
Backgrounder

Organizational and Supervisory Law in the Nonprofit Sector

Canadians' lives are being touched by nonprofit organizations on an increasing scale: the work of these organizations makes the national news and is in evidence at community meeting places and on people's doorsteps. Charities and other nonprofits are filling important needs in a society that is affected by growing social service demands and declining government assistance. With nonprofit groups numbering perhaps 200,000 in Canada and rising, it is critical that appropriate legislation support nonprofit activity and encourage these groups to be accountable. At present, organizational and supervisory law pertaining to nonprofits is ambiguous and outdated.

Organizational and Supervisory Law in the Nonprofit Sector is one of three new research papers commissioned by the Canadian Policy Research Networks (CPRN) with financial support from The Kahanoff Foundation. It highlights the need for modern laws that respond to the particular features of nonprofits. The paper addresses the deficiencies in the current legislation, and puts forth proposals to address three broad areas of reform.

Organizational and supervisory law must take into account the special nature of charities and other nonprofits. Regulations must oblige organizations to carry out their objectives while being managed ethically. They must also compel organizations to relate their activities and financial situation back to members, participants, donors, volunteers and other stakeholders.

What Is Organizational and Supervisory Law and Why Is It Necessary?

Organizational laws are the rules around which nonprofits are created and conduct their affairs. Organizational laws can make it easier and less costly for individuals to work out arrangements that are needed to establish and run a formal charity or nonprofit. They help establish the obligations and rights of managers, directors, members and others. Good organizational laws reduce the potential for costly conflicts down the road. Both the federal and provincial governments have legislation governing social service charities, religious organizations, social clubs and other types of nonprofits.

Supervisory law deals with the tools governments rely on to administer and enforce organizational laws. When supervisory mechanisms work well, such as in monitoring the activities of nonprofit organizations and in seeing that information is publicly available, the result can be higher

confidence in the sector. Supervisory agencies may also provide welcome support to nonprofit managers by being an important source of knowledge and advice.

Right now in Canada, this legal responsibility falls in part to the federal government through its corporation acts. Nonprofits are also regulated at the provincial level, creating a confusing, and sometimes contradictory set of organizational and supervisory requirements.

Narrowing the Gap between Existing Law and the Needs of Nonprofits

Any proposed legal reforms must permit nonprofits to continue to flourish in Canadian society. The 200,000 or so nonprofits in Canada operate under many forms and have diverse goals and philosophies. Blanket legislation must not undermine the ability of nonprofits to be innovative or to fulfil their goals.

Governments must reshape organizational law to focus on those issues that concern a broad range of types of nonprofit organizations. The following proposals address three areas where current legislation is outdated and sometimes at odds with the general purpose of nonprofits.

1. Address undesirable restrictions and omissions in the law. The law should allow nonprofits to work effectively: requirements in the law that are unnecessary and inappropriate for nonprofits should be eliminated. Also, there is a need to address certain problems with the existing legal form, "unincorporated association." Unlike corporations, unincorporated associations cannot, in their own name, own property or receive gifts of property, sue and be sued, and be bound by and benefit from civil obligations. This omission in the law should be remedied.

The needs of nonprofit organizations would also be served by having a menu of legal options that could be tailored to their specific needs. For instance, there are no provisions in the law now regarding the inner goings-on of associations. The reformed law could offer guidance to nonprofit managers on such internal matters as the rights of members, the status of honorary members, and requirements for calling and organizing meetings.

2. Recognize the importance of safeguards against fraud and misrepresentation. Trust and goodwill are associated with the notion of nonprofit. To maintain public confidence in nonprofits, legislated standards are necessary to ensure that nonprofit managers and officers apply a "duty of care" by exercising diligence in carrying out their tasks. They must also act with a "duty of loyalty", that is, honestly, faithfully, and in the best interests of the organization. These standards would apply to all nonprofits, regardless of their form or purpose, and remedy the confusion in the courts where distinctions are sometimes drawn between nonprofit corporations, trusts and associations.

Where there are no members to oversee the activities of the management and board, such as in the case of public benefit, religious and private nonprofits, strict controls could be put in place to prevent managers and directors of nonprofits from gaining financially. As well, members of nonprofit associations could be given the right to sue for breaches of duty of loyalty and to sue for compliance.

3. Supervisory Law: Promote Communication, Communication, Communication. Communication channels should be open and active. By legislating public reporting requirements, nonprofit managers and directors could be made more accountable, and members and other stakeholders

could make more informed decisions. The types of information that should be readily available to members include details of the activities, resources and outputs of nonprofit organizations. Nonprofit supervisors could audit and monitor the information for accuracy. A supervisory agency could help nonprofits to define their objectives and communicate them to donors, volunteers, beneficiaries and governments, and could represent the interests of charities when they are under attack. Government supervisory activities could be reformed to give them a mandate to assist nonprofit participants to understand and comply with their legal requirements, and to encourage high standards of corporate governance.

Coordinating Policies to Create a More Stable and Certain Environment

Nonprofit organizations cannot operate effectively without public trust. All governments have a common interest in ensuring mechanisms are in place to promote trust. Federal and provincial governments should work out a common approach to supervisory policies, perhaps through intergovernmental forums and administrative agreements.

To improve the current situation, the government could either establish a national commission or develop a cooperative approach to nonprofit supervision. For a coordinated approach to work well, it would integrate nonprofit supervision with Revenue Canada's current role. For example, some activities now carried out by Revenue Canada, including the registration of charities, could be assumed by the nonprofit commission or by a secretariat representing the federal and provincial governments.

These arrangements must complement the self-regulation occurring in the sector. Effective accountability requires that organizations adhere to high standards of governance and that their performance can be measured and assessed. These requirements cannot be mandated and enforced by governments; they ultimately depend on the will of nonprofit officers and stakeholders.

For the well-being of nonprofits, the bottom line is to improve existing laws, untangle the multijurisdictional webs of regulations, and fill gaps in the current legal treatment of the sector. The more coherent and effective legal framework resulting from these reforms will benefit organizations and increase public confidence in Canada's growing nonprofit sector.

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