

Legal Issues in NFP Governance

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Introduction

Governance of not-for-profit organizations (“NFPs”), whether as registered charities or non-profit organizations, and its relationship with the law is so intrinsically intertwined that it is impossible to address one without the other. Some of the legal issues involving the governance of NFPs run the gamut from corporate law and organizational structures; trust law and fiduciary duties for the governing board; charitable law and the correlation between charitable purposes and charitable property; employment law and the interrelationship between the governing board and management; operational issues, such as privacy law, anti-spam and fundraising; as well as tax law in maintaining the tax status as either a registered charity or a non-profit organization, to name a few. Having an effective governance strategy will require an NFP to be familiar with all of these legal considerations. Best governance practice can only occur when there is knowledge of and compliance with applicable laws.

Context of Legal Governance in an NFP

In looking at the importance of legal issues in the governance of NFPs, it is important to understand the difference between for-profit and NFP entities. Within a for-profit context, there are shareholders who own the corporation and have the power to elect the board of directors. As equity owners, shareholders are the accountability base for the corporation’s quest for profit. An NFP, on the other hand, has no shareholders. Instead, it has members who have no equity interest in the corporation. Members are the accountability base for the corporation and generally have the power to elect directors. Similar to a for-profit corporation, directors of an NFP have the fiduciary duty to manage or supervise the management of the NFP, and to achieve the not-for-profit purposes of the NFP as opposed to earning a profit.

Governance of an NFP in general terms means establishing, implementing and monitoring appropriate rules and policies by the NFP’s governing body in order to achieve its not-for-profit purposes. Effective governance involves a variety of considerations. First and foremost, the NFP must identify the purposes for which it was incorporated and how decisions are to be made by its governing body. Understanding these aspects will ensure that decisions are made through proper channels of authority and for the proper reasons. It is ultimately the responsibility of the NFP’s governing board to focus on achieving the purposes of the NFP.

In establishing a proper governance regime, it is also important for NFPs to ensure that appropriate structural and operational due diligence is followed. This means that the board must have a good understanding of the structure of the organization and how decisions by the board and members are made.

In order for effective decisions to be made, a meeting must be held by those charged with making the decisions in question. However, directors and officers of NFPs are often not familiar with the applicable rules that apply to holding a meeting of the board or the members. Some of the key issues to consider when holding a meeting are outlined below.

Considerations before calling meetings

How and when meetings are to be held will be based on a variety of considerations. For instance, before calling a meeting, it is important to determine the legislation under which the NFP was incorporated because different incorporating statutes may create different requirements for the NFP. The statute may also contain rules on how meetings must be held.

It is also necessary to look at organizational documents, such as letters patent or articles of incorporation. These documents sometimes contain provisions that are relevant to the conduct of meetings. Generally, however, the most relevant and informative document for meetings is the general operating by-law of the NFP. It is necessary to ensure that the by-law was properly adopted and it is compliant with applicable legislation.

It is also important that proper notice is provided since invalid notice may affect the validity of meeting decisions. Notice must be provided in order to ensure that persons who are entitled to attend a meeting are aware of the meeting. Notice must also be provided in a manner which is *bona fide* and clear. In general, who is entitled to receive notice will depend on whether it is a meeting of the directors or the members of the NFP.

Board Meetings

Directors, as the governing body, have the duty to manage or supervise the management of the activities and affairs of a corporation as codified in both the *Canada Not-for-profit Corporations Act* and the yet to be proclaimed Ontario's *Not-for-Profit Corporations Act*. Board meetings provide directors with the opportunity to express their views before coming to a collective decision. Resulting board resolutions constitute the authority for dealing with third parties and to direct the course of the corporation.

Members' Meetings

In contrast to board meetings, members' meetings are held to allow members to call the board to account. Who qualifies as a member will vary depending on an NFP's incorporating documents. However, even if members and directors consist of the same group of individuals, separate board meetings and members' meetings must be held to transact business as required.

In general, there are two types of meetings for members: general meetings (for which all members of the corporation are invited to attend) and meetings of a particular class or section of the members. Different purposes and results can occur with regard to both general and class meetings of members. As well, there are two types of general meetings of members: annual meetings (which must be held once per year in order to transact certain transactions and elect directors) and special meetings (which are called from time to time as required).

Minuting the Meeting

Given the importance of the business that is transacted at meetings, NFPs must develop and implement careful methods to record decisions of the board and members. This is done by preparing and keeping

proper meeting minutes. Incorporated NFPs are generally required to maintain minutes of meetings by the corporate statutes under which they are incorporated. In addition, other statutes may also have books and records requirements that include maintaining minutes (e.g., the *Income Tax Act*).

The purpose of recording minutes is to provide a concise record of decisions and deliberations. In the absence of evidence to the contrary, minutes of meetings are records of proof concerning what transpired at the meeting. As such, minutes also serve to inform directors, members and agents of the NFP of such decisions. Minutes also provide a means of informing the courts of decisions made by the organization with regard to future litigation or a regulator, such as CRA in the event of a tax audit.

Summary

Exercising appropriate legal governance of an NFP is a complex exercise that requires appropriate due diligence and consideration across a variety of areas of law. It involves careful balancing of director responsibility and the board's fiduciary duty to the purposes for which the NFP was incorporated. Governance involves compliance with legislation, letters patent/articles, by-laws and an array of other areas of the law. Governance is not achieved unless compliance with the law is accomplished.



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