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**An Analysis of  
Ontario's New Not-For-Profit Corporations Act  
Bill 65**

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Ontario's Bill 65, the *Not-For-Profit Corporations Act, 2010* (the "**New Act**" or the "**Bill**") was recently introduced, as expected after the Province's consultations with the not-for-profit sector over the course of several years and the passage of the *Canada Not-For-Profit Corporations Act, 2009* last year.

The New Act is designed to apply over a period of three years to most of the corporations that are governed by the Ontario *Corporations Act* (the "**Current Act**"), including those created by special legislation. The exceptions include insurance companies and companies with objects "in whole or in part of a social nature" (a "**Social Corporation**"), which are subject to special transitional rules.<sup>1</sup> Co-operatives and business corporations will continue to be subject to their own Acts.

The Ministry of Consumer Services indicated in its press release that the legislation was intended to:

1. Enhance corporate governance and accountability;
2. Simplify the incorporation process;
3. Give more rights to members; and
4. Better protect directors and officers from personal liability

Summaries of those measures and the New Act can be found in the press releases and the Explanatory Notes to the Bill.<sup>2</sup> The Explanatory Notes provide a good summary of all of the New Act's provisions and can be downloaded here: [http://www.ontla.on.ca/bills/bills-files/39\\_Parliament/Session2/b065.pdf](http://www.ontla.on.ca/bills/bills-files/39_Parliament/Session2/b065.pdf)

Rather than providing a reworded summary, this bulletin aims to explore some of the changes from the Ontario *Corporations Act* (the "**Current Act**") regime, which most Ontario not-for-

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<sup>1</sup> Section 210(3) of Bill 65

<sup>2</sup> <http://news.ontario.ca/mcs/en/2010/05/ontarios-not-for-profit-corporations-act.html>, [http://www.sse.gov.on.ca/mcs/en/Pages/News\\_12May2010.aspx](http://www.sse.gov.on.ca/mcs/en/Pages/News_12May2010.aspx), and [http://www.ontla.on.ca/bills/bills-files/39\\_Parliament/Session2/b065.pdf](http://www.ontla.on.ca/bills/bills-files/39_Parliament/Session2/b065.pdf).

profit corporations are subject to and differences between the New Act and the federal *Canada Not-For-Profit Corporations Act, 2009*<sup>3</sup>.

### **Distinction Between Charitable Corporations, Non-Charitable Corporations and Public Benefit Corporations**

As many of the corporations governed by the Current Act are charities (whether at common law or registered charities) or are not-for-profit corporations which solicit funds from the general public, the fact that the New Act creates categories based on whether a corporation is a charity will be of interest to many readers. The New Act treats charitable corporations differently than non-charitable corporations and public benefit corporations differently than non-public benefit corporations. The New Act also distinguishes between “religious corporations” and those which are not. Coupled with the different transitional provisions for Social Corporations, and the revenue criteria which are used to determine audit and review engagement requirements, the New Act divides the world of not-for-profit corporations it governs into eight or more categories.

A charitable corporation is defined as a corporation incorporated for religious, educational, charitable or public purpose.<sup>4</sup> This definition is the same as that used in the Ontario *Charities Accounting Act*, but may not exactly correspond to or even be intended to correspond to the common law definition of a charity or to whether the corporation is a registered charity pursuant to the *Income Tax Act*. A non-charitable corporation is simply defined as one that is not a charitable corporation.<sup>5</sup> The New Act establishes a public benefit corporation as one which is either a charitable corporation or a non-charitable corporation that receives more than \$10,000 a year from government grants or from persons who are not either employees, directors, officers or members of the corporation.<sup>6</sup> It should be noted that the definition is not identical to the federal *Not-For-Corporations Act* and the implications differ as well.

### **Simplification Of The Incorporation Process**

One of the most important changes the Bill implements is how not-for-profit corporations can be created. Bill 65 would replace incorporation at the discretion of the Minister with incorporation as of right.<sup>7</sup> Letters Patent will be replaced Articles of Incorporation. Articles of Amendment would now replace Supplementary Letters Patent. It is expected that the incorporation process will become significantly faster and more efficient. Incorporation will likely become possible within about one week rather than as much as six weeks or more.

### **For-Profit Activities**

The press release for Bill 65 explicitly claims that it will “allow not-for profits to engage in for-profit activities where the revenues are reinvested in support of the corporation’s not-for profit purposes” and that it does away with any “uncertainty about which profit-generating activities are permitted.”<sup>8</sup> The only significant new reference in the New Act to this matter is worded as a restriction rather than a permission, requiring the articles of incorporation, “[i]f any purposes of a corporation are of a commercial nature” to explicitly “state that the commercial purpose is intended only to advance or support one or more of non-profit purposes of the corporation.”<sup>9</sup>

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<sup>3</sup> *Canada Not-for-profit Corporations Act, 2009, c. 23*

<sup>4</sup> Section 1 of Bill 65

<sup>5</sup> *Ibid.*

<sup>6</sup> *Ibid.*

<sup>7</sup> Section 7 of Bill 65

<sup>8</sup> <http://news.ontario.ca/mcs/en/2010/05/ontarios-not-for-profit-corporations-act.html>.

<sup>9</sup> Section 8 of Bill 65

It should be borne in mind that the Canada Revenue Agency's position with respect to unrelated business would continue to apply to registered charities. It is not clear that this legislation overrides any common law principles or trust obligations, which may continue to preclude a not-for-profit corporation from carrying on for-profit commercial activities if those activities do not directly also advance its purposes.

## **Directors**

One of the peculiarities of the *Corporations Act* was the requirement for a fixed number of directors, which could only be changed by a special resolution of the members. The New Act continues the requirement for a fixed number of directors but permits the corporation, by special resolution, to empower the directors to determine and fix the number of directors.<sup>10</sup> This permits the members to consider whether the number of directors should be easily changed early in its life (or immediately after the New Act comes into force), grant the directors that power after which the number of directors can be conveniently changed without having to be brought back again to the members for a special resolution. The greater flexibility offered by this provision approximates other jurisdictions' ability to create boards of directors whose size can be changed from time to time, limited only by a minimum and maximum number.

The Bill changes the current requirement that all directors must be or become members of the corporation, requiring that only two-thirds of the directors be members of the corporation. The Bill does place restrictions on who may be a director of a public benefit corporation, requiring that no more than one-third of the directors may be officers or employees of the corporation or its affiliates.<sup>11</sup> Once again, common law may further restrict the ability of employees or paid officers of the corporation to become directors of a charity.

A further significant change is that directors may be removed by an ordinary resolution rather than by a special resolution making the requirements for electing and removing a director the same.<sup>12</sup>

The New Act sets out to protect directors by implementing an explicit and statutory standard of care for directors and officers to act honestly and in good faith with a view to the best interest of the corporation and to exercise the care, diligence and skill that a reasonable prudent person will exercise in comparable circumstances.<sup>13</sup> There is a further requirement in the New Act for directors to comply with the corporation's articles and by-laws.<sup>14</sup> The Bill then sets out a broad due diligence defence, allowing directors and officers to rely in good faith on financial statements, on professional advisors and on the reports and advice of officers and employees, although the reliance upon the report or advice of an officer or an employee is subject to an explicit condition that it be "reasonable in the circumstances to rely on the report or advice". The purpose of these provisions is to change the standard from a subjective standard that has been applied to professionals with particular expertise serving as directors to the objective one. The hope is that people with particular expertise will not be dissuaded by the subjective standard from serving. It will probably take a court decision that this statutory standard supercedes any differing common law standard for there to be absolute clarity, as we expect that in circumstances where a particular director had expertise

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<sup>10</sup> Section 22 of Bill 65

<sup>11</sup> Section 23 of Bill 65

<sup>12</sup> Section 26(1) of Bill 65

<sup>13</sup> Section 43(1) of Bill 65

<sup>14</sup> Section 43(2) of Bill 65

which should have informed his or her decision making that an injured party will still assert the common law standards notwithstanding the Ministry's intentions.

Insurance for officers and directors is explicitly referred to in the New Act and it incorporates the *Charities Accounting Act* and its regulation's provisions respecting the purchase of insurance for directors of charitable corporations. The New Act also provides that directors and officers may be indemnified by the corporation, including costs involved in defending the derivative actions which are introduced by this Bill. However, it does not incorporate the conditions that a charitable corporation would have to satisfy before indemnification found in the *Charities Accounting Act* regulation, even though they are similar to the insurance requirements. The New Act does make any charities law paramount over its provisions so we would suggest that a charitable corporation should continue to conform with the *Charities Accounting Act's* regulations prior to indemnification.

### **Meetings and Notices**

The New Act does away with the Current Act's permission for charitable corporations to give notice of members' meetings by publication of the notice in a newspaper where the majority of the members are located. Nor does it provide any convenient way of posting notice for corporations which meet together in a fixed place regularly. Notice must now be actively provided to the members, which fortunately can now be done electronically. The New Act resets the minimum and maximum notice periods to 10 and 50 days.

The New Act changes the operation of those members meetings in other ways. It provides clarity and a default for quorum (50% of the members).<sup>15</sup> It permits a single member to raise a "proposal" at an annual meeting, replacing the requirement that a minimum of 5% of the members seek to place a resolution before the next meeting.<sup>16</sup>

Perhaps most conveniently, the members meeting could now be held entirely electronically<sup>17</sup> and voting can be by electronic means<sup>18</sup>.

### **Members Rights**

As promised by the Province, the New Act does give more rights to members and expand their remedies. Following the lead of the *Canada Not-For-Profit Corporations Act, 2009*, and the business corporation statutes, the Bill would give members the right to bring derivative actions and to seek court ordered investigations.<sup>19</sup> Furthermore, members who disagree with a decision to implement a fundamental change in the corporation (such as changing the activities the corporation may carry on, an amalgamation, the sale, lease or exchange all or substantially all of its property) are entitled to make their dissent known and then to be paid by the corporation a fair value of their membership interest, provided the corporation is not a public benefit corporation.<sup>20</sup> Notionally, membership in a public benefit corporation would not and should not carry with it any personal value to the member and no right to "cash out".

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<sup>15</sup> Section 57(1) of Bill 65

<sup>16</sup> Section 17(6) of Bill 65

<sup>17</sup> Sections 53(4) and 53(5) of Bill 65

<sup>18</sup> Section 58 of Bill 65

<sup>19</sup> Sections 182 and 173 of Bill 65

<sup>20</sup> Section 186 of Bill 65

The derivative action rights track those in the federal legislation. A religious corporation, it must be noted, is not subject to a derivative action.<sup>21</sup> The investigation rights are also similar to those of the federal legislation.

It is significant that, unlike the federal legislation, Ontario chose not to implement what is known as the oppression remedy, which would have permitted a member, director, officer or even a creditor to seek a court order for any relief the court deems just for any acts the court finds oppressive or unfairly prejudicial to or unfairly disregards the interests of any shareholder, creditor, director, officer or member. The federal legislation offers this right, but tries to limit the havoc it could create by restricting the ambit of this remedy. The *Canada Not-For-Profit Corporations Act* prescribes a religious belief defence to the oppression remedy, which remains untested.<sup>22</sup> The primary difference between the oppression remedy and a derivative action is that a derivative action is designed to protect the corporation and its purposes while the person seeking the oppression remedy is seeking something for herself or himself.

The New Act does provide for the right to seek an investigation by a court appointed inspector upon application by a member or debtor of a corporation on the grounds of fraud or on grounds which would otherwise have justified the oppression remedy.<sup>23</sup> An investigation order is also primarily a public interest remedy as the courts have determined it is not to be used as a substitute for discovery in the pursuit of private interests.<sup>24</sup> In the author's view, that investigation right, combined with the presumption that the interests of the corporation and its purposes (whether charitable or not) are adequately protected by derivative actions, justifies the omission of the oppression remedy from the New Act.

Of significant import to corporations who maintain not-voting memberships, are the New Act's provisions which give all members, including those who do not have general voting rights, the ability to vote in certain limited circumstances, such as on any extraordinary sale, lease or exchange of all or substantially all of the property of the corporation, an amalgamation, a change to any rights or conditions attached to those non-voting members or a change in the rights of other classes of members so as to change the relative rights of the non-voting members.<sup>25</sup> This complicates the decision about whether non-voting members should be retained and while there are ways to work around these obligations, unduly complicates matters for many existing not-for-profit corporations.

### **Corporate Governance**

The New Act explicitly invokes what lawyers call the indoor management rule for corporations it governs, so that persons who have entered into contracts with a not-for-profit corporation will not face an assertion by the corporation itself that its articles or by-laws have not complied with or that an extraordinary sale, lease or exchange of all or substantially all of the property of the corporation has not been authorized by the members.<sup>26</sup> However, if the person has or ought to have had knowledge of the fault, this section does not prevent the corporation from alleging that against that person.<sup>27</sup>

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<sup>21</sup> Section 182(3) of Bill 65

<sup>22</sup> *Canada Not-for-profit Corporations Act*, 2009, c. 23, s. 253.

<sup>23</sup> Section 173 of Bill 65

<sup>24</sup> *Holden v Infolink Technologies Ltd.* (2005), 11 B. L. R. (4th) 128 at paras. 23 and 26 (Ont. S.C.J.).

<sup>25</sup> Section 104(2) of Bill 65

<sup>26</sup> Section 19(1) of Bill 65

<sup>27</sup> Section 19(2) of Bill 65

We would note however, that this section 19(1) does not explicitly prevent a corporation from asserting that the provisions of this Act have not been complied with, although section 16(3) does make it clear that no act of a corporation is invalid “by reason only” that it is contrary to its articles, by-laws and the New Act. Whether an assertion that the New Act is not complied with can likely be made and considered by a court if there are other grounds for holding the act to be invalid will likely be the subject of litigation sometime in the future unless the Bill is further amended. There is some comfort in the fact that this wording is common to many of the business corporation statutes.

The New Act recognizes the prevalence of audit committees amongst well governed not-for-profit organizations but does not mandate them. Where there are audit committees, the New Act does regulate their composition and requires audited financial statements to be reviewed by that committee before they are approved by the board of directors.<sup>28</sup> The New Act maintains the existing requirement that those financial statements be approved and presented to the members at the annual general meeting, but place greater restrictions on their use (e.g. requiring them to be signed and accompanied by the audit or review engagement report, if any) and sent to the members who have requested them at least 21 days before the annual meeting (or signing of resolution in lieu of an annual meeting).

### **Audit and Review Exemptions**

The Act provides small corporations with flexibility in how they deal with audits or review engagements. An auditor, defined by the Act to mean “a person authorized to practice public accountancy under the *Public Accounting Act, 2004*”<sup>29</sup> is required, unless the members of a public benefit corporation pass an “extraordinary resolution” (a vote of more than 80% of the members voting at a special meeting called for the purposes of considering that resolution), to have a review engagement carried out if its annual revenue is between \$100,000 and \$500,000 or to waive both an audit and review engagement if its annual revenue is less than \$100,000. Non-public benefit corporations may waive the requirement for an audit or review engagement if their revenue is less than \$500,000 and may specify a review engagement only if the annual exceeds \$500,000. A public benefit corporation is always required to have an audit carried out if its revenues exceed \$500,000. All of those threshold amounts may be changed by regulation. The extraordinary resolution must be renewed each year.<sup>30</sup>

### **Transition**

The Ministry of Consumer Services intends to prepare a set of standard form by-laws for not-for-profit corporations governed by the New Act. Where a corporation fails to pass organizational by-laws within 60 days after it is incorporated, section 18(1) deems that the standard organizational by-law will apply. Those standard organizational by-laws will be published in the Ontario Gazette and made publicly available.<sup>31</sup>

Corporations which are continued under this Act will be required to bring its Letters Patent, Supplementary Letters Patent, by-laws and any special resolutions into conformity with the Act and may do so by filing Articles of Amendment or by amending its by-laws, once the Act is in force.<sup>32</sup> The New Act, perhaps in recognition of the fact that not all not-for-profit corporations in Ontario will be aware of its existence and amend its articles to conform, specifically provides that any provision that is not amended to conform with the Act is deemed

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<sup>28</sup> Section 79 of Bill 65

<sup>29</sup> Section 1 of Bill 65

<sup>30</sup> Section 75 of Bill 65

<sup>31</sup> Section 18(2) of Bill 65

<sup>32</sup> Section 206(1) of Bill 65

after three years to be amended to the extent necessary to conform.<sup>33</sup> In essence, the Act's provisions will always supersede existing Letters Patent, Supplementary Letters Patent or by-laws of the corporation. Relying upon this provision is in our view highly problematic. Doing so would leave potentially large inconsistencies between the corporation's Letters Patent and by-laws, documents the directors, members and staff are most likely to go to for guidance or work with and the requirements of the Act. It is likely that actions will be taken that contravene the Act but appear to comply with those documents. Furthermore, the New Act imposes new requirements, which will likely go unnoticed and unfulfilled if they are not incorporated into the documents which are supposed to govern a corporation's activities.

The Act specifically provides for the ability of a corporation to restate its articles so that the corporation's constating documents are clearly in compliance with the Act.<sup>34</sup> A corporation may not restate its articles unless those articles are in complete conformity with the Act, necessitating the amendment of its articles.<sup>35</sup> It is our recommendation that all corporations amend their letters patent, supplementary letters patent and by-laws to conform with the Act, so as not to unintentionally create confusion and questions about whether the letters patent, supplementary letters patent and by-laws can be relied upon.

As mentioned earlier, the existing *Ontario Corporations Act* continues to apply to any company that has objects which are "in whole or in part of a social nature" for a period of five years. We expect that, while objects of a social nature are not defined in the New Act, it is likely that these are social clubs. The Current Act does contain a reference and a specific provision for these sorts of entities, based on their potential use as covers for illegal gambling or gaming houses.<sup>36</sup> Those corporations can continue to operate under the *Corporations Act* for up to five years. They may apply to continue under the New Act or another appropriate Act at any time during those five years but will be dissolved if they fail to do so by the end of the five year period.

## **Summary**

The New Act is a comprehensive update of corporate law for not-for-profit corporations in the Province of Ontario. It cleans up and resolves some of the peculiarities of the Current Act, implements an as of right and speedy incorporation process and introduces provisions which provide a reasonable balance between efficient governance by the directors of the corporation, their protection from personal liability, incorporate some of the developments in good corporate governance which are already being implemented by forward thinking organizations while providing members with some significant rights and remedies. Overall, the New Act provides a great deal more guidance and clarity about various corporate matters relative to the Current Act (many of which are not discussed in this bulletin) and provides corporations without share capital with more default options. The New Act is necessarily somewhat more complex and prescriptive than the Current Act. Bringing an existing corporation into compliance, while taking advantage of some of the conveniences it offers will require careful planning, particularly if the existing corporation does not wish to change its current structure and processes unnecessarily. The advantages offered by the New Act and the possibility of confusion and error if a corporation does not deliberately bring its constating documents into conformity justify, in our view, that exercise.

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<sup>33</sup> Section 206(2) of Bill 65

<sup>34</sup> Section 108 of Bill 65

<sup>35</sup> Section 206(3) of Bill 65

<sup>36</sup> *Corporations Act*, R.S.O. 1990, c. C.38, s. 316.

Furthermore, some organizations might consider which of the corporate acts might best suit their purposes and practices and consider whether incorporating in another jurisdiction might make sense. Perhaps most importantly for those corporations which are registered charities, in amending their constating documents and changing their practices to comply with the New Act, they will need to be careful that they continue to satisfy the Canada Revenue Agency, the *Income Tax Act* and the common law.

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