</th>
</tr>
</thead>
<tbody>
<tr>
<td>PBC Corporation (PBC) with GAR of up to $100,000 (ss.76(1)(a))</td>
<td>May, by extraordinary resolution (80%), dispense with an auditor</td>
<td>May, by extraordinary resolution (80%), dispense with an auditor engagement by extraordinary resolution (80%)</td>
</tr>
<tr>
<td>More than $100,000 but less than $500,000 (ss.76(1)(b))</td>
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<tr>
<td>$500,000 or more (ss.76(1)(c))</td>
<td>An auditor must be appointed annually</td>
<td>Audit is required</td>
</tr>
</tbody>
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Non-PBC corporation with GAR of:

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<td>Non-PBC corporation with GAR of up to $500,000 (ss.76(2)(b))</td>
<td>May, by extraordinary resolution (80%), dispense with an auditor</td>
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4. Number of Directors and Election

- Minimum 3 directors
- Articles may provide a maximum and minimum range
- For PBCs - not more than 1/3 of the directors may be employees of the corporation or its affiliates (charities can have none)
- Directors are elected at meetings of members
- Board may appoint additional directors up to 1/3 of the number of directors elected at the previous annual meeting of members
- Ex-officio directors continue to be permissible
- Directors are no longer required to be members
- Maximum 4 year term for directors (but no limit on number of maximum terms)
- May have staggered terms

5. Directors and Officers - Powers, Duties and Defence

- Directors may borrow money on the credit of the corporation without members' authorization, unless articles or by-laws provide otherwise
- Directors may view certain corporate records that the corporation is required to prepare and maintain (e.g. meeting minutes, accounting records, members' resolutions, etc.) and receive free extracts of them
- Objective standard of care for directors and officers to
  - Act honestly and in good faith with a view to the best interests of the corporation
  - Exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances
- Directors and officers must comply with the ONCA, the articles and by-laws
- Reasonable diligence defence for directors (not officers)
  - Not liable if fulfilled their duty if they exercise the care, diligence and skill that a reasonably prudent person would have exercised in comparable circumstances
  - Defence includes good faith reliance on financial statements and reports of professionals
- Weak liability protection - the government rejected the recommendation to include a partial liability shield for directors
6. Members
   • A corporation must have members
   • Articles must set out the classes of members
   • If only one class of members, all must be voting
   • If two or more classes, articles must provide voting rights to at least 1 class
   • By-laws must set out the conditions for membership
   • Where more than one class, the members of each class have certain built-in protections
   • Default 1 vote per member, unless articles provide otherwise

7. All classes of members, even non-voting classes of members, are entitled to vote separately as a class on certain amendments to articles and by-laws dealing with rights and classes of membership
   • Non-voting members are given voting rights in some limited circumstances
     – Extraordinary sale
     – Amalgamation
     – Continuance to another jurisdiction
     – Change to any rights or conditions attached to non-voting members or change the rights of other classes of members relative to the rights of the non-voting members
   • Thus a class of members could reject a change – effectively resulting in a class veto

8. The treatment of members mirrors that in the Ontario Business Corporations Act in relation to shareholder’s rights
   • In most cases, giving non-voting members the right to vote on fundamental changes may not be justified
   • Some corporations may want to collapse all membership classes into one class and remove non-voting membership classes
     – Change them into a non-membership category, such as “affiliates”, “associates”, “supporters”
     – May set out their rights and duties as non-members
     – Consider timing for such change
     – But their donations will not be exempt from the $10,000 threshold
     – For corporations that are non-profit organizations, query whether this may affect the NPO status
7. Members’ Meetings
• Must be held in Ontario at the place provided in the by-laws or, in the absence of such a provision, at the place within Ontario that the directors determine.
• May be held outside Ontario if the place is specified in the articles or all the members entitled to vote at the meeting agree that the meeting is to be held at that place.
• No longer requires notice be sent by mail provided that notice is given 10 to 50 days before the meeting.
• Directors may fix a “record date” of no more than 50 days before a members’ meeting to determine who the members are for purpose of calling a members’ meeting.
8. Members’ Rights

- Members may elect and remove directors at anytime
- A member entitled to vote at an annual meeting of members may raise any matter as a “proposal” but must give at least 60 days notice
  - A proposal may nominate directors for election if it is signed by at least 5% of voting members or such lower percentage set out in the by-laws (but nominations may still be made at the meeting)
  - Proposal must relate in a significant way to the activities and affairs of the corporation
  - Directors can refuse to discuss the proposal if they give at least 10 days notice, but a member may appeal their decision to court

- Members may requisition meetings of the members (but need 10% of the votes to do so, or lower if the by-laws so states)
- Members may examine certain corporate records – articles, by-laws, the minutes of meetings and resolutions of members and committee of members, registers of directors, officer and members
- Right to access membership lists - to include name and address – only for the purpose of influencing voting, requisitioning a members’ meeting or other matters relating to the affairs of the corporation
- Right to financial statements
9. Members’ Remedies

- Compliance or restraining order – if a corporation, or its directors and officers, fails to comply with the duties set out in the ONCA and regulations, the articles or by-laws

- Rectification order – if the name of a person has been wrongfully entered, retained, deleted or omitted from the registers or records of a corporation, that person may apply to a court for an order rectifying the registers or records

- Dissent and appraisal remedy for non-PBCs - in relation to fundamental changes

- Unlike CNCA, there is no “religious corporation” exemption to the compliance or restraining orders dissent and appraisal remedy

- Derivative action – Allows members to bring an action in the name of the corporation to enforce one of its rights

- Exemption for “religious corporation” - e.g. Cannot bring derivative action to recover misappropriated church property

- Lack of definition for “religious corporation” means that the courts will have to define that term

- Unlike the CNCA, there is no oppression remedy

- Investigation order – A member (or holder of debt) may apply to the court for an investigation of the corporation

- One of the grounds listed for an investigation order tracks the language of the oppression remedy - “the activities or affairs of the corporation or of any of its affiliates are or have been carried on or conducted, or the powers of the directors are or have been exercised, in a manner that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of a member”
• Possible that non members may still qualify as “complainants” for the purpose of compliance or restraining order or derivative action (except a religious corporation) based on the broad scope of the definition of “complainant” in the ONCA
• However, lack of economic incentives to invoke these corporate law remedies may mean less member litigation than shareholder litigation in relation to OBCA and CBCA corporations
• But even a non-member could allege breach of trust under s.10 of the Charities Accounting Act in the case of charities

10. Conflict of Laws
• ONCA must be read in conjunction with applicable charity law
• If there is a conflict between the ONCA or its regulations and a provision made in any other legislation that applies to the following
  – A non-share capital corporation, then the provision in the other legislation prevails
  – A charitable corporation, then the legislation applicable to charitable corporations prevails
• Some provisions of the ONCA will not apply to charities

• ONCA permits directors to fix their remuneration and to receive reasonable remuneration and expenses for any services they provide to the corporation in any other capacity
  – Common law rule overrides the ONCA – prohibits directors a charity to receive direct and indirect remuneration from the charity
  – But directors may be reimbursed out-of-pocket expenses
  – Possible to seek PGT consent court order to permit directors be paid, but generally high threshold for such an order
### Section 21
- ONCA permits directors and officers to enter into contracts or transactions with the corporation as long as they disclose any conflict of interest that may exist.
  - Common law rule overrides the ONCA – prohibits directors of charities to place their personal interests in conflict with their duty to the charity.
  - Regardless of whether there is actual loss to the charity.
  - Possible to seek PGT consent court order to permit directors be paid, but generally high threshold for such an order.

### Section 32
- ONCA permits corporation to invest its funds as its directors think fit, subject to its articles or by-laws or any limitations accompanying a gift.
  - Section 10.1 of the *Charities Accounting Act* overrides the ONCA – states that s.27 to s.31 of the *Trustees Act* applies.
  - Prudent investor rule applies to the directors of charities.
  - Directors must consider certain criteria to invest.
  - Authorizes delegation to an agent in certain circumstances.

### Section 33
- ONCA permits corporation to indemnify the directors and officers and to purchase insurance.
  - ONCA expressly requires that the purchase of insurance be in compliance with the *Charities Accounting Act* and its regulations.
  - Regulation 4/01 under the *Charities Accounting Act* requires directors to consider certain factors enumerated in the regulation before they consent to the indemnification of its directors or purchasing D&O insurance.
  - The indemnification or the purchase of insurance must not render the corporation insolvent.
C. OVERVIEW OF CONTINUANCE PROCESS

- Part III of the OCA will be repealed upon proclamation of the ONCA and ONCA will immediately apply.
- 3 year grace period for OCA corporations to comply.
- Failure to continue within the 3 year grace period:
  - Will not result in dissolution of the corporation by the government.
  - Letters patent, supplementary letters patent and by-laws will be deemed to be amended to comply with the ONCA, non-compliant provisions deemed to become invalid.
  - Will result in uncertainty as to which provisions apply.
- Prudent for existing OCA corporations to continue under the ONCA sooner as opposed to later within the three year grace period.

Steps for continuance:
- Review its letters patent and by-laws.
- Contact CRA (if a registered charity) where there are proposed changes to the purpose(s).
- Prepare Articles of Continuance and other required documents.
- Create new by-laws.
- Get membership approval.
- File required documents.
- Certificate of Continuance will be issued.
- Charities – send Certificate of Continuance, Articles of Continuance and new by-law to CRA.

Unresolved issues regarding continuance process:
- It has not been determined if charities incorporated in Ontario will be required to have their articles approved by the PGT.
- Not known what will be the position of CRA on the process of continuance, i.e. will it be the same as CNCA?
- Social clubs with share capital will have 5 years to continue – different rules.
As part of the continuance process, OCA corporations may, by articles of amendment, amend any provision in their letters patent, supplementary letters patent, by-laws or special resolution to bring the provision into conformity with the ONCA.

Timing to change membership class structure:
- May put new structure in new ONCA by-law as part of the continuance process – but may allow members whose membership class was removed to possibly have the right to challenge the changes.
- Consider revising the by-law under the OCA first before continuance into ONCA.

D. PRACTICAL STEPS FOR CONTINUANCE
1. Collect governing documents
   • Letters patent, supplementary letters patent
   • All current by-laws, including amendments
     – Amending by-laws
     – Members’ resolutions?
     – Board resolutions?
     – Are by-laws valid? Were they properly adopted?
   • Can obtain microfiche copies from Ministry for LP and SLPs
   • CRA may have by-laws
   • Collect governance related documents – e.g., organizational charts, policies, manuals

2. Review governing documents and consider
   • Do they reflect current governance structure? If not, what is current governance structure?
   • Do they reflect current governance process? If not, what is current governance process?
   • Are changes desired? What are they?
   • Are there new provisions to be inserted?
   • Write them down
   • Come up with a wish list

3. Review the key features of the ONCA
   • This understanding will help the corporation determine how its governance structure and the content of the articles of continuance and by-laws will be impacted.
4. Compare ONCA rules with current governance structure and practice
   • Are the current by-laws or the desired governance structure and process inconsistent with ONCA requirements?
   • If inconsistent with a ONCA mandatory requirement, how will the corporation adjust its governance structure and process in order to ensure compliance?
   • If inconsistent with a ONCA default requirement, is the preferred alternative mechanism permitted under the ONCA? Should the overriding provision be set out in the articles or by-laws?
   • If different options are prescribed, which one should the corporation choose? Should the preferred option be set out in the articles or by-laws?

5. Determine whether changes should be made prior to continuance
   • Changes to membership rights
     – Under ONCA - separate vote by class or group of members will be required if to change the rights attached to a class or group of members or for certain fundamental changes
     – Regardless of whether the membership class is a voting class or non-voting class.
     – Each class of members (including non-voting members) will have a de facto veto right
   • Some corporations may want to collapse classes into 1 voting class
   • Changes to corporate objects
     – Purposes of the corporation will need to be stated in the articles of continuance
     – May want to update them to reflect and align with current or future activities
     – If registered charity, needs CRA approval
     – May want to apply for SLP under OCA on parallel basis
6. Timing of Continuance

- Some corporations will want to continue right away, others may want to wait
- Revising governance structure to be reflected in new by-law may need some time for directors and members to consider
- Considerations
  - Length of time and complexity of process to revise the by-laws
  - Nature of changes in new by-laws – substantive vs administrative
  - Size of membership
  - Changes to membership structure
  - Changes to corporate objects

7. Draft articles of continuance and new by-laws

- Information on articles of continuance not available yet
- By-law will need to be replaced or substantially revised because the ONCA differs from the OCA
- OCA contained very few rules, ONCA provides many detailed rules
- Some changes may only be administrative
- Some changes may require detailed considerations and consultation with members
- Understanding the ONCA framework
  - Rules in the Act
  - Some details in the Regulations
  - Need to refer back and forth between the Act and the Regulations

8. Approaches to by-law drafting

- Minimalist approach
  - ONCA contains detailed rules, so by-laws do not require the same level of details
  - By-laws to set out provisions:
    - Override the default rules in the ONCA
    - Utilize optional rules in the regulations
    - Important governance procedures
  - Advantages - simple by-laws, no risk of amending by-laws to remove ONCA requirements or violate ONCA requirements
  - Disadvantages - Have to work with 4 or 5 documents back and forth and need to know where to look for what and which provisions take precedence if conflict
Comprehensive approach
- Detailed by-laws will be a consolidation of all mandatory rules, default rules that have not been overridden, overriding provisions, etc.
- Will still need to work with articles, but limited provisions in the articles
- Advantages - one go to place for essential governance procedures
- Disadvantages - More upfront cost and time to prepare by-laws, by-laws will need to clearly identify which provisions can be amended and which ones cannot

9. Obtain membership approval and filing
- Need special resolution to approve articles of continuance
- May require separate class vote of the articles and by-laws if certain membership rights are amended
- Once approved, file articles of continuance and other documents with Ministry
- Will be issued certificate of continuance
- No need to file approved by-laws with the Ministry

10. Other consequential filings and records updates
A) Canada Revenue Agency
- Registered charities have to file certificate of continuance, articles of continuance and new by-laws with CRA
- If purposes have been changed as part of the continuance process, the corporation may obtain pre-approval from CRA for new purposes before filing articles of continuance
- If no pre-approval is obtained, then CRA may require that the governing documents be revised if they do not meet CRA’s requirements – need to apply for articles of amendment
B) Provincial and territorial filings
   • May need to update provincial or territorial registrations
   • e.g., corporate registrations, business name registrations, fund-raising registrations, etc.
   • Ontario charities – not sure what is required by Public Guardian and Trustee

C) Other filings
   • May be required to provide continuance documents with third parties, e.g.,
     – Funding organization
     – umbrella organization

D) Updating corporate records and procedures
   • Corporate minute book
   • Other documents, e.g., corporate governance policies, manuals, etc.
   • Staff and volunteers will need to be trained and become familiar with the new governance documents

E. CONCLUSION
   • Monitor Ministry and CRA updates
   • Be familiar with the ONCA rules
   • Prepare early
   • Have someone or a committee be responsible for the process
   • Have the board engaged early on
   • Seek legal help, conduct legal review, prepare draft by-laws
   • Do not miss the 3 year time frame for continuance
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