

ONTARIO BAR ASSOCIATION
Not-for-Profit and Charitable Organizations
in the Health Sector:
Evolving Governance & Compliance Issues
April 8, 2013

WORKING WITH THE CNCA: INCORPORATION AND CONTINUANCE

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2

OVERVIEW

- Status of the *Canada Not-For-Profit Corporations Act* (CNCA)
- Overview of Incorporation Process
- Overview of Continuance Process
- Key Features of the CNCA
- Drafting Articles
- Drafting By-laws
- Special Considerations for Continuance

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3

A. STATUS OF THE CNCA

- *Canada Corporations Act* (CCA) not updated since 1917
- New CNCA enacted on June 23, 2009
- In force on October 17, 2011
- Replaced Part II of CCA
- As of March 12, 2013, only 763 of approximately 17,000 corporations had continued

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B. OVERVIEW OF INCORPORATION PROCESS

- Replaces the letters patent system with a statutory regime similar to *Canada Business Corporations Act*
- Incorporation as of right - removes Ministerial discretion to incorporate
- Faster
- File articles of incorporation to obtain certificate of incorporation, not letters patent
- Only one incorporator
- Corporation has capacity, rights, powers and privileges of a natural person
- *Ultra vires* doctrine no longer applies
- May carry on activities outside Canada to the extent that the laws of that jurisdiction permit

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5

C. OVERVIEW OF CONTINUANCE PROCESS

- The new rules do not apply automatically to CCA corporations
- Existing CCA corporations will be required to continue under the CNCA within 3 years of proclamation – i.e., by October 17, 2014
- Failure to continue will result in dissolution of the corporation
- Can amend letters patent and by-laws prior to continuance under CCA

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- All CCA corporations will need to
 - Review letters patent and by-laws
 - Prepare articles of continuance, notice and new by-law
 - Get membership approval
 - File articles and notice with Corporations Canada, no filing fee
 - Certificate of continuance will be issued
 - File approved new by-law within 12 months of adoption
 - Charities – send certificate of continuance, articles of continuance and new by-law to CRA

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7

D. KEY FEATURES OF THE CNCA

1. Understand the CNCA Framework

- Rules in the Act
- Details in the Regulations
 - “prescribed”
 - “regulations”
- Need to refer back and forth between the Act and the Regulations
- Articles
- By-laws
- Unanimous member agreement

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8

2. Soliciting and Non-Soliciting Corporations

- All corporations categorized into soliciting and non-soliciting corporations
- Becomes a soliciting corporation if it receives more than \$10,000 in its last financial period from
 - Public donations
 - Federal, provincial and municipal governments
 - Conduit entities
- Status starts at the AGM in the following fiscal year for 3 years
- Low threshold means many corporations will become soliciting corporations, some may move in and out
- Need to monitor their funding sources and track their soliciting status

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9

- Implications of being a soliciting corporation
 - Minimum 3 directors, at least 2 directors must not be officers or employees of the corporation or its affiliates
 - No material effect on registered charities because directors cannot receive remuneration
 - Articles must provide for the distribution of remaining property on dissolution to qualified donees
 - No unanimous member agreement
 - File annual financial statements with Corporations Canada
 - Audit and public accountant rules more stringent

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10

- If a corporation is concerned about oscillation, it can voluntarily be structured as a soliciting corporation
 - At least 3 directors and at least 2 are not employees (no employees for charities)
 - Articles to provide that property will be paid to qualified donees on dissolution
 - No unanimous member agreement
- Then, for those years when it exceeds \$10,000 threshold
 - File annual financial statements with Corporations Canada
 - Follow audit and public accountant rules for soliciting corporations

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11

3. Public Accountant and Financial Review

- CNCA divides corporations into two categories for purpose of determining obligation to appoint a public accountant and level of financial review
- Designated corporations
 - A soliciting corporation with \$50,000 or less in gross annual revenues for its last financial year
 - A non-soliciting corporation with \$1 million or less in gross annual revenues for its last financial year
- Non-designated corporations are soliciting and non-soliciting corporations with annual revenues in excess of these amounts

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Type of Corporation (Gross Annual Revenues)			Appointment of Public Accountant (PA)	Review Engagement or Audit
Soliciting	Designated	\$50,000 or less	Members must appoint a PA by ordinary resolution at each annual meeting. Exception – Members may waive appointment by annual unanimous resolution	PA must conduct review engagement, but members may pass an ordinary resolution to require an audit instead. (If no PA is appointed, then compilation only)
	Non-Designated	More than \$50,000 and up to \$250,000	Members must appoint a PA by ordinary resolution at each annual meeting	PA must conduct an audit, but members can pass a special resolution to require a review engagement instead
	Non-Designated	more than \$250,000	Members must appoint a PA by ordinary resolution at each annual meeting	PA must conduct an audit.

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Type of Corporation (Gross Annual Revenues)			Appointment of Public Accountant (PA)	Review Engagement or Audit
Non-Soliciting	Designated	\$1 million or less	Members must appoint a PA by ordinary resolution at each annual meeting. Exception – Members may waive appointment by annual unanimous resolution	PA must conduct review engagement, but members may pass an ordinary resolution to require an audit instead. (If no PA is appointed, then compilation only)
	Non-Designated	more than \$1 million	Members must appoint a PA by ordinary resolution at each annual meeting	PA must conduct an audit.

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14

4. Directors – Number, Change and Term

- Non-soliciting corporations - minimum 1 director
- Soliciting corporations - minimum 3 directors, at least 2 of whom are not officers or employees of the corporation or its affiliates
 - But common law rule overrides CNCA - charities cannot have employees as directors
- Articles must specify a fixed number of directors or a minimum and maximum number of directors
- File notice of change within 15 days of any change or of a change in a director's address
- Maximum length of term 4 years (but no limit on number of maximum terms)

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5. Election, Appointment and Removal of Directors

- Members elect directors by ordinary resolution at an annual meeting
- Directors are not required to be members
- Exception #1 - Board may appoint a person to fill vacancy as long as there is a quorum
- Exception #2 - Articles may permit directors to appoint additional directors up to 1/3 of the number of directors elected at the previous AGM
- Directors can be removed by majority vote of members

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16

6. Ex Officio Directors

- Cannot have ex officio directors
- Examples of possible workarounds
 - Establish in by-law a special membership class that permits the class to elect a director
 - Have articles provide for the appointment of a director by the board and have a board policy that certain office holders will be appointed as directors
 - Include special qualification requirements for a particular seat on the board
- What would work will depend on the governance of the corporation

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17

7. Directors and Officers – Duties and Defence

- Directors and officers have duties to act honestly and in good faith with a view to the best interests of the corporation and to exercise the care, diligence and skill of a reasonably prudent person in comparable circumstances
- Objective standard of care, replaced common law subjective standard of care
- Directors and officers also have duty to comply with the CNCA, the regulations, and the articles, by-laws, and any unanimous member agreement

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18

8. Members

- Must have members
- Articles to set out the classes of members
- If only one class of members, all are voting
- If two or more classes, articles must provide voting right to at least 1 class
- By-laws must set out the conditions for membership
- Separate class votes
 - Fundamental changes, such as amalgamation, continuance, sale of all or substantially all of the property of a corporation other than in the ordinary course of its activities
 - Changes of the rights attached to a class or group of members

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- Class votes regardless of whether the membership class is a voting class or non-voting class – *de facto* veto rights (limited opt-out available)
- The treatment of members mirrors that in the *Canada Business Corporations Act* in relation to shareholder's rights
- In most circumstances, giving non-voting members the right to vote on fundamental changes may not be desirable

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- If corporation wants broad-based community support, may enlist them in some capacity in the corporation, but do not refer to them as "members"
- 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

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21

9. Members' Rights

- Requisition a meeting of members (5% of voting right)
- Submit proposals to amend by-laws or require any matter to be discussed at annual meetings (any one member)
- Submit proposal to nominate directors (5% of voting right)
- Access corporate records, including membership list
- Availability of unanimous members agreement (except for soliciting corporations)

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22

10. Members' Remedies

- Oppression remedy against the corporation
- Court order to commence a derivative action
- Compliance and restraining orders
- Court ordered wind-up and liquidation
- Special exemption of remedies for religious corporations if all of the following are met
 - The corporation is a religious corporation
 - The act or omission, conduct or exercise of powers is based on a tenet of faith held by the members of the corporation
 - It was reasonable to base the decision on a tenet of faith, having regard to the activities of the corporation

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23

11. By-laws

- No Ministerial approval of by-laws needed – by-laws are effective as soon as they are adopted according to the requirements of the CNCA
- Must be filed with Corporations Canada within 12 months of their adoption

12. Special Act Corporations

- Part 19 of the CNCA automatically applies
- No continuance process or any steps needed
- May continue under the CNCA
 - After continuance, special act will cease to apply
 - Continuance process is essentially the same as that for Part II CCA corporations

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24

E. DRAFTING ARTICLES

- Articles of Incorporation (Form 4001)
- Articles of Continuance (Form 4031) will replace LP and SLPs
- When preparing the articles, should prepare new by-laws at the same time because
 - Coordinate the provisions set out in articles and by-laws
 - Decide what default provisions in the CNCA to override and whether the overriding provisions should be included in the articles or the by-laws
 - Even if CNCA requires certain provisions to be set out in the by-laws, it is possible to include them in the articles instead

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25

- Information to be included in the articles
 - Corporation's name
 - Province or territory where the registered office is situated
 - Minimum and maximum number of directors or fixed number
 - Statement of purpose
 - Restrictions on activities (optional)
 - The classes, or regional or other groups of members that the corporation is authorized to establish – not condition of membership
 - Statement regarding distribution of property on dissolution
 - Additional provisions (optional)

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26

F. DRAFTING BY-LAWS

- By-laws will need to be prepared for incorporation
- Continuance - by-laws will need to be replaced or substantially revised
 - Some changes may only be administrative
 - Some changes may require detailed considerations and consultation with members

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27

1. By-law Amendment Mechanism

- CNCA provides two ways to amend by-laws, depending on the subject matter of the changes
- Default mechanism
 - Board may adopt by-laws, effective upon passage by the board
 - Must be confirmed by members at next meeting to remain in force
- Special approval
 - For matters affecting members' rights, e.g., notice of members' meetings, membership transferability and conditions, absentee voting
 - Effective when confirmed by members by special resolution (no need for board approval)

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- By-laws drafted under the CNCA must be very clear about which amending formula applies to various provisions (or risk certain by-law provisions not being legally in force) – for example:
 - Have 2 by-laws with all by-law provisions requiring special resolution in a separate by-law
 - Have 1 by-law, and place all provisions requiring special resolution in one clearly marked section
 - Have 1 by-law, and clearly mark throughout by-law which provisions require special resolution to amend
 - Have 1 by-law, and provide in articles that all by-law amendments require a special resolution

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29

2. Approaches to By-law Drafting

- By-laws will need to be replaced or substantially revised because the old and new rules are very different
- Minimalist approach by-laws
 - Rationale: CNCA contains detailed rules, so by-laws not to duplicate mandatory rules or default rules that are not to be overridden
- Comprehensive approach by-laws
 - One stop approach - consolidation of all applicable rules
 - Can have governance policy manuals to address other matters, e.g., committee structures

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30

3. Two Mandatory Provisions that Must be Included in By-laws

- Conditions of membership
- Notice of meeting of members
 - By-laws must set out the manner in which notice of meeting of members is to be given as prescribed in the regulations
 - Four options are prescribed in the regulations
 - May choose one or more of the options
- May include these provisions in the articles instead

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31

4. Types of CNCA Rules

- CNCA provides both a general framework and sets of rules for corporations to operate
- Three types of rules in CNCA
 - Mandatory Rules - Cannot be overridden by the articles or by-laws
 - Default Rules - By-laws or articles can override
 - Alternate Rules - Articles/by-laws can include certain optional rules provided by CNCA

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32

G. SPECIAL CONSIDERATIONS FOR CONTINUANCE

1. Gather Current Governance Structure and Procedure

- Collect governing documents
 - Letters patent, supplementary letters patent
 - All current by-laws, including amendments
 - Amending by-laws
 - Members and board resolutions?
 - Are by-laws valid? Were they previously filed with and approved by Corporations Canada?
 - Contact Corporations Canada to obtain copies
 - Collect other governance related documents, e.g., organizational charts, policies, manuals

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33

2. Review Governing Documents and Consider

- Do they reflect current governance structure/process? If not, what is current governance structure/process?
- Are changes desired? What are they?
- Are there new provisions to be inserted?
- Write them down

3. Review the Key Features of the CNCA

- 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

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34

4. Compare CNCA Rules with Current Governance Structure and Practice

- Are the current by-laws or the desired governance structure and process inconsistent with CNCA requirements?
 - If inconsistent with a CNCA mandatory rule, how will the corporation adjust its governance structure and process in order to ensure compliance?
 - If inconsistent with a CNCA default rule, is the preferred alternative mechanism permitted under the CNCA? Should the overriding provision be set out in the articles, by-laws or unanimous member agreement?

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35

- If different options are prescribed in the regulations, which one should the corporation choose? Should the preferred option be set out in the articles, by-laws or unanimous member agreement?
- Are there provisions that the corporation would like to include in its governing document and the CNCA is silent on those issues? If so, should the provisions be set out in the articles, by-laws or unanimous member agreement?

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36

5. Determine Whether Changes Should be Made Prior to Continuance

- Changes to membership rights
 - Some corporations may want to collapse classes into 1 voting class
 - If change membership rights as part of the continuance, then articles of continuance and by-laws also require separate class vote
 - Consider changing membership classes and rights by amending the by-laws under the CCA first, prior to continuance under the CNCA – i.e., 2 step process
- Changes to corporate objects

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37

6. 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
- File articles of continuance and notice with Corporations Canada
- Certificate of Continuance will be issued
- May file approved by-laws at the same time, or file them later within 12 months

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38

7. Other Consequential Filings and Records Updates

- CRA
 - Complete checklist
 - File certificate of continuance, articles of continuance and new by-laws with CRA
 - If purposes have been changed as part of the continuance process, need to file statement of activities
 - If dissolved due to failure to continue, its registered charity status will also be revoked

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39

- Provincial and territorial filings - e.g., corporate registrations, business name registrations, fund-raising registrations
- Ontario charities - provide Public Guardian and Trustee with certificate of continuance and articles of continuance, but not new by-laws
- Other filings - may need to provide continuance documents with third parties, e.g., funding organization, umbrella organization
- Updating corporate records and procedures - e.g., minute book, corporate governance policies, manuals
- Training - staff and volunteers will need to be trained and become familiar with the new governance documents


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40

8. Managing the Continuance Process

- 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
- Meet the October 17, 2014 deadline!

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