THE NEW GOVERNANCE REGIME FOR FEDERAL CHARITABLE CORPORATIONS

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I. INTRODUCTION

Canadian charitable corporations have long suffered from lack of an adequate federal incorporation choice. Part II of the *Canada Corporations Act*[1] (the "CCA"), which was last substantially revised in 1917, has long been recognized as outdated, cumbersome and filled with gaps.[2] The problem besetting the charitable sector has been compounded by the lack of modernized not-for-profit ("NFP") corporate legislative choices at the provincial and territorial levels except in Saskatchewan,[3] where modern legislation went into effect in 1997.

Apart from its WWI vintage, Part II of the CCA is sparse (consisting of 6 sections) and awkward to use (incorporating by reference, *mutatis mutandis*, various provisions from Part I of the CCA that applied to for-profit corporations before their migration to the *Canada Business Corporations Act*[4] beginning in 1975). Incorporation under Part II of the CCA is by letters patent, which is an exercise in Crown prerogative and slow by modern standards. By-laws require board, membership and Ministerial approval before becoming effective. Corporate borrowing can only be authorized by a special by-law passed by a least 2/3rds of the members at a special meeting. The CCA does not contemplate modern methods of holding board or membership meetings such as by conference call or teleconferencing. Nor does it recognize the validity of board and membership resolutions passed by written consent. Continuances to or from the CCA are not allowed. Beyond forcing the corporation to liquidate, membership rights and remedies under the CCA are rudimentary. Board powers, duties and defences (such as the good faith reliance and due diligence defences) are left to the unreformed common law. There is no relaxation of the audit requirement irrespective of the charitable corporation's size or the willingness of its members to forego an audit.

The charitable sector's plea for a modern governance corporate statute has finally been answered. On June 23, 2009, Bill C-4, the *Canada Not-for-profit Corporations Act* (the "Act"), received Royal Assent.[5] The unofficial best estimate as to when the Act will come into force is late Spring 2011. The coming into force of the Act should be welcome news indeed not only for the nearly 19,000 active federal NFP corporations (many of them charitable corporations) that will soon be able to continue under the Act[6] but, as well, for the many more provincial and

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[1] R.S.C. 1970, c. C-32.

[2] On the early history of federal NFP corporate statutes and the subsequent reform initiatives, see Coleen Kirby, "Background Paper for Former Bill C-62: An Act Respecting Not-for-profit Corporations and Certain Other Corporations", presented to the Ontario Bar Association, Trusts and Estates Law, February 3, 2009.

[3] *Non-profit Corporations Act, 1995,* S.S. 1995, c. N-4.2 (the "Saskatchewan Act").

[4] Now, R.S.C. 1985, c. C-44 (the "CBCA").

[5] Now, S.C. 2009, c. 23. To more immediately differentiate the Act from other corporate legislation, this article sometimes refers to the new Act as the "CNCA". Note that this article is based, in part, on the version of the draft regulations released for public consultation on June 17, 2010 (interchangeably, the "Draft Regulations" or the "CNCR").

[6] Note that the 19,000 figure excludes approximately 5,000 CCA Part II corporations that appear to have stopped filing annual reports and are, therefore, deemed to be inactive. Statistics for Part II CCA corporations were provided by Industry Canada on January 25, 2010.

territorial NFP corporations that will have the option of moving to the Act under its voluntary continuance provisions.[7]

One example of the Act's benefits to federal charitable corporations is that they will now have the ability to pass written resolutions in lieu of holding meetings. This will be of particular benefit to smaller charitable corporations as it will eliminate the need to go through the formal process of calling a meeting where there are only a handful of directors or members. Another example is the relaxation of the audit requirement for small charitable corporations. These and other examples of the benefits of the Act are discussed in further detail at Parts IV and V of this paper.

This paper reviews the types of NFP corporations contemplated under the Act (Part II), summarizes the rules that will apply to charitable corporations (Parts III and IV), analyzes possible practical problems with the Act and suggests possible solutions to any such problems (Part V) and outlines the process for continuing under the Act (Part VI) before concluding (Part VII).

II. APPLICATION TO FEDERAL CHARITABLE CORPORATIONS

A key to understanding the Act is to recognize that it differentiates among certain NFP corporations and accords modest differential treatment depending on the defining characteristics of the corporation. In particular, the Act recognizes three types of federal NFP corporations: (a) non-soliciting corporations; (b) soliciting corporations; and (c) religious corporations. A religious corporation will generally form a subset of (b). As will be seen, a charitable corporation could fit into any of these types but will, generally, not fit within category (a).

1. Non-Soliciting Corporations

Non-soliciting corporations are the residual category.[8] Thus, any corporation that is not a soliciting corporation fits into the non-soliciting category.

2. Soliciting Corporations

The Act recognizes a fundamental distinction between soliciting and non-soliciting corporations. The statutory distinction roughly correlates to the real-world distinction between public benefit corporations (which includes charitable corporations) and mutual benefit corporations, except that the Act relies on a measure of public funding as a proxy for the difference in the corporation's intended beneficiaries or purpose. The basic premise is that corporations that receive public funds (in a broad sense) should, in the public interest, be subject to tighter regulation than those corporations that do not rely on public funding. There are,

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[7] Based on 2003 data, there were estimated to be approximately 161,000 NFP corporations in Canada. See Statistics Canada and Special Survey Division, Business and Trade Statistics Field, *Cornerstones of Community: Highlights of the National Survey of Nonprofit and Voluntary Organizations,* 2003 revised (Minister of Industry, 2005 Catalogue No. 61-533-XIF) at 5, available online at:
http://nonprofitscan.imagecanada/ca/files/nonprofitscan/en/nsnvo/nsnvo_report_english_pdf).

[8] Note that the Act uses, but does not define, the term "non-soliciting corporation".

therefore, 2 separate elements of the distinction. First, there are minimum governance standards or rules imposed on soliciting corporations that are not imposed on non-soliciting corporations.[9] Second, there is a concomitant need to differentiate the 2 types of corporations. In this regard, the Act relies on the brightest of bright-line tests: funds received in a specified timeframe.

In general, the Act does not attempt to distinguish between soliciting and non-soliciting corporations on the basis of their underlying objects, the nature of their underlying activities or their charitable (or non-charitable) status under the *Income Tax Act* (Canada)[10] (the "ITA"). Instead, under the Act, the definition of "soliciting corporation" is based on whether aggregate receipts from a short-list of public sources during a financial period are in excess of $10,000.[11] If a corporation's revenues from public sources exceed $10,000 in, say, 2011 (FY1), the corporation would be a soliciting corporation commencing at its next ensuing annual meeting (held in 2012 or FY2) and ending (unless extended by its revenues in a subsequent financial period) at the annual meeting held 3 years later (*i.e.*, in 2015 or FY5). In effect, this low financial threshold comprises a *de minimus* exemption. It is designed to filter out the inadvertent capture of corporations that do not receive significant public funds. The annual period to calculate revenues strikes a balance between continuity for an organization over time and flexibility where its funding sources have permanently changed.

The funding sources that determine whether a corporation is "soliciting" are:

(a) public donors (*i.e.*, more specifically, donors who are not members, directors, officers or employees of the corporation at the time of the funding request or persons who are related by blood, marriage or cohabitation arrangement to such persons);

(b) governments or governmental agencies (whether federal, provincial or municipal); and

(c) conduit entities (*i.e.*, other soliciting corporations or other entities that have received funds in excess of $10,000 in its previous financial period from these same sources).[12]

Funding source (c) (conduit entities) is primarily intended to capture indirect funding from public sources, *i.e.*, funds received through a conduit that is itself publicly funded (such as the United Way).

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[9] See the discussion in Parts III and IV of this article.

[10] R.S.C. 1985, c. 1 (5th Supplement). This is subject to an exception discussed in connection with liquidation distributions in Table 1 below.

[11] Act, s. 2(1) definition of "soliciting corporation" and ss. 2(5.1) and (6) read in conjunction with CNCR, s. 16.

[12] Act, s. 2(5.1). See W. D. Gray, "The Late, But Welcome, Arrival of a New Federal Not-for-profit Corporations Law" (2010), 49 C.B.L.J. 40 (the "*CBLJ Article*"), at 45, concludes that the approach to differentiating between soliciting and non-soliciting corporations is one of the Act's fundamental strengths. The other fundamental strengths are selecting the CBCA model, adapting the CBCA model to NFP corporations, defining NFP corporations exclusively by their liquidation constraints and differentiating soliciting and non-soliciting corporations by functional rules and a bright-line financial test.

To clarify, a donation from a person who is not an existing member at the time of the funding request, but, who, in accordance with the articles or by-laws governing admission of members, becomes a member as a result of making a donation is to be included in calculating the receipt of public funds. However, a donation from, or membership contributions or dues payable by, an already existing member does not count in determining the receipt of public funds. Similarly, unsolicited donations (such as a gift left to the charitable corporation under a will) do not count in determining the amount of public funding.

The test for determining whether a corporation is a "soliciting corporation" is effectively applied on the last day of its fiscal year-end.[13] The test is not applied at any other point during a fiscal period. Thus, for example, assume that the fiscal period of corporation, C, ends on December 31 each year and that it only receives $6,000 in public funds on December 15, 2011 and a further $6,000 in public funds on January 15, 2012. C will not become a soliciting corporation by virtue of these receipts because in no financial year did its receipts from public funds exceed $10,000. On the other hand, if C receives $6,000 on January 15, 2011 and a further $6,000 on December 15, 2011, it would become a soliciting corporation from its 2012 annual meeting through to its 2015 annual meeting. A non-soliciting corporation becomes a soliciting corporation at the first annual meeting held after the financial period in which its revenues from public sources exceed $10,000.

As a further safety-value, the Act empowers the Director appointed under s. 281 to determine that a specific applicant corporation is not, or was not, "…a soliciting corporation if the Director is satisfied that the determination would not be prejudicial to the public interest."[14]

In most cases, a significant charitable corporation will be a soliciting corporation because of its receipt of >$10,000 in donations in a fiscal year. This paper will hereafter assume that the annual donations to the charitable corporation exceed $10,000 and will not, therefore, consider the application of the Act to small incorporated charities (*i.e.*, those whose annual donations do not exceed $10,000).

3. Religious Corporations

The Act provides that religious corporations enjoy an exemption from court-ordered liquidations, derivative actions and oppression proceedings (but not a compliance or restraining order issued under s. 259) if:

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[13] Under the Draft Regulations, the "prescribed period" is one financial year (each a "FY"). The "prescribed duration" is 3 years, but a corporation does not begin to be a "soliciting corporation" until the annual meeting immediately following the year-end in which it exceeds the $10,000 annual revenue threshold. The reason for the delay in change of status is to afford the corporation time to make any necessary changes at its ensuing annual meeting such as, for example, changes in the size and composition of the board, appointment of a public accountant, level of review to be conducted with respect to the annual financial statements and amendment to the liquidation distribution provisions of the articles. Thus, if corporation, C, receives $10,001 in FY1 and receives less than $10,000 in each subsequent financial year, it would become a soliciting corporation at its annual meeting in FY2 and remain a soliciting corporation until its annual meeting in FY5.

[14] Act, s. 2(6).

(a) the impugned act, omission, conduct or exercise of powers is based on a tenet of faith held by the members of the corporation; and

(b) it was reasonable to base the act, omission, conduct or powers on the tenet of faith, having regard to the corporation's activities.[15]

The Act does not, however, attempt to define what constitutes a "religious corporation" or a "tenet of faith". Instead, these concepts have been intentionally left to the courts. Thus, religious corporations will not be entirely immune from the disciplinary effects of the liquidation, derivative action and oppression remedies. For example, courts will be able to deal with cases involving misappropriation of church property but will not have jurisdiction to hear disputes involving religious tenets of faith that are more properly argued outside of any courtroom.

In most (but not necessarily all) cases, a religious corporation can be expected to receive a type and level of funding that will make it a soliciting corporation.

III. REGULATING CHARITABLE CORPORATIONS

As stated, the Act regulates soliciting corporations more tightly than non-soliciting corporations. The particular rules imposed on charitable corporations whose revenues exceed $10,000 in a financial year are set out in Table 1 below.

Table 1 – Regulation of Charitable Corporations (whose Annual Revenues > $10,000)

Subject	Soliciting Corporation
Liquidation of residual assets[16]	Any residual assets (after satisfying all liabilities and returning property to a donor who gave the property on condition that it would be returned on dissolution) are to be distributed exclusively to one or more "qualified donees", defined as such under the ITA.[17] Qualified donees under the ITA comprise registered charities, registered national arts

[15] *Ibid.*, ss. 224(2)(liquidation), 250(3)(derivative action) and 253(3)(oppression remedy). While a complete discussion of the need for a carve-out for religious corporations is beyond the scope of this article, it is doubtful that courts would choose to adjudicate on tenets of faith in the absence of specific provisions. Courts pay defence to the business judgment of boards and management of for-profit corporations without legislative mandate. Much the same institutional incapacity operates in the case of tenets of faith as it does in the case of the business judgment rule. See *Peoples Department Stores Inc. (Trustee of) v. Wise*, 2004 SCC 68, [2008] 3 S.C.R. 461, 244 D.L.R. (4th) 564 (S.C.C.). That said, courts will doubtless find the specific carve-outs handy.

[16] As stated, the *CBLJ Article*, *supra*, note 12, at 44-45, lists the Act's approach to defining the NFP corporation on the basis of its liquidation constraint as one of its fundamental strengths.

[17] Act, ss. 235 and 234. Note that s. 235 technically extends beyond non-soliciting corporations to include other "registered charities" within the meaning of s. 248(1) of the ITA and corporations that have received >$10,000 from public sources in any financial period ended within 5 years of the liquidation date. See, also, the CNCR, s. 37. For purposes of the liquidation distribution, the corporations to which s. 235 applies might be described as "extended soliciting corporations". Section 235 is the only occasion when the Act refers to "registered charities".

	service organizations, housing corporations in Canada set up exclusively to provide low-cost housing for the aged, the Crown (federal, provincial or territorial), Canadian municipalities, the United Nations and its agencies, foreign universities the student body of which ordinarily includes Canadian students and foreign charitable organizations to which the Government of Canada has made a gift in the donor's taxation year or in the 12 months before that period.[18]
Board composition[19]	Minimum of 3 directors and a minimum of 2 non-management directors (*i.e.*, directors who are not officers or employees of the corporation or an affiliate).[20]
Appointing a public accountant and waiving the audit requirement[21]	See Table 2 of this paper.
Filing annual financial statements[22]	Must file annual financial statements with Corporations Canada where they will be available for inspection/copying by any member of the public.
Unanimous member agreement ("UMA") or unanimous member declaration ("UMD")[23]	Not available to a soliciting corporation.[24]

The default rules applicable to every charitable corporation under the Act are that it must appoint a public accountant and have an audit of its annual financial statement. However, in recognition that, for smaller charitable corporations, the costs of appointing a public accountant

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[18] ITA, ss. 110.1(1)(a) and (b), 118.1(1), 149.1(1) and 248(1) definition of "qualified donee".

[19] The *CBLJ Article*, *supra*, note 12, at 55-57, expresses the concern that the rules applicable to non-soliciting corporations (including boards consisting of only one director or that exclude outside directors) may encourage unwarranted exploitation of the tax exempt status available to certain NFP organizations.

[20] Act, s. 125. Here, the term "non-management" is meant to be short-hand for a director who is neither an officer nor an employee of the corporation or any affiliate.

[21] The *CBLJ Article*, *supra*, note 12, at 63, questions whether the distinctions between soliciting and non-soliciting corporations with respect to appointing a public accountant and the level of review of financial statements could have been eliminated in the interests of regulatory simplification.

[22] The requirement that soliciting corporations file their financial statements with Corporations Canada (where they will be available for inspection and copying by any member of the public) is justifiable on the basis of providing transparency and, thereby, encouraging public confidence in NFP corporations - that, by definition, receive funding from public sources. Generally, public disclosure of the financial statements of non-soliciting corporations would be an inappropriate intrusion into the affairs of what are essentially "mutual benefit" organizations. Nevertheless, for policing reasons, the Director retains the authority under the Act to order a non-soliciting corporation to file its financial statements with the Director, but, at the same time, the Act exempts such financial statements from public disclosure through Corporations Canada.

[23] Since members of charitable and other soliciting corporations have no economic rights as such (either before or upon liquidation), a UMA or UMD is inappropriate for a soliciting corporation.

[24] Act, s. 170(1).

and having an audit may outweigh the incremental benefits, various exemptions are available in the Act and the regulations based primarily on the status of the corporation as a soliciting corporation, the aggregate revenue in the last completed financial period of the corporation and annual membership approval. As well, the Director appointed under the Act is vested with the discretion to, in effect, increase the revenue thresholds applicable to particular corporations.[25] These exemption rules are summarized in Table 2 below.

Table 2 – Soliciting Corporation Exemptions from Public Accountant and Audit Requirements

Annual Revenues ("AR") for Previous Fiscal Year ("FY")	**Public Accountant ("PA")**	**Audit/Review Engagement/Compilation[26]**
AR ≤ $50,000	PA not required if members entitled to vote at an annual meeting unanimously consent. Waiver must be made annually.[27]	Compilation applies if no PA. If PA appointed, review engagement applies unless members pass an ordinary resolution (*i.e.*, not less than a simple majority voting approval) requiring an audit.[28]
$50,000 < AR ≤ $250,000	Appointment of PA required unless (i) the Director is satisfied that deeming AR to be ≤ $50,000 would not be prejudicial to public interest; and (ii) the other conditions immediately above are met.[29]	Audit may be waived in favour of review engagement by special resolution of members (*i.e.*, not less than 2/3rds voting approval).[30]

[25] *Ibid.*, s. 190. The Director appointed under the Act has the power to deem a soliciting corporation not to have exceeded the $50,000 threshold (governing the appointment of a public accountant) and $250,000 threshold (governing the requirement for an audit rather than a review engagement report) where to do so "would not be prejudicial to the public interest". Note that the Director's power under s. 190 is in addition to the Director's power under s. 2(6) to, in effect, make a determination that a particular corporation is deemed not to be a soliciting corporation.

[26] In a compilation, no public accountant expresses any opinion on the financial statement. Where a public accountant does prepare the compilation report, the financial statement is accompanied by a "notice-to-reader" warning of the accounting firm's limited engagement.

[27] Act, ss. 179(a) and 182, and CNCR, s. 80(1).

[28] Act, s. 188. Note that, in these circumstances, only the approval of those members entitled to vote at an annual meeting is needed to require an audit. Members not entitled to vote at an annual meeting have no say on whether to require an audit.

[29] *Ibid.*, ss. 181(1) and 190(a).

[30] *Ibid.*, ss. 189(2) and 190(b), and CNCR, s. 84. Again, in these circumstances, only the approval of those members entitled to vote at an annual meeting is necessary to require an audit. Members not entitled to vote at an annual meeting

$250,000 < AR	Same as immediately above.	Audit required unless (i) the Director is satisfied that deeming AR to be ≤ $250,000 would not be prejudicial to the public interest and (ii) the other conditions immediately above are met (in which case review engagement applies).[31] If (i) the Director is satisfied that deeming AR to be ≤ $50,000 would not be prejudicial to the public interest and (ii) the other conditions above for waiving appointment of PA are met, compilation report applies.[32]

IV. MODERNIZED CORPORATE LAW FRAMEWORK

The new Act provides a comprehensive, modern framework for the governance of federal charitable corporations and other federal NFP corporations. It is closely modelled on the CBCA template - by far the dominant Canadian corporate model. Use of the CBCA template allows federal charitable corporations, their advisors and the courts to tap into the rich reservoir of case law that has accumulated under the CBCA, and cognate federal, provincial and territorial corporate legislation, during the past 35 years.

1. Incorporation

The Act abandons the letters patent system that makes incorporation an exercise in Crown prerogative and, therefore, not subject to judicial challenge. Instead, incorporation under the Act is as of right (subject to the same name clearance requirements found in the CBCA),[33] except that, under the Act, there are no mandatory legal elements such as “Inc.”, “Corp.”, “Association” or “Society”.

Articles of incorporation for a CNCA corporation will closely parallel the articles required for incorporation of a CBCA corporation. This will include the name of the corporation (except, in the case of a CBCA, one of the mandatory legal elements), the province where the registered office is located, the number of directors or the minimum and maximum number of directors and any restrictions on the activities that the corporation may carry on.[34] In addition, the articles must set out the classes, or regional or other groups, of members that the corporation is authorized to establish and, if there are 2 or more classes or groups, any voting rights attaching

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have no say on waiver of an audit requirement (unless, for example, the articles specifically require a separate class approval).

[31] Act, s. 190.

[32] *Ibid*., ss. 189(2) and 190(b), and CNCR, s. 84.

[33] Act, s. 13(1) and CNCR, Part 3 (Corporate Names), ss. 42-59. For CBCA corporations, the counterparts are CBCA, s. 12(1) and the *Canada Business Corporations Act Regulations, 2001*, SOR/2001-512 (the “CBCR”), Part II (Corporate Names), ss. 17-34.

[34] Act, ss. 7(1)(a), (b), (d) and (e).

to these classes or groups.[35] Further, the articles must contain statements concerning (a) the distribution of residual assets on liquidation and (b) the purpose of the corporation.[36]

Finally, the articles may, but are not required to, entrench any provisions that could be set out in the by-laws.[37] Where the articles do so, "[a]ny requirement under [the] Act to set out a provision in the by-laws is deemed met by setting out the provisions in the articles."[38]

2. Abolition of *Ultra Vires* Doctrine, and Restricting the Activities of Registered Charities

Like the CBCA, the new Act abolishes the *ultra vires* doctrine.[39] Thus, the statement of purpose in the corporation's articles will not operate to invalidate activities carried on by the corporation that a member or third party could argue fall outside the authorized purposes of the corporation. Rather, CNCA corporations will enjoy all of the rights, powers and privileges of a natural person, thereby enabling such corporations to engage in any commercial or non-commercial activities, subject only to voluntary restrictions contained in the articles.[40]

A corporation that is intended to be a registered charity under the ITA will need to adopt voluntary restrictions on its activities to meet the requirements of Canada Revenue Agency ("CRA") to qualify for, and maintain, status as a registered charity. For example, a charity whose objects state that the corporation is to provide shelter for the poor could cast its articles to state that: "The corporation shall not carry on any activities other than the provision of shelter for the poor".[41] Such restrictions can be enforced by way of a compliance or restraining order under s. 259 (not through invalidating all acts that contravene the restriction). In addition to restrictions on its activities and a statement of purpose, the articles of a charitable corporation should also include a statement that the corporation will be operated on a non-profit basis and that directors will not be remunerated in their capacity as such.

3. Directors and Officers

The CNCA replaces the common law duties of care and loyalty applicable to directors and officers with statutory duties of care and loyalty identical to those under the CBCA and incorporates both the statutory due diligence and good faith reliance defences enshrined in the CBCA.[42] Thus, each director and officer of a CNCA corporation owes a duty of loyalty exclusively to the corporation. As well, each director and officer is subject to an objective duty

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[35] *Ibid.,* ss. 7(1)(c).

[36] *Ibid.,* ss. 7(1)(f) and (g). However, the Act assigns no legal purpose to the purpose requirement.

[37] *Ibid.,* s. 7(3).

[38] *Ibid.,* s. 7(3.1). Stated otherwise, where the Act states that a statutory rule is subject to the by-laws (opt-out) or that the by-laws may provide for a rule (opt-in), the reference in the Act to the "by-laws" includes the articles if that by-law provision is entrenched in the articles.

[39] *Ibid.,* s. 16(1). See, also, the further discussion on s. 16(3) of the Act at Part VI.1 *infra*.

[40] *Ibid.,* ss. 16(1) and 17(2).

[41] Saskatchewan Act, *supra*, note 3, s. 16(2).

"to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances". It remains to be seen whether how courts will apply this objective standard of care in the circumstances of an NFP corporation. Meanwhile, there is no reason to expect that courts will accord directors and officers of NFP corporations more lenient treatment that is accorded directors of a CBCA corporation.

The CNCA expands the rights of indemnification, facilitates the advance of defence costs and permits a charitable corporation to purchase directors' and officers' liability insurance coverage.[43] With respect to indemnification, the main issue is likely to be the ability of the corporation to good on its obligation to indemnify a director and officer. With respect to the purchase of liability insurance, the issues will include availability, policy limits, deductibles and scope of coverage.

The CNCA adopts substantially the same statutory conflict of interest regime found in the CBCA.[44] Thus, a director or officer who has a direct or indirect interest in a material contract or transaction with the corporation (including as a director or officer of the opposite party) must:

(a) disclose the nature and extent of the conflicting interest to the board or appropriate board committee at the earliest opportunity;[45] and

(b) with limited exceptions, abstain from voting on any resolution to approve the contract or transaction.[46]

In addition, the contract or transaction must:

(c) either be:

  (i) approved by those directors entitled to vote (*i.e.,* a vote that excludes that of the conflicted director);[47] or

  (ii) confirmed by special resolution of the member (*i.e.*, approval of not less than 2/3rds of the members voting on the resolution);[48] and

(d) be fair and reasonable to the corporation when it was approved or confirmed.[49]

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[42] Act, ss. 148(1), 149 and 150.

[43] *Ibid.,* s. 151.

[44] *Ibid.,* 141.

[45] *Ibid.,* ss. 141(1) through (4).

[46] *Ibid.*, s. 141(5). The exceptions allow the director to vote on the approval of a contract or transaction that primarily relates to her remuneration as a director, officer, employee or agent, is for indemnity or insurance or is with a subsidiary or other affiliate.

[47] *Ibid.,* s. 141(8).

[48] *Ibid.,* s. 141(9).

[49] *Ibid.,* ss. 141(8)(c) and (9)(c).

Failure to comply with these requirements can result in an application by the corporation or any of its members to set aside or annul the contract or transaction on any terms that the court fit or require the conflicted director or officer to account to the corporation for any profit or gain realized on the contract or transaction.[50]

To facilitate modern board practices, the Act expressly allows directors to meet by conference call and to transact business by way of written resolution.[51]

4. Members and Membership Rights/Remedies

Except with respect to disputes on tenets of faith of religious corporations, members of charitable corporations will enjoy enhanced rights, including the rights to bring an oppression action and to seek leave of the court to bring a derivative action on behalf of the corporation.[52] Subject to the same exception for religious tenets of faith, members retain their existing rights under the CCA to bring an application for the just and equitable winding-up of their corporation. As well, the Act expands the grounds for seeking winding up of the corporation.[53] Courts will have greater flexibility to avoid draconian liquidation orders and instead make lesser, more context-sensitive orders that are still sufficient to rectify the grounds of complaint.[54] Finally, members (including members of religious corporations) will have the right to seek a summary compliance or restraining order.[55]

Time will tell how often and in what circumstances members will invoke these new remedies. Members (unless they happen to be “qualified donees” entitled to residual assets upon liquidation) of charitable corporations will not have the same economic incentives to invoke corporate law remedies that shareholders in CBCA corporations have long exercised.

Perhaps, more important than these judicial remedies, the Act gives members the power to set the number of directors and remove directors before the expiration of their terms of office by ordinary resolution.[56] This makes directors accountable to members and subject to removal by members at any time.

Again, as with directors, the Act expressly allows members to meet by conference call and to transact business by way of written resolution.[57]

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[50] *Ibid.*, s. 141(1).

[51] *Ibid.*, ss. 136(7) and 140(1) respectively.

[52] *Ibid.*, ss. 253 and 251 respectively. Under s. 251, leave can also be granted to defend an action brought against the corporation.

[53] *Ibid.*, s. 224.

[54] *Ibid.*, s. 224(3), which cross-references to the wide relief available under the s. 253 oppression remedy.

[55] *Ibid.*, ss. 259 (compliance/restraining order) and 260 (summary application).

[56] *Ibid.*, ss. 130 and 131. Subsection 7(5) of the Act prevents the articles from entrenching directors, *i.e.*, the articles cannot require that more than a simple majority of those members entitled to vote thereon is needed to remove a director.

[57] *Ibid.*, ss. 159(4) and 166(1) respectively.

5. By-laws

The Act replaces the cumbersome procedure for adopting or amending by-laws, which under the CCA, requires approval by the directors, members and, finally, Corporations Canada. Under the new Act, directors will have the residual power to pass by-laws and amending by-laws.[58] With some exceptions, the board may pass by-laws or amending by-laws that take effect immediately and that will remain in effect unless the members fail to confirm such by-laws or amending by-laws at the next ensuing meeting of members.[59] Amending by-laws that change:

(a) conditions required for being a member (*i.e.*, membership eligibility);

(b) the manner of giving notice to members entitled to vote at a meeting of members (*i.e.*, membership meeting notices); or

(c) method of voting by members not in attendance at a meeting of members (*i.e.*, proxy or other absentee voting),

only come into effect when passed by special resolution of the members.[60]

In addition, while by-laws or amending by-laws must be filed with Corporations Canada within 12 months from confirmation by the members, they will no longer require the approval of Industry Canada or any other governmental approval.[61] By-laws do not lose any of their effectiveness just because they are not filed.

6. Borrowing

Under the Act, directors have the default power to borrow and grant security on behalf of the corporation subject to any contrary restrictions imposed by the articles or by-laws.[62] In this important respect as well, the borrowing authority rules long applicable to CBCA corporations will be extended to CNCA corporations, which should help reduce their transactions costs incrementally.

7. Fundamental Changes

To a significant extent, the CNCA tracks the CBCA provisions governing amendments to articles (including changes to membership rights), amalgamation, continuance (import to the CNCA or export from the CNCA to the laws of a province, territory or foreign jurisdiction), sale (lease or exchange) of all or substantially all the corporation's property and court-ordered arrangements and reorganizations.[63] As stated in Part I of this paper, the provisions for

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[58] *Ibid.* s. 152(1).

[59] *Ibid.*, ss. 152(2) and (3).

[60] *Ibid.*, ss. 197(1)(e), (h), (l) and (m).

[61] *Ibid.*, ss. 152(3) and 153, and CBCR, s. 60.

[62] Act, s. 28(1).

[63] *Ibid.*, Part 13 (Fundamental Changes), ss. 197-216.

continuance[64] into or out of the federal jurisdiction are new and have not previously been available under the CCA.

In general, fundamental changes will require the approval of 2/3rds of each class of member voting at a special meeting or the unanimous written consent of such members. However, in contrast to the CBCA, the CNCA does not provide a statutory dissent and appraisal right.

V. PROBLEMS AND SOLUTIONS

1. Does Membership Have Any Privileges?

Unlike business corporations, charitable corporations governed by the Act are non-share capital corporations and, as such, are unable to distribute profits to members before liquidation.[65] In the case of an extended soliciting corporation, the distribution of net assets cannot be made to members unless, fortuitously, they happen to be "qualified donees" under the ITA.[66] In effect, the Act provides that the interest of members in a charitable corporation or other soliciting corporation are non-pecuniary. That leaves voting rights, which may be dealt with in the articles – failing which certain default rules apply.

The Act states that members of a corporation have the right to vote at any meeting of the members if there is only one class or group of members. The inherent voting rights extend to the election of directors,[67] waiver or appointment of a public accountant,[68] waiver of an audit,[69] amendment of the articles,[70] authorization of certain by-law amendments[71] or confirmation of by-law amendments made by directors,[72] long-form amalgamations,[73] export continuance,[74] sale

[64] *Ibid.,* ss. 211 and 212 (import continuance) and 213 (export continuance).

[65] Act, ss. 34(1) and (2).

[66] Even if the articles of an extended soliciting corporation do not provide for a liquidation distribution to one or more qualified donees, s. 235(3) directs the liquidator to apply to court for a distribution to one or more qualified donees. See footnote 17 above for the meaning of the term "extended soliciting corporation" as used in this article.

[67] *Ibid.,* s. 128(3).

[68] *Ibid.,* s. 181(1) and 182(1).

[69] *Ibid.,* s. 188 and 189.

[70] *Ibid.,* s. 197(1).

[71] *Ibid.,* s. 152(6) and 197(1).

[72] *Ibid.,* s. 152(2).

[73] *Ibid.,* s. 206(5).

[74] *Ibid.,* s. 213(5).

of all or substantially all of the assets of the corporation,[75] dissolution[76] or liquidation and dissolution.[77]

Where, however, the corporation has 2 or more classes or groups of members, these voting rights (with the limited exceptions set out in s. 199(1) of the Act) need only be attached to at least one membership class or group.[78] It is, therefore, possible to have a class or group of members that has no voting rights outside the minimum voting rights mandated under the Act. However, in that case, since the class of membership also has no right to receive any property of the charitable corporation either before or at the time of liquidation, it is questionable what purpose there is in providing for a meaningless or empty class in the articles. One-third of the members of a class ("Class A") in a charitable corporation that has no pecuniary or economic rights and no voting rights can block an amendment to the articles to create a new class of members having rights superior to those of Class A. Even here, however, the articles can expressly opt-out of such veto power in favour of the Class A members. Technically, a special resolution of the Class A members is also required to approve a voluntary liquidation of the corporation[79] - although this would not prevent an application for a court-ordered liquidation.[80] Thus, membership in a charitable corporation means something but not necessarily much.

A member can pursue various remedies accorded members and other "complainants" in the Act, the most important of which are as follows:[81]

(i) oppression remedy;[82]

(ii) application for a court-ordered liquidation;[83]

(iii) derivative action;[84] and

(iv) compliance and restraining order;[85]

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[75] *Ibid.,* s. 214(6).

[76] *Ibid.,* s. 220(3).

[77] *Ibid.,* s. 221(3).

[78] *Ibid.,* s. 154(3) and (4).

[79] *Ibid.,* s. 221(3).

[80] *Ibid.,* s. 224(1).

[81] Note that numerous lesser member remedies are scattered elsewhere through the Act.

[82] Act, s. 253.

[83] *Ibid.*, s. 224(1).

[84] *Ibid.*, ss. 251 and 252. Note that, while restrictions apply to use of the derivative action on behalf of a religious corporation, a member can additionally or alternatively resort to s. 141(10) in cases where the corporation has entered into a contract or transaction giving rise to a conflict of interest by a director or officer.

[85] *Ibid.,* s. 259.

(v) controversies with respect to the election of directors or the appointment of a public accountant,[86]

subject, in the cases of (i), (ii) and (iii), to the limitations applicable to tenets of faith of religious corporations.

2. Liability of Directors and Officers

Section 146 of the Act imposes liability for unpaid employee wages, vacation pay and reimbursable employee expenses on directors.[87] This is in addition to the other liabilities imposed under the Act on directors. In 2003, the Saskatchewan Act was amended to protect directors and officers of Saskatchewan NFP corporations from excessive or unwarranted liability.[88] In part, Saskatchewan introduced the liability shield to remove financial disincentives that discourage strong director candidates from joining the boards of NFP corporations.[89]

Section 112.1 of the Saskatchewan Act immunizes directors and officers of a Saskatchewan corporation from personal liability for misfeasance. It does not seek to protect directors and officers from malfeasance, *i.e.*, breach of the statutory duty of loyalty (including self-dealing). Nor can it shield directors from federal laws imposing personal liability for withholdings and remittances under the ITA and under federal GST,[90] CPP[91] and EI[92] legislation.

For directors and officers of federal charitable corporations who want greater liability protection than the CNCA affords (particularly directors and officers of NFP corporations engaged in high-risk activities), consideration might therefore be given to continuing the corporation from the federal jurisdiction to the Saskatchewan Act as soon as the CNCA comes into effect. After all, partial immunity is preferable to liability for which a director or officer may claim indemnification from the corporation. Continuance to Saskatchewan would take place in 2 steps. First, if the federal charitable corporation is currently governed by Part II of the

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[86] *Ibid.,* ss. 169(1) and (2).

[87] In *Proulx v. Sahelian Goldfields Inc.* (2001), 204 D.L.R. (4th) 670, the Ontario Court of Appeal held that director liability to employees "for all debts" under the CBCA means that directors are, subject to the monetary cap set out in the CBCA, jointly and severally liable for unreimbursed out-of-pocket expenses such as travel, food and lodging expenses that an employee incurs in the course of providing services to the corporation. Subsection 146(1) of the CNCA contains the identical formulation found in s. 119 of the CBCA. Similarly, in *Mills-Hughes v. Raynor* (1988), 63 O.R. (2d) 343, 47 D.L.R. (4th) 381, the Ontario Court of Appeal held that director liability to employees "for all debts" (which appears in CBCA, s. 119(1) and OBCA, s. 131(1)) means that directors are liable for vacation pay despite the failure to explicitly list liability for vacation pay in the CBCA.

[88] Saskatchewan Act, *supra,* note 3, as amended by S.S. 2003, c. 33, s. 2, adding s. 112.1 to the Saskatchewan Act.

[89] The *CBLJ Article*, *supra*, note 12, at 60-62, briefly discusses the controversial issue of providing a partial immunity to protect directors and officers of NFP corporations from misfeasance claims. The CBA Submission at 24-26 recommended that the CNCA include a provision closely modeled on s. 112.1 of the Saskatchewan Act.

[90] Directors' liability for goods and services tax ("GST") is provided for under the *Excise Tax Act*, R.S.C. 1985, c. E-15.

[91] Directors' liability for Canada Pension Plan ("CPP") contributions is provided for under the *Canada Pension Plan*, R.S.C. 1985, c. C-8.

[92] Directors' liability for employment insurance ("EI") premiums is provided for under the *Employment Insurance Act*, S.C. 1996, c. 23.

CCA, it would initially continue under the CNCA and then, as step 2, immediately continue from the CNCA to the Saskatchewan Act.[93]

Unless there is a continuance to Saskatchewan (where there is a partial immunity from liability), the main protective devices under the CNCA are:

(a) obtaining directors' and officers' insurance (subject to all the coverage deductibles, caps, exclusions, defences and premium charges such insurance entails);

(b) obtaining indemnity (subject to the charitable corporation's continuing solvency);

(c) exercising a proper and timely dissent; and

(d) if all else fails, tendering a resignation before the liability begins to accrue.

VI. TRANSITIONING TO THE NEW ACT

Once the new Act comes into force, it will no longer be possible to incorporate a charitable corporation under Part II of the CCA. Rather, all new federal charitable corporations will be formed under the new Act.

A charitable organization to which Part II of the CCA applies will have a period of time within which to apply for a continuance under the new Act. If the CCA body corporate does not apply for a continuance within 3 years after s. 297(5) of the Act comes into force, Corporations Canada may, upon first giving notice in writing to the body corporate and to each director, dissolve that body corporate. The body corporate will cease to exist on the date set out on its certificate of dissolution.

To continue under the Act, a CCA body corporate will need to file articles of continuance under s. 211. The content of the articles of continuance parallels that of the articles of incorporation described at Part IV.1 *supra*. In addition, once the Act comes into force, a charitable body corporate formed under provincial, territorial or foreign law may apply to Corporations Canada for a certificate of continuance under s. 211 if so authorized by the laws of its home jurisdiction and if the body corporate satisfies, or by its articles of continuance would satisfy, the requirements for incorporation under the Act.

Finally, over the years, our federal Parliament has enacted various Special Act charitable corporations. In most respects, the CNCA will not apply to Special Act corporations. In other cases, however, the CNCA will apply in part by reference or adoption. For example, s. 294 of the CNCA provides that, with some exceptions, certain provisions apply to any body corporate without share capital incorporated by Special Act of Parliament and not continued any other

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[93] There is no provision for a direct continuance of a CCA Part II corporation to a provincial or territorial statute.

federal Act.[94] Federal Special Act corporations need to examine closely to what extent, if at all, the CNCA applies to them.

VII. CONCLUSION

The CNCA can be fairly described as a comprehensive, modern corporate statute, the primary focus of which is enabling or private ordering. That is, it allows federal charitable corporations, their boards and members to organize their affairs in a manner that is optimal for their particular needs. By no means can the Act be fairly characterized as a heavy-handed regulatory overlay on federal charitable corporations. The Act imposes only those basic minimum requirements on charitable and other soliciting corporations as detailed in Part III above.

[94] These provisions are Part 3 (*i.e.*, ss. 16-19, abolishing the *ultra vires* doctrine, providing for the right to carry on the body corporate's activities throughout Canada and to exercise extraterritorial capacity, abolishing the constructive notice doctrine and codifying the indoor management rule) and ss. 160(1)(calling annual meetings), 168 (court-ordered meetings), 212 (amendment of charter), 221 (voluntary liquidation and dissolution), 222 and 223 (involuntary dissolution) and 279 (filing annual return) and Part 19 (Special Act Bodies Corporate Without Share Capital).