

Amending the Ontario Not-for-Profit Corporations Act to enable and support the work of organizations providing public benefit in Ontario

The Challenge

October 2010, The Ontario Not-For-Profit Corporations Act, received third reading in the Ontario legislature and is due to be proclaimed in the fall of 2012. **Unfortunately, without a few key amendments, many organizations in the nonprofit sector will have great difficulty using the act and are at risk of being significantly destabilized, and/or are faced with complex and difficult restructuring.**

The act up-dates corporate legislation for the non-profit and charitable sector; legislation that was first passed in 1903 and has not been updated since 1953. As a result the sector has been functioning with antiquated legislation for many years, which, while having many old fashioned provisions, was on the other hand, flexible enough to allow the sector to adapt and change within it. There has been enormous growth and diversity developed in the sector since 1953 and, over time the sector has evolved corporate structures that have unique features and provide the flexibility this unique sector requires.

The ONCA, the new corporate legislation for the sector was designed to maximize uniformity with the Ontario Business Corporations Act and, while many of the provisions in the new act are suitable for the sector, there are instances where the sector has evolved sector-specific practices that are not accommodated. **These adjustments to the legislation are vital because the intent and purpose of a non-profit organization with its commitment to mission is very different from that of a business corporation with its responsibility to maximize value for shareholders.**

The public, funders and indeed many working in the sector, believe that nonprofit organizations in their communities all meet the same core criteria that demonstrates their commitment to the public good. Those criteria are:

- The organization has a public purpose and mission;
- The organization operates for the public good not personal gain.
- The organization reinvests any excess revenue in its public purpose; and
- The organization retains its assets in the public domain for the public good

Regrettably, in its current form, the ONCA does not provide the assurance the public needs that public benefit organizations meet these four basic criteria. Indeed, the ONCA actively prevents many nonprofit organizations providing public benefit (the 34% of the sector who provide public benefit but are not charities) from offering permanent guarantees to their funders and communities. As a sector we worry about this disconnect between what funders and the public expect and what is provided in the new act. We also

think it will permit unscrupulous operators to abuse the public's trust to the detriment of all.

The sector has longstanding and effective governance practices that have evolved over the years that are undone by this legislation. Those alert organizations that grasp the implications of the ONCA early may be able to undertake complex and costly restructuring before the act is proclaimed. Most of the sector however will be caught unawares and chaos will ensue as they discover their corporate structure is ill suited to the new legislation.

Fortunately the amendments required to make this act supportive of the sector are relatively few and easy to make. The key ones are:

- **Members should not be allowed to pass binding resolutions on Boards of Directors.** In business corporate legislation, including the OBCA, member resolutions are advisory and non-binding on Boards of Directors. We are not clear why this act should be different. The ONCA as currently written allows binding resolutions from members which will place many Boards in difficult positions as member resolutions may be at odds with an organization's contracts and agreements with funders and community partners. Significant numbers of organizations will find themselves unable to recruit qualified candidates to serve on their voluntary boards of directors.
- **Provide an "opt-in" option to a clear and permanent definition of Public Benefit Corporation** based on organizational purpose (not revenue source). This will ensure all organizations working for public benefit have a transparent, permanent and higher threshold of accountability to their communities when they opt to become a public benefit organization.
- **Provide a permanent non-distribution constraint on dissolution for all nonprofit organizations opting to be Public Benefit Corporations** to ensure assets remain in the public domain for the long-term. This will eliminate the logistical confusion and potential for misuse created by the current temporary year-by-year asset lock in the ONCA. The temporary asset lock will cause nonprofit organizations to "yo-yo" in and out of non-distribution constraints.
- **Make non-voting members non-voting.** The ONCA currently gives non-voting members a vote on key corporate issues of fundamental importance. The sector's longstanding practice of having non-voting members not have a vote should be respected. The sector should not have to face costly and complex restructuring to accommodate a provision imported from the business sector that does not apply in a nonprofit corporation. Non-voting members (minority shareholders) in a business corporation have a financial interest in the corporation. Non-voting members in the Public Benefit

corporations have no financial interest. In member based corporations, to the extent that they have a right to participate in a distribution of the remaining assets on winding-up of the corporation, non-voting members of a non-public sector corporation should have the right to vote on matters which might affect their economic interest. There is no justification for giving voting rights to otherwise non-voting members who have no financial interest. Indeed, the sector created non-voting members precisely for individuals who should not have a vote. In the sports sector all the participating children (over 3 million) are non-voting members, and in other sectors non-voting members are corporations, other community organizations or for example magazine subscribers that wish to support and affiliate with the nonprofit.

- **Make proxies optional.** Many sector organizations do not like mandatory proxies, as they want to encourage members to attend meetings at which important issues are discussed before a decision is made. Some organizations that would be willing to use proxies strongly disagree with the right to appoint a non-member as a proxy. Organizations should be permitted to elect to use proxies or not based on their needs.
- **Amend Fair Value Payout for member-based organizations** Organizations that are not public benefit and exist to serve their members in the ONCA are required to pay to dissenting members the “fair value” of their memberships – even if they have decided that there is not to be any distribution of net assets on dissolution to members. The fairest and easiest is to restrict the payout to the member to the amount of loans the member made to the corporation. This will avoid many conflicts and misunderstandings in the non-PBC corporations. Valuing the corporate membership will be difficult and costly. It also makes sense to provide for equal distribution of assets on dissolution unless the by-laws provide other wise.

Details of Amendments - Ontario Not-For-Profit Corporations Act**REVERSE THE POWER OF MEMBERS TO OVERRIDE DIRECTORS****Delete wording**

21. ~~Subject to this Act~~, the directors of a corporation shall manage or supervise the management of the activities and affairs of the corporation. 2010, c. 15, s. 21.

Delete

~~17 (6). A member entitled to vote at an annual meeting of the members may make a proposal to make, amend or repeal a by-law in accordance with section 56. 2010, c. 15, s. 17 (6).~~

By-laws are not to be lightly amended or able to be amended solely by either the Board or the Members. The existing act has a better system of amending by-laws with better checks and balance.

Amend 56.1 and 60.1

56. (1) A member entitled to vote at an annual meeting of the members may,
(a) give the corporation notice of any matter that the member proposes to raise at the meeting for any purpose connected with the affairs of the corporation that is not inconsistent with this act, referred to as a “proposal”; and
(b) discuss at the meeting any matter with respect to which the member would have been entitled to submit a proposal. 2010, c. 15, s. 56 (1).

60.1 The members of a corporation who hold at least 10 per cent of votes that may be cast at a meeting of the members sought to be held, or a lower percentage that is set out in the by-laws, may requisition the directors to call the meeting for any purpose connected with the affairs of the corporation that is not inconsistent with this act stated in the requisition. 2010, c. 15, s. 60 (1).

The ability of the members to override the directors comes from the insertion of the phrase “Subject to this Act,” in section 21 of the new Act. That section otherwise gives the directors the exclusive authority to “manage or supervise the management of the business and affairs of a corporation”.

In the Business Corporations Act, the phrase is “Subject to any unanimous shareholder agreement,” (s. 115).

As a result, the provision allowing for member proposals to be made to a members’ meeting is not overridden by s. 21. In a business corporation, only a shareholders’ agreement can override the general authority of the directors – which is as it should be.

AMEND DEFINITION OF Public Benefit Corporation (PBC) to permit all nonprofits to choose to be public benefit corporations.

1. (1) “public benefit corporation” means,
- (a.) a charitable corporation, and
 - (b.) a non-charitable corporation, the articles of which provide that the corporation is a public benefit corporation for the purposes of this Act

The definition of public benefit corporation, draws on the similar definition of non-profit housing co-operative, in the Co-operative Corporations Act and the transitional provision contained in Section 26 of the Co-operative Corporations Statute Law Amendment Act, 1992.

ENSURE for all Public Benefit Corporations a robust non-distribution constraint, including successor obligations.

New section 89.1

89(1) This section applies to public benefit corporations and to those other corporations the articles of which provide that the corporation is subject to the provisions of this section (“asset locked corporation”).

(2) Any profits or accretions to the value of the property of an asset-locked corporation shall be used to further its activities

(3) An asset-locked corporation cannot be converted into or continued as any other kind of corporation and no attempt to do so is effective.

(4) An asset-locked corporation shall not distribute or pay any of its property to its members during its existence or on its dissolution.

(5) Despite subsection (4), an asset-locked corporation may pay a member,

(a) amounts owed to the member including interest on a member loan or any other loan from the member at a rate not exceeding the prescribed maximum annual percentage; or

(b) reasonable amounts for goods or services provided by the member.

(6) No person shall accept compensation for the withdrawal of membership by a member of an asset-locked corporation other than,

(a) compensation for amounts owed to the member by the co-operative; or

(b) compensation for improvements made by the member to the property of an asset locked corporation if the compensation is reasonable and is approved by the board of directors.

(7) A person who accepts compensation in contravention of this section shall pay the asset locked corporation an amount equal to the value of the compensation or the excess compensation and that amount is a debt the asset-locked corporation may recover in a civil proceeding.

(8) An asset-locked corporation may not amend its articles to do anything described in s. 102(1)(j) or (m) or amend its articles so that the corporation is no longer an asset-locked

corporation and no attempt to do so is effective.

(9) An asset-locked corporation may not amalgamate except with another asset-locked corporation.

Similar provisions in the Co-operative Corporations Act have been found effective to prevent a sale of assets to members: see Bridlewood Co-operative v. Superintendent of Financial Services of Ontario, a decision of the Superior Court of Justice, dated April 5, 2005.

ELIMINATE VOTING RIGHTS FOR NON-VOTING MEMBERS WHO DO NOT HAVE A RESIDUAL ECONOMIC INTEREST IN THE CORPORATION,

Add to s.1(1): “residual interest” means the right of a member to receive a distribution under s.150(1)(b)(ii) or 167(1)(d)(ii).”

Amend s.105(2): “Subsection (1) applies whether or not memberships of a class or group otherwise carry the right to vote if:

- (i) the corporation is not a public benefit corporation; and
- (ii) each member of the class or group has a residual interest.”

Amend s.111(3): “Each member of an amalgamating corporation has the right to vote in respect of an amalgamation agreement whether or not the membership of such member otherwise carries the right to vote if:

- (i) the amalgamating corporation is not a public benefit corporation; and
- (ii) the member has a residual interest.”

Amend s.116(3): “Each member of the corporation has the right to vote in respect of a continuance whether or not the membership of such member otherwise carries the right to vote if:

- (i) the corporation is not a public benefit corporation; and
- (ii) the member has a residual interest.”

Amend s.118(4): Each member of the corporation has the right to vote in respect of the sale, lease or exchange whether or not the membership of such member otherwise carries the right to vote if:

- (i) the corporation is not a public benefit corporation; and

(ii) the member has a residual interest.”

Sector uses non-voting members as an affiliation strategy to engage constituencies that should not have a vote.

MAKE PROXIES OPTIONAL AND ALLOW CORPORATIONS TO RESTRICT PROXY HOLDERS TO MEMBERS

Amend (S.64(1) to read If provided in by-laws every member entitled to vote at a meeting of the members may by means of a proxy appoint a proxyholder or one or more alternate proxyholders, who may be required to be members, as the member’s nominee to attend and act at the meeting in the manner, to the extent and with the authority conferred by the proxy. 2010, c. 15, s. 64 (1).

Delete s. 65

Voting with proxies or electronic voting should be decided by each organization.

RAISE FLOOR FOR AUDIT OR REVIEW ENGAGEMENT of Public Benefit corporations from \$100,000 to \$500,000 – similar to non-public benefit corporations, and allow for volunteer members to perform the audit function, if approved by the members.

Amend 76(2) to delete reference to “other than a public benefit corporation”

Members of a corporation may pass an extraordinary resolution,

(a) to have a review engagement instead of an audit in respect of the corporation’s financial year if the corporation had annual revenue in that financial year of more than \$500,000 or such other prescribed amount; or

(b) to not appoint an auditor and to not have an audit or a review engagement in respect of the corporation’s financial year if the corporation had annual revenue in that financial year of \$500,000 or less or such other prescribed amount. 2010, c. 15, s. 76 (2).

Delete the words “corporation, any of its affiliates, and” in section 69(1). This reflects current practice for small non-profits that are too small to afford an outside auditor. There, the members can opt to appoint one or more of their senior members to conduct the audit – as volunteers, they are permitted to do so under the *Public Accounting Act*, and the organizations resources are better spent on its activities.