GLENLYON CORPORATE CENTRE
127-4300 NORTH FRASER WAY
BURNABY, BC V5J 0B3 CANADA

General Disclaimer/Important Information

Introduction

The information contained in this document will be useful to readers with the following objectives:

- To establish a Canadian organization for non-profit purposes that requires only one person to form. ("Person" in this context means a "natural person" or individual.)
- Ideally, this organization should have the lowest possible restrictions on distribution of assets, spending, and the like.

The legal research and analysis in this document support the following conclusions:

- As discussed below, **Community Contribution Companies (CCC)** are a relevant point of comparison because they are, in principle, similar to the UK's **Community Interest Companies (CIC)** and the US's **Low-profit Limited Liability Companies** (L3C). However, their numerous restrictions and requirements are onerous compared to other the options available under Canadian law. Thus, CCCs do not satisfy the objectives stated above.
- The most attractive option based on the objectives is a **Member-Funded Society (MFS)**.
- The second-best option is a non-soliciting **Not-for-Profit Corporation (NFP)**.
- In either case, is not preferable to seek **registered charity** designation from the **Canada Revenue Agency (CRA)** because rigorous compliance requirements apply to charities. (Moreover, a MFS cannot be charity.)

After reading this entire document, consider the following follow-up questions:

- Regarding MFS:
  - In your estimation (using the information and calculation guide provided), will your organization will be under the $20,000 threshold limit for MFS status?
  - Looking forward, is your organization likely to be disqualified from MFS status by funding or operational changes in the future?
- Regarding NFP:
  - Do you intend for your organization to operate in more than one province?
  - In your estimation, will your NFP will be non-soliciting?
  - If so, will your NFP remain non-soliciting for a while or quickly exceed the $10,000 threshold limit?
- In either case, do you foresee major changes/developments in the near future that would compromise your organization's maintenance, compliance or status?

For answers to these follow-up questions,
it is best to seek legal advice that considers the specifics of your case.

Table of Contents

Community Contribution Companies (CCC)

- A Community Contribution Company is a hybrid of a traditional business corporation and a not-for-profit society. It is aimed at fostering social enterprise and socially beneficial investment in the province of BC.

- In principle, CCCs are similar to Community Interest Companies ("CIC") that exist under U.K. law and to Low-profit Limited Liability Companies ("L3C") that exist under the state law of several U.S. states.
  - However, CCCs are, in effect, more like traditional corporations than not-for-profit organizations.
  - For instance, CCCs have no special tax advantages. Moreover, CCCs are subject to numerous reporting requirements and restrictions on profit distribution, dividend payment, and dissolutions, as listed below:
    - A CCC's annual reports are accessible to any member of the public.
    - BC law restricts a CCC's ability to distribute profits to shareholders, and spending is subject to a mandatory reporting requirement.
    - BC law limits a CCC's ability to declare a dividend to its shareholders, or to pay interest on a debenture or other debt at a rate tied to company profits: limited to not more than 40% of the CCC's profit for that financial year and any unused dividend for any previous financial year.
    - CCCs are subject to an "asset lock" on dissolution that ensures 60% of its capital is put toward the stated community purposes.

- For all these reasons, CCCs do not satisfy the objectives stated in the Introduction.

Provincial — Member-Funded Societies (MFS)

- Member-funded societies are incorporated provincially under the *Societies Act*, S.B.C. 2015, c. 18.
- If an organization's object and purpose is one of the matters specified in section 2 of the *Societies Act*, then it may carry on business as a society in furtherance of that objective. Section 2 lists agricultural, artistic, benevolent, charitable, educational, environmental, patriotic, philanthropic, political, professional, recreational, religious, scientific, social, or sporting as examples of legitimate purposes.

- Under the *Societies Act,* there are two categories of societies: member-funded societies (which is new as of 2016) and other societies.
- Member-funded societies ("MFS") exist primarily for the benefit of their members and must have the following statement in their constitution:

  > *"This society is a member-funded society. It is funded primarily by its members to carry on activities for the benefit of its members. On its liquidation or dissolution, this society may distribute its money and other property to its members."*

- Note that although a society is a "non-profit" entity, this means only that the members of the society will not share in the net profits or net losses of the operation.
  - It does not mean that the society cannot earn a profit.
  - If a society accumulates assets or earns profits, the money or assets must be used in the society's operations to further the society's purposes.

- **Tax exempt status:**
  - The CRA decides if an organization, including MFSs, qualifies for tax-exempt status as a non-profit organization ("NPO").
  - NPOs are tax exempt and can receive donations, but cannot issue tax receipts like registered charities.
  - NPOs are generally exempt from paying income tax, but may have to pay tax on property income or on capital gains.
  - NPOs do not have to register federally or provincially to acquire its tax-exempt status.
  - NPOs also have much broader permitted purposes and activities than registered charities. (Under the *Income Tax Act*, a charity—whether or not it is registered—cannot be an NPO.) See **Tax** section below.

Comparing BC societies

- MFSs are subject to fewer accountability measures than other societies, that is, "ordinary", publicly funded societies.
- Other societies have comparatively more accountability measures than MFSs as well as numerous requirements regarding financial statements, distributions on dissolution, and number of directors.

Comparing BC societies		
	Member-funded societies	**Other societies**
Number of directors	One director is sufficient. There are no residency requirements.	Must have at least three directors, one of whom is ordinarily resident in B.C..
Composition of board of directors	No restrictions on number of board members who are employed by or under contract with the society.	Majority of board must not be employed or be under contract with the society.
Disclosure of remuneration	No disclosure of remuneration is required.	Financial statements must set out remuneration paid to directors and to highly paid employees/ contractors.
Financial statements	Public does not have right to copies.	Public has right to obtain copies.
Conversion to company (such as on dissolution)	Can be converted.	Not possible to convert.
Distribution of assets (money, property, etc.) on dissolution	No restrictions. For example, assets could go to members.	Assets can only be distributed to certain entities (such as non-MFS, registered charities or community service cooperatives).

Pros and Cons of MFSs

There are several pros and cons to MFSs that are related to the objectives stated in the Introduction.

- **Pros**
  - MFSs have no minimum number of directors or residency requirements, which means that means that an MFS is allowed to have only one director who need not be ordinarily resident in BC.
  - MFSs have no restrictions on the number of directors employed by or under contract with the MFS.
  - MFSs are subject to fewer accountability measures than other societies, specifically, they are not required to provide public access to financial statements, or disclose remuneration of directors, employees, or contracts to the public.
  - Upon dissolution, an MFS is allowed to
    - convert to BC company, and
    - distribute its assets to any person specified in their bylaws or in ordinary resolution, such as its members.
- **Cons**
  - MFSs have threshold limits on public donations and government funding.
    - If an MFS exceeds the threshold limit, it is no longer qualified to be MFS. Additional procedures, such as application for court approval, are required to re-obtain MFS status.
  - MFSs could be disqualified from receiving benefits, such as certain types of government funding, that other societies subject to the dissolution “asset lock” might be eligible for. This is partly because the *Societies Act* allows MFSs to distribute their assets to their members on winding up.
  - MFSs cannot issue official donation receipts because they cannot be registered charities.

Questions to ask before formation

- The *Societies Act* and *Societies Regulations* describe the two main restrictions that preclude an organization from being a MFS:
  - It cannot be a type of organization prohibited by the Act/Regulation from being member-funded.
  - It cannot receive public donations or government funding above a certain threshold, as discussed.

- The following questions help determine whether your organization can be an MFS.
  1. **Types of prohibited organizations:**
     If the answer is "yes" to any of the following, your organization cannot be an MFS:
     - Is your organization a registered charity or "qualified donee" under the *Income Tax Act*?
     - Is your organization a student society under the *College and Institute Act* or the *University Act*?
     - Is your organization a hospital society or a organization that owns, manages or operates a licensed community care facility that is designated as a hospital society under the *Hospital Act*?
     - Does your organization receive or has your organization received loans or grants of money from the British Columbia Housing Management Commission?
     - Is/has your organization [been] a service provider under the *Community Living Authority Act*?
     - Is your organization an authority that has received a grant for the previous school year under the *Independent School Act*?
  2. **Public donations and government funding threshold limit — calculation guide:**
     - What is the actual/estimated total amount of public donations plus government funding that your organization received over a 2-year period? = $ ______
       - If $ ______ is $20,000 or less, your organization can be MFS.
       - If $ ______ is more than $20,000, but is 10% or less of the society's gross income for that period, your organization can be MFS.
       - If $ ______ is more than $20,000 *and* is more than 10% of the society's gross income for that period, your organization cannot be MFS.

Details on public donations and government funding

- **Public donations:**
  - Public donations include gifts in kind.
  - Donations made by someone within the society (*viz.* member, director, senior manager, employee of society, or a spouse or relative of such person) are not considered public donations.
- **Government funding:**
  - Fees that societies earn or income received under service contracts or other contracts are not considered government funding.
  - Government funding does include grants, interest-free loans loans or with interest substantially below the market rate, or similar funding, provided by entities such as provincial/federal governments, municipalities, and the like.

How to become an MFS

- A new organization indicates if it wants to be an MFS at the time of formation. (There is a separate procedure for already existing societies.)
- Becoming an MFS is a choice. Even if a organization qualifies to be MFS, it is not required to become one. (One consideration is that MFSs are not eligible for certain types of government funding, such as community gaming grants.)

Federal — Not-for-profit Corporation (NFP)

- Not-for-profit corporations are incorporated federally under the *Canada Not-for-profit Corporations Act*, S.C. 2009, c. 23 (the "NFPCA"), which governs the incorporation of companies without share capital that operate in more than one province.
- The NFPCA distinguishes between companies that are soliciting corporations and non-soliciting corporations using threshold funding limits (similar to MFS). It uses the gross annual revenues of the company to determine the level of financial review required; this varies depending on if a corporation is soliciting or non-soliciting.
  - A "soliciting corporation" is a corporation that receives public donations and/or government grants in excess of $10,000 in a single financial year.

Some fundamentals

- **Number of directors:**
  - Every corporation must have at least one director, except a soliciting corporation, which has more. (A soliciting corporation must have no fewer than three directors, at least two of whom are not officers or employees of the corporation or its affiliates.)
- **Member classes:**
  - A corporation must have at least one class or group of members, in which case, all members are voting members.
    - A corporation may have two or more classes or groups of members, and not all classes or groups have to be given the right to vote.
    - If there is more than one class or group of members, the articles must give the right to vote to at least one class or group.
- **Tax exempt status:**
  - The CRA decides if an organization, including NFPs, qualifies for tax-exempt status as a non-profit organization (NPO). NPOs are tax exempt and can receive donations, but cannot issue tax receipts like registered charities.
  - NPOs are generally exempt from paying income tax, but may have to pay tax on property income or on capital gains.
  - NPOs do not have to register federally or provincially to acquire its tax-exempt status.
  - NPOs also have much broader permitted purposes and activities than registered charities. (Under the *Income Tax Act*, a charity—whether or not it is registered—cannot be an NPO.)
  - Does NFP need to file an *NPO Information Return*? See **Tax** section below.

- **Filing requirements:**
  - The NFPCA requires NFPs to disclose certain changes as they are implemented (e.g. amendments to articles, bylaws and directors).
  - NFPs are required to file a Form 4002 (Annual Return) within 60 days of its anniversary date (the date it was incorporated, amalgamated, or continued under the Act).

Pros and Cons of NFPs

There are several pros and cons to NFPs that are related to the objectives stated in the Introduction.

- **Pros**
  - Only one director is required for *non-soliciting* NFPs.
  - During formation, there are options for number of member classes and types of members.
- **Cons**
  - There are threshold funding limits on public donations and government funding that materially affect a NFP's "soliciting" or "non-soliciting" status.
    - If a non-soliciting NFP exceeds the threshold limit, it is no longer qualified to be "non-soliciting", and a different, more onerous set of compliance requirements will apply.
  - NFPs have comparatively more filing requirements than MFS. (As such, consider whether your organization intends to operate in more than one province.)
  - Non-soliciting NFPs cannot issue official donation receipts because they cannot be registered charities.

Tax Matters — Non-profit organization (NPO)

- An NPO, as defined in the *Income Tax Act*, is a club, society, or association that is not a charity and that is organized and operated solely for: social welfare; civic improvement; pleasure or recreation; or <u>any other purpose except profit</u>.
  - Non-profit purposes are broad (especially compared to charitable purposes). Essentially, revenues must go to programs which provide some group benefit.
  - MFSs and NFPs are NPOs once they are deemed so by the CRA.
- To be considered an NPO, no part of the organization's income can be payable to or available for the personal benefit of any proprietor, member, or shareholder, unless the exemption for amateur athletics promotion applies.
- An NPO is exempt from tax on all or part of its taxable income for a fiscal period if it meets all of the above requirements for that period.
- Tax considerations are separate from requirements for formation, ongoing compliance and reporting obligations, and certain changes in legal status (*viz.* MFS to non-MFS, non-soliciting NFP to soliciting NFP.)

<u>Why not get the "registered charity" designation?</u>

- To be able to issue official donation receipts and to be exempt from tax, the *Income Tax Act* requires that an organization created and operated exclusively for charitable purposes must register with the CRA as a charity.
  - If your organization plans to operate as a charity and wants to issue official donation receipts and not have to pay income tax, you must apply to be a registered charity. If it your charity not registered, it does not qualify for these tax advantages.
  - However, if your organization is operating as a charity, it cannot be considered a NPO even if it is not registered as a charity. An organization can only meet one definition, NPO or charity, not both.

<u>Will your organization need to file an NPO Information Return?</u>

- Your organization could potentially need to file an NPO Information Return because it is a non-profit organization as described in *Income Tax Act.*
- Your organization will need to file an NPO Information Return if it received or was entitled to receive taxable dividends, interest, rentals, or royalties totalling more than $10,000 in the fiscal period. In later years, your organization must file if its total assets were more than $200,000 at the end of the immediately preceding fiscal period.
- An organization that has to file an NPO Information Return may also have to file other returns such as a *T2–Corporation Income Tax Return*, a *T2Short*, or a *T3–Trust Income Tax and Information Return*. A corporation generally has to file a *T2–Corporation Income Tax Return*, or a *T2Short*, even though it may be an NPO.