



Business Law Playbooks

Part 1 – Choosing the Appropriate Business Vehicle for Your Business Idea

Prepared by the Queen's Business Law Clinic in collaboration with Queen's Partnerships and Innovation

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About Queen’s Partnerships and Innovation

Queen’s Partnerships and Innovation (“QPI”) aims to advance research, innovation, and knowledge mobilization to strengthen Queen’s local, national, and global impact. QPI provides faculty, students, post-doctoral fellows, and other members of the Queen’s community with a variety of services and resources to facilitate strategic initiatives and research partnerships. QPI is also proud to work with external organizations (both industry and not-for-profits) to connect them with expertise, resources, and incubation support.

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Why do you need a Playbook?

For many people with little or no previous business or entrepreneurial experience, understanding the relationship between law and business – and how it may affect the success or failure of their business idea – is a very important step. In this series of Playbooks, we seek to provide general information on the legal concepts that should be considered by the entrepreneur starting out their business venture.

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1 Choosing the Appropriate Business Vehicle for your Business Idea

When starting your business, one of the biggest decisions you will face is choosing an appropriate business vehicle. This decision may have a long-lasting effect on your business: how profits are shared, how much you pay in taxes, the amount of paperwork you will have to deal with each year, your personal liability as a business owner, and your ability to raise additional capital to expand your business.

Whether you plan on operating a for-profit or not-for-profit business, it is important to understand the business vehicle options available which will enable you to make an informed decision. Many start-up founders believe incorporation is the most appropriate vehicle for their business idea – just because that is the way others have done it. However, the choice of an appropriate business vehicle is business and client specific. Your individual circumstances, short and long-term business goals, business idea, and potential for growth and liability, among other factors, should be considered before choosing a business vehicle.

While there are a few considerations that every business owner should bear in mind when deciding on the appropriate business structure, the three major issues are (1) liability, (2) taxation, and (3) record-keeping. Other factors which should be considered are listed below:

- Will you be operating this business on your own or in collaboration with others?
- Will there be any potential liabilities arising from the use of your products or services?
- Who has the decision-making power –solely your responsibility, or a joint responsibility?
- Do you have sufficient initial working capital to cover the start-up costs of the business? If not, how do you plan to raise your initial working capital? Some possibilities include: contributions from family and friends, personal contributions, and grants or loans from financial institutions.
- Are you interested in keeping the start-up costs low?
- Do you need flexibility in your business structure?
- Will you be interested in exploring tax benefits for your business?
- How do you plan to distribute the profits and losses incurred by the business?
- Will you need to raise additional capital for the business in the near future?

- Will you be operating the business in Ontario only or do you foresee the opportunity to expand your business to other provinces or internationally?
- What is your long-term goal for the business – do you anticipate that your business will grow, and would you like to make room for future growth?
- Will you be able to maintain and keep up to date all records required to be kept by a corporation in compliance with regulatory requirements?
- Are you or your business partner(s) residing in Canada?
- Do you plan to operate your business to make a profit, or are you interested in setting up a not-for-profit organization?
- Will your proposed activities be carried out for the public benefit and do they fall within any of these categories – relief of poverty, advancement of education, advancement of religion, or advancement of other purposes beneficial to the community?
- If you plan to operate a not-for-profit business, how do you intend to raise funds to carry out your proposed activities? Will you accept donations and do you intend to provide tax relief to your donors?

1.1. Forms of Business Vehicles

1. Sole Proprietorship
2. Partnerships (General, Limited, and Limited Liability Partnerships)
3. Corporations – For-Profit and Not-For Profit Corporations
4. Registered Charities, Non-profit (Unincorporated) Organizations
5. Social Enterprises
6. Joint Ventures and Trusts

1.1.1. Sole Proprietorship

Are you planning to start your business on your own? If yes, you may structure your business as a sole proprietorship. A sole proprietorship is the simplest form of business vehicle. It requires no formalities to create and grants the owner of the business sole control and decision-making abilities. Sole proprietors are required to register a business name under the Ontario *Business Names Act* (“BNA”) only if the business name is different than the sole proprietor’s name. There are tax implications attached with this type of business vehicle – profits and liabilities from the sole proprietor business are deemed to be personal income of the proprietor and taxed accordingly. The owner is also personally liable for all financial obligations of the business.

1.1.2. Partnerships

Are you planning to start your business with others? If yes, a partnership arrangement may be suitable for your business. Similar to a sole proprietorship, no formal registration is necessary

when setting up a partnership. A partnership is legally created when two or more persons carry on business together in order to make profit. Unlike sole proprietorships, partnerships are governed by specific provincial legislation - in Ontario, we have the Ontario *Partnerships Act* (the “OPA”). The OPA sets out default rules which govern a partnership relationship. However, it is prudent for partners to enter into a partnership agreement. This agreement is a contract between the partners that sets out the major terms of the business relationship including: the division of revenue and partnership property, contribution share of each partner, expenses, right to make management decisions, risks and tasks for each partner, and the process of dissolving the partnership. There are also tax implications for using this business vehicle – just like a sole proprietor, partners are required to declare their share of the business’ income and expenses as their personal income and are taxed accordingly.

A partnership, also like a sole proprietorship, is required to register its business name under the BNA if the business name is not composed of the names of the partners.

1.1.3. Corporations

Are you looking for protection from liability and the ability to raise capital for your business? If so, incorporation is likely the appropriate vehicle for your business. You can incorporate under either the *Canadian Business Corporations Act* (“CBCA”) or the *Ontario Business Corporations Act* (“OBCA”). For example, Indigo Books & Music is incorporated under the OBCA while Shoppers Drug Mart is incorporated under the CBCA. The QBLC can assist you in deciding which option is best for you if you choose to incorporate.

A corporation is treated as an independent legal entity, separate from its owners. It has its own legal identity and can sue or be sued. Under its legal identity, a corporation can carry on business, buy and sell property, borrow money from various sources and incur liabilities. A corporation also owns its own assets. The corporation is managed by its directors and officers, however the ultimate control of the corporation rests in the hands of the shareholders. Shareholders own specific rights to the corporation through their ownership of shares.

A corporation also has a perpetual existence, until it is dissolved in accordance with regulatory requirements. While incorporation protects you from liability, it also means that a corporation is required to comply with more stringent regulatory and tax requirements. The drawbacks to incorporation for start-ups include higher start-up costs and annual filing obligations. The process of incorporating a company is more expensive than forming a partnership or a sole proprietorship. You will also need to obtain legal, tax, and accounting advice from professionals which increases the general costs of incorporation. A corporation can be for-profit or not-for-profit. We will discuss each form of corporation in subsequent publications.

1.1.4. Charities and Non-Profit (Unincorporated) Organizations

Registered Charities

These are charitable organizations, public foundations, and private foundations that are created and resident in Canada. Their main goal is to use their resources for charitable activities. The

Heart & Stroke Foundation, for example, is a registered charity. Their charitable purposes must fall into one or more of the following categories:

- The relief of poverty (e.g. food banks, soup kitchens, and low-cost housing units)
- The advancement of education (e.g. colleges, universities, and research institutes)
- The advancement of religion (e.g. places of worship and missionary organizations)
- Other purposes that benefit the community (e.g. animal shelters, libraries, and volunteer fire departments)

Some of the major attractions of becoming a registered charity include the ability to issue official donation receipts and enjoy income tax exemptions. You must apply to the Canada Revenue Agency (“CRA”) to obtain charitable status before becoming a registered charity. Please note however, that not all organizations operating as charities are registered charities – in other words, you can carry out charitable activities, but are not or do not qualify to be registered with the CRA as a registered charity. These unregistered charities cannot provide donors with tax receipts.

Non-Profit (Unincorporated) Organizations

Some associations, clubs, and societies provide services that are exclusively for social welfare, civic improvement, pleasure, recreation, or another purpose. So long as the services they provide do not include generating profit, such organizations are referred to as non-profit organizations. One advantage of the non-profit organization is that it may qualify as a tax-exempt non-profit organization if certain CRA requirements are met. Note that you cannot be classified as both a charity and a non-profit organization. You can only meet one definition.

1.1.5. Social Enterprises

These are organizations with both business and social goals. Their main objective is to produce goods and services sold for profit with the aim of using the proceeds of sale to further the achievement of social and environmental goals. Operating as a social enterprise allows public benefit organizations to raise funds through alternative means in order to better fulfill their organization’s mandates. It provides an opportunity for the non-profit sector to be more sustainable and less reliant on donations and grants from individuals and government sources. In 2012, Ontario established the Office for Social Enterprise (“OSE”) which focuses on supporting social enterprises in Ontario. A social enterprise can be set up in different forms including, but not limited to, a cooperative, non-profit society, civil society association or credit union. They can be structured as a for-profit or not-for profit organization.

1.1.6. Joint Ventures and Trusts

Joint Ventures

Joint ventures are short-term, project-specific, contractual relationships. This type of contract is called a joint venture agreement. The parties' obligations in a joint venture is within the agreement itself and these obligations can vary depending on the project. Joint ventures do not have any specific governing legislation. Note that the parties to the joint ventures have to comply with their respective governing legislation (e.g. *OPA, CBCA*, etc.).

Unlike partnerships, parties in a joint venture are not agents of one another, and they treat any income they earn and any expense they acquire from a project entirely separately. There is also no partnership property or jointly owned property. The assets of each party coming into the project remain the assets of that party.

Trusts

A trust company is created when a person (settlor) transfers property to another (trustee) to hold for the benefit of a specific person or a class of people (beneficiaries). This relationship allows a trustee to carry out business on behalf of the beneficiaries. A trust is not strictly a legal entity, but it is treated as one for tax purposes. A trust agreement governs the relationship between the parties involved and the rules that the trustee and the beneficiaries must follow. The trustee owes a fiduciary obligation to the beneficiaries, meaning the trustee must act in the best interest or to the benefit of the beneficiaries rather than themselves.

1.2. Quick Chart Summaries - Advantages and Disadvantages

Type of Entity	Advantages	Disadvantages
Sole Proprietorship	<ul style="list-style-type: none"> • Easy and inexpensive to set up • Regulatory burden is very light • Direct control of decision making • Enjoys tax advantages in certain scenarios • No profit/loss sharing – owner bears all the benefits and risks alone 	<ul style="list-style-type: none"> • Unlimited liability • Income from the business is taxed using the personal income tax rate • Lack of continuity – business dissolves upon the disability or death of the sole proprietor • Raising capital from traditional sources may be difficult
Partnership	<ul style="list-style-type: none"> • Fairly easy to set up – can be set up informally or upon entering into a partnership agreement • Inexpensive to set up • Start-up is quick. • Start-up costs can be split with partner(s) • Equal decision-making powers with partner(s) 	<ul style="list-style-type: none"> • All partners are jointly liable for any debts and liabilities incurred by the firm or each individual partner <ul style="list-style-type: none"> ○ Partners are “jointly and severally liable” for the actions of each partner ○ This can be mitigated by purchasing insurance which can be expensive



	<ul style="list-style-type: none"> • Equal share of profits and risks of the business • Some tax advantage in certain scenarios (e.g. partners may avoid potential tax liability by “rolling over” their assets to the partnership under s.97(2) of the <i>Income Tax Act</i>, subject to certain requirements <ul style="list-style-type: none"> ○ A rollover shifts the tax liability to the partnership instead of the contributing partner) 	<ul style="list-style-type: none"> • A person may continue to be liable for losses and debts of the partnership which were accrued when the person was still a partner even after leaving the partnership or upon their death • The partnership interest held by a partner forms part of a partner’s personal assets, thus exposing it to the personal liabilities incurred by the partner outside of the partnership
<p style="text-align: center;">Incorporation</p>	<ul style="list-style-type: none"> • Limited liability for shareholders • Ability to raise equity capital for the business • Continuous existence and transferability • Indemnification of directors • Tax benefits such as the Small Business Deduction, Lifetime Capital Gains Exemptions for Canadian-Controlled Private Corporations and the ease of estate planning 	<ul style="list-style-type: none"> • Initial costs of incorporation • Annual filing requirements • Residency requirements for directors (<i>CBCA</i>) • Dissolving a corporation is more complex than other business structures • Directors’ actions are restricted by their fiduciary duties and duty of care owed to the corporation • Disclosure requirements of directors • Potential of directors’ personal or statutory liability
<p style="text-align: center;">Registered Charities</p>	<ul style="list-style-type: none"> • Ability to issue official donation receipts to donors • Exempt from paying income tax • Eligible to receive gifts from other registered charities • Increased credibility in the community • Exempt from GST/HST and may be eligible for only a partial rebate (usually 50%) of any GST/HST paid 	<ul style="list-style-type: none"> • Costs of incorporating and the attendant annual record-keeping requirements • Must have a minimum of three directors, who must meet the definition of an eligible director under the legislation • Directors owe a measure of personal liability to the charity • Must comply with more stringent legislative and CRA reporting requirements



<p>Not-For-Profit (Unincorporated) organizations</p>	<ul style="list-style-type: none"> • Tax exemption – may pay taxes on property income or capital gains • More flexibility on the structure of the association • Fewer regulatory requirements (e.g. no minimum spending requirement, no registration process required, no annual filing requirements) 	<ul style="list-style-type: none"> • Not a separate legal entity – cannot enter into contracts under its own name; it cannot sue or be sued, it cannot hold property • Not governed by any statute • No limited liability – Members are personally liable for the acts and liabilities of the association
<p>Social Enterprise</p>	<ul style="list-style-type: none"> • Easy to raise capital – from goods and services, access to grants • Easier to garner support from the public • Flexible business structure – could be a for-profit corporation or a not-for-profit corporation 	<ul style="list-style-type: none"> • In Canada, only a Community Contribution Company (“CCC”) in British Columbia or a Community Interest Company (“CIC”) in Nova Scotia can be formed specifically for social enterprise • No special tax treatments
<p>Joint Ventures</p>	<ul style="list-style-type: none"> • Project specific • Regulatory burden is generally light • Parties' rules are flexible • Minimal working capital required for start-up • Not formed by implication • No income or property sharing 	<ul style="list-style-type: none"> • Limited outside opportunities • Lack of continuity for your business once your project comes to an end • Uneven division of work • Can be difficult to raise capital on your own
<p>Trusts</p>	<ul style="list-style-type: none"> • Allows a settlor to direct the allocation and use of assets without needing to directly manage or oversee the assets 	<ul style="list-style-type: none"> • Is only a legal entity for tax purposes



	Start-up costs	Regulatory burden	Individual control of decision making	Tax benefits	Individual share of income	Exposure to liability	Ability to raise capital	Continuous existence	Legal duties
Trust	X	X	X	X	n/a	X	n/a	X	X
Joint Venture	X	X	X	X	X	X	X	n/a	n/a
Social Enterprise	X	X	X	X	n/a	X	X	X	X
Not-For-Profit Organizations	X	X	X	X	n/a	X	X	X	X
Registered Charity	X	X	X	X	n/a	X	X	X	X
Incorporation	X	X	X	X	X	X	X	X	X
Partnership	X	X	X	X	X	X	X	X	n/a
Sole Proprietor	X	X	X	X	X	X	X	n/a	n/a

Legend:

X = Low

X = Medium

X = High



1.3. Conclusion

Ensure that you take the time to consult with legal, accounting, and tax professionals before making a decision on the appropriate business structure for your business. Choosing the optimal organizational structure that best enables your objectives and goals will save you a whole lot of time, energy, and money which you can instead spend on growing your business idea.



Business Law Playbooks

Part 2 – Sole Proprietorships

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2 Sole Proprietorships

2.1. How is a Sole Proprietorship Formed?

A sole proprietorship is an unincorporated business formed by an individual who has chosen to produce goods or offer services to the general public, in exchange for money, and with a view to make a profit. There are no formalities involved in the creation of a sole proprietorship, making it one of the easiest and simplest forms of carrying on business in Ontario and Canada. All that is required of the business owner is to register a trade name, obtain a tax number, and open a bank account. Many small businesses are faced with the decision of whether to incorporate at the outset, or whether to start operations as a sole proprietorship or a partnership and incorporate later. Unlike partnerships and corporations, which are governed by specific legislations pertaining to the business structure, sole proprietorships are not. We will be examining some of the factors to be considered when making that decision in this Playbook.

2.2. Features of a Sole Proprietorship

A sole proprietorship is, by nature, informal. It is the easiest and least expensive form of business to set up and operate. You may choose to carry on business as a sole proprietor under your personal name or register a business name. Unlike a partnership or corporation, there is no distinction between the business and its owner in a sole proprietorship. This means that the owner is personally responsible for any debts or liabilities incurred by the business and retains all profits made by the business. You own 100% of your business and have all the decision-making powers. You are basically the master of your own ship. Your tax obligations are relatively simple – no separate business tax return is required to be filed with the Canada Revenue Agency (“CRA”), as all income generated from the business is reported on your personal tax returns. This also means that you are able to deduct all expenses relating to the business from your personal income. For a start-up business that is losing money in the early years, this option of deducting business losses can help reduce the tax payable. Some expenses that may qualify as business expenses include travel expenses, advertising, and the cost of equipment. If your business is home-based, additional costs like a portion of your rent or mortgage payments, phone, internet and utility bills could also be deducted on your taxes.

Examples of businesses that can start operations as a sole proprietorship include landscaping, catering, accounting/tax preparation, legal, computer/IT, graphic design, event planning photography and consulting services, along with fitness instructors, motivational speakers and manufacturers. Please note that some of these activities may have additional statutory or regulatory requirements or may be better suited for another business structure depending on the potential liability that may flow from its operations. The QBLC recommends that you seek legal counsel before beginning a business.

2.3. Sole Proprietorship vs Partnership

Partnerships and sole proprietorships share many commonalities, as a partnership is essentially a sole proprietorship with multiple proprietors. A partnership is a relationship between two or more people carrying on a business together with a view to profit. This is very similar to the

definition of a sole proprietorship. Both are business structures that are without legal personality, and the use of a name other than the names of the partners must be registered in accordance with the *Business Names Act* (“BNA”). Any gains or losses “flow through” the partnership and are represented on the partner’s personal income tax. The differences between the two business vehicles are the result of having multiple proprietors and the relationship between them. A sole proprietorship, as a single person, does not have to concern themselves with any other party’s actions. For more information about the partnership business structure, please refer to the “Partnerships” Playbook.

2.4. Sole Proprietorship vs Incorporation

Unlike sole proprietorships and partnerships, incorporation is a highly formal process. The process of incorporation (literally meaning “to give a body”) creates a new legal person. The fact that a corporation has its own legal personality comes with many implications for your business. As a legal person, a corporation can own its own property, retain its earnings, and enter contracts in its own name. Most importantly, it creates a separation between the business and its shareholders. Shareholders have no direct claim to any of the business’ property or earnings, but also are not liable for any of the business’ liabilities. For example, if a corporation takes on a loan but goes bankrupt, the shareholders cannot be compelled to pay the outstanding balance on the loan.

Unlike a corporation, with its separate legal entity and perpetual existence, a sole proprietorship is no more than the person. This means the business cannot be transferred, and if the sole proprietor dies, so does the business. The founders of a corporation can pass away, and the corporation itself remains fully functional and able to conduct business. Meanwhile, shares of a corporation can be transferred like property, subject to any transfer restrictions that might be attached to the shares.

While sole proprietorships have no setup and maintenance requirements, corporations have a variety of requirements they need to fulfil. There is a fee to incorporating, and annual returns are required by the government. There are ongoing statutory obligations, like annual shareholder meeting and maintaining a corporate minute book. If the corporation continues to grow and attract investors, securities legislation and disclosure obligations may become important.

While the business’ profits or losses are claimed on the sole proprietor’s personal taxes, corporations file taxes on their own behalf, paying the corporate income tax rate. Corporations also distribute their profits as dividends, which are then taxed as the recipients of the income. This is sometimes referred to as “double taxation”.

Lastly, it may be difficult to secure financing from a bank to fund a sole proprietorship because any debt borrowed will be considered as a personal loan. On the other hand, corporations can raise capital through equity financing. Equity financing is the issuance of shares in the corporation for money or other capital. Unlike debt financing, equity financing doesn’t need to be repaid, but instead grants the shareholders some control over the corporation.

2.5. Operating Under Your Own Name as a Sole Proprietorship

If you operate under your own full, legal name, you are not required to register a name in Ontario, nor are you bound by any of the regulations in the *BNA*.

2.6. Registering a Business Name as a Sole Proprietorship in Ontario

Operating a sole proprietorship in any name that is not your own requires a registration of the business name. In Ontario, the rules for naming a business are governed by the *BNA*. The registration of a business name requires a registry search to ensure that no other names are similar to your proposed name. After registration, names in Ontario must also be renewed every five years. Each step of this process has an associated fee.

2.7. Trademarks Considerations

Before selecting a name for your sole proprietorship, or any other business vehicle, consider your ability to trademark your name. A trademark is a way for the public to identify that the goods or services being provided are from a certain party. Considering trademarks early in the business process goes a long way in protecting your business' reputation, as well as protecting against potential trademark infringement claims.

Trademarks include words, names, logos, designs or other traits like a certain colour that distinguishes the goods or services of that person from any other similar goods or services. These trademarks can be registered or unregistered. Registered trademarks are governed by the *Trade-marks Act* and are maintained by the Canadian Intellectual Property Office.

Unregistered trademarks are those that are protected at common law, and are protected by the tort (civil wrong) of "passing off". The claimant for an infringement of an unregistered trademark can show their name is associated with a set of products and a reputation within a certain geographical area, and if your name is found to be infringing on an unregistered trademark, you may be forced to change your name or be prohibited from conducting business in a certain geographical region.

The test for trademark infringement is whether a reasonable consumer, acting in a bit of a hurry, would mistake a good or service as being provided by another party. We recommend conducting a search of registered and unregistered trademarks before deciding on a business name. The QBLC can assist you in drafting an opinion on the eligibility for your name and logo for its ability to be filed as a registered trademark.

2.8. Steps to Set Up a Sole Proprietorship

2.8.1. Step 1: Decide on a Business Structure

Decide on the appropriate business structure – get legal and accounting advice from experts

2.8.2. Step 2: Choose a Business Name

Decide whether to use your personal name or choose a business name. If choosing a business name, you must register under the *BNA*. You must conduct a search through the [Ontario Business](#)

[Registry](#) to find out whether your proposed name is available. The cost to conduct a search may vary depending on the type of search records requested. Please contact the QBLC for assistance if you seek to conduct a name search for your sole proprietorship.

If your chosen name is available, register your business name in Ontario. You must register a business name if your chosen business name is different from your full name. Business name registration is effective for 5 years, after which you must renew it. The cost of registration of your business name might vary depending on your method of filing. Payment can be made online using a Visa or MasterCard, by mailing a cheque or money order to the Minister of Finance or by cash. Please contact the QBLC if you are seeking help in registering a business name in Ontario.

2.8.3. Step 3: Receive a Master Business Licence

If you registered a name, you should expect to receive your Master Business Licence by mail within 20 business days.

2.8.4. Step 4: Protect Your Intellectual Property

Protect your trademark. Register your trademark and purchase a domain using your preferred business name. Even if you are not yet ready to build your website, you will save yourself some trouble by reserving your domain name so that it is not taken up by another entity before you are ready to use it. The QBLC offers its clients trademarks advice by assisting them in conducting detailed trademark searches and providing them with a legal opinion on the availability of their proposed trademarks for registration in Canada.

2.9. Conclusion

There are good reasons to operate your business as a sole proprietorship. There are no formalities before getting started and you have absolute control over the business. However, there are also drawbacks like unlimited personal liability.

Choosing the optimal business vehicle from the outset will save you time, money, and energy which you can put towards growing your business instead. Make sure you consult legal, accounting, and tax professionals before you decide on the appropriate business structure.



Business Law Playbooks

Part 3 – Partnerships: General, Limited, and Limited Liability Partnerships

Prepared by the Queen's Business Law Clinic in collaboration with Queen's Partnerships and Innovation

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3 Partnerships: General, Limited, and Limited Liability Partnerships

3.1. How is a Partnership Formed?

Partnerships are a relationship between two or more persons carrying on a business with a view to profit. Partnerships can arise explicitly (with a partnership agreement) or implicitly (by fulfilling the definition of a partnership above). In Ontario, partnerships are governed by the *Partnerships Act* (“PA”). In general, receiving a share of the profits in the business, without evidence to the contrary, will serve as proof that the person is a partner on the business. Partners need not exert any control over the business to be considered a partner. Partners exerting control over a partnership’s operations are known as general partners, while partners who are not interested in the control or management of the partnership are known as silent partners. A general discussion of these two categories of partners is set out below.

Lastly, partners need only be legal persons, not natural persons. Thus, a partnership may be created by two unrelated corporations, natural persons, or a combination of natural persons and corporations.

3.2. Features of a Partnership

There are some distinctive features of a Partnership:

3.2.1. Agency

The most important feature is the creation of an agency relationship between partners. Partners are agents of each other partner in all matters relating to the business. Each partner can bind their partners without their knowledge or consent to contracts, imposing obligations on them unilaterally.

3.2.2. No Separate Legal Personality

Like a sole proprietorship, partnerships have no separate legal personality. This means the partnership cannot hold its own property, enter into any contracts, sue, or be sued. Actions that require legal personality must be done by a partner personally on behalf of the partnership.

3.2.3. Profit Sharing and Income Tax Benefits

Partners can only be paid by the distribution of the business’ profits. This means a partner cannot be an employee of the business and partners are unable to seek any statutory protections that an employee may have. Also, like sole proprietorships, all profits and losses that occur in a partnership will “flow through” the partnership and are reported on the partner’s personal income taxes, allowing partners to use business losses to offset income from other sources.

3.2.4. Liability of a Partner

Partners are personally liable for the debts of the partnership, so a creditor can pursue a claim against any partner personally if a loan defaults. Partners are also “jointly liable”, which means that any obligation assumed by one partner can be enforced against all other partners. Partners are “severally liable”, as partners are equally individually responsible for the partnership’s losses, unless otherwise agreed to in the partnership agreement.

3.2.5. Governing Law

Without a partnership agreement, the relationship between all the partners is governed by the *PA*. The *PA*’s default provisions put forth a few factors: equality, consensualism, and fiduciary duties. Thus, without an agreement modifying the default provisions, all partners share equally in the profits and losses, can all take part in managing the business, and make decisions based on a consensus. Additionally, partners cannot enter and exit the partnership freely. A partner entering or exiting the partnership will be deemed a new partnership, with the old one dissolved.

Partnerships can conduct business under the names of the partners. If the partners decide they would like to use a different name, the name must be registered in compliance with the *Business Names Act* (“*BNA*”).

3.3. The Partnership Agreement

As noted above, partnerships can exist with or without a partnership agreement. The partnership agreement has several main functions: it provides certainty that a partnership exists, and it allows partners to modify many of the default obligations from the *PA*.

With a partnership agreement, many of the obligations between the partners can be renegotiated by the partners to suit their preferences with the main exception of the fiduciary duty owed to each other. For example, partnership agreements can allow for decisions to be made by a simple or super majority instead of by consensus, alter the contributions each partner makes to the partnership and how profit and losses are split between partners, or allow for the addition and expulsion of partners. The last is an example of a power that can only be granted with a partnership agreement.

A partnership agreement strictly governs the relationship between partners and not the partnership’s relationship with third parties. While a partnership agreement may split the losses of the partnership in the manner agreed upon by the partners, a third party seeking to recover its debt from the partnership or from one of the partners enjoys the benefit of the principle of joint liability. This means that if a partnership owes money to a third party, that third party can choose to go after one or all the partners personally to recover his money.

The QBLC can assist you in drafting a partnership agreement and help you tailor the rules of partnership to your specific circumstances.

3.4. Partnerships vs Sole Proprietorships

Sole proprietorships and partnerships are very similar in nature, as neither business structure has a separate legal personality. The differences between a sole proprietorship and a partnership are minimal, besides the differences arising from having multiple parties. The decision of partnership or a sole proprietorship is made automatically by the amount of people managing the business.

Characteristics	Partnerships	Sole Proprietorships
Formation	<ul style="list-style-type: none"> Partnerships are formed when persons carry on a business in common with a view to profit, or if they sign a partnership agreement 	<ul style="list-style-type: none"> Sole proprietorships are formed when an individual carries on business
Lifetime	<ul style="list-style-type: none"> Unless provided otherwise in the partnership agreement, a partnership is dissolved when the business in common is concluded, a partner dies or is disabled, or by agreement of the partners 	<ul style="list-style-type: none"> Sole proprietorships end when the sole proprietor dies or is disabled
Ownership Structure	<ul style="list-style-type: none"> Two or more legal persons – partners can be individuals or corporations 	<ul style="list-style-type: none"> Operated by a single individual
Business Name Registration Requirements	<ul style="list-style-type: none"> If operating under the partners' full names, no business name registration is necessary If operating under any other business name, the name must be registered in compliance with the <i>BNA</i> 	<ul style="list-style-type: none"> If operating under the sole proprietor's full name, no business name registration is necessary If operating under any other business name, the name must be registered in compliance with the <i>BNA</i>
Separate Legal Personhood	<ul style="list-style-type: none"> The business is not legally distinct from the partners – contracts must be signed in the partners' names 	<ul style="list-style-type: none"> The business is not legally distinct from the business owner – contracts must be signed in the sole proprietor's name
Liability	<ul style="list-style-type: none"> Partners have unlimited joint and several liability for the debts of the partnership – each partner is personally 	<ul style="list-style-type: none"> A sole proprietor has unlimited personal liability for the debts of the business



	liable for the obligations of the other partners within the partnership	
Employees	<ul style="list-style-type: none"> The partnership can hire employees, but the partners cannot be employees themselves 	<ul style="list-style-type: none"> The sole proprietorship can hire employees, but the owner cannot be an employee themselves
Taxes	<ul style="list-style-type: none"> Income from the partnership “flows through” to the partners as business income Profit is shared either equally between partners, or in accordance with the partnership agreement 	<ul style="list-style-type: none"> Income from the sole proprietorship “flows through” to the sole proprietor as business income
Governing Law	<ul style="list-style-type: none"> Partnerships are governed by the <i>PA</i> and must comply with the <i>BNA</i> 	<ul style="list-style-type: none"> Sole Proprietorships must comply with the <i>BNA</i>

3.5. Partnerships vs Incorporation

Unlike a partnership, a corporation is a highly formal business structure. It is impossible for a corporation to be created inadvertently. The process of incorporation (literally meaning “to give a body”) creates a new legal person. The existence of legal personality for a corporation brings with it a higher sense of responsibility as there are regulatory requirements that the corporation must comply with. As a legal person, a corporation can own its own property and can enter into contracts in its own name. Most importantly, legal personality creates a separation between the business and its shareholders. Shareholders have no direct claim to any of the business’ property or earnings, but are also not liable for any of the business’ liabilities. For example, if a corporation takes on a loan but goes bankrupt, the shareholders cannot be compelled to pay the outstanding balance on the loan, provided there was no fraudulent behaviour involved.

While partnerships have minimal maintenance requirements (an accounting of the business and allocating its profits and losses), corporations have a variety of requirements they need to fulfil. There is a fee to incorporate, and annual returns are required by the government. There is also management overhead, like holding annual shareholder meetings and having to maintain a corporate minute book.

As a separate legal entity, corporations also have perpetual existence. Because a partnership is made up of individual partners with no legal personality, a partnership ceases to exist upon the death of a partner (unless partners agree otherwise in a partnership agreement). The founders

of a corporation can pass away, and the corporation itself remains fully functional and continues to conduct its business. Transferring an interest in a corporation is also different, as shares can be exchanged while a partner can only transfer his/her partnership interest in the business. This partnership interest represents their share of profits and losses, voting rights and managerial responsibilities (if any). A partner cannot delegate or assign any portion of their other rights, including the right to take part in the management of the business.

While the business' profits or losses are claimed on the partner's personal taxes, corporations file taxes on their own behalf. Corporations instead distribute their profits as dividends, which are then taxed as the recipients of the income.

Lastly, corporations can utilize "equity financing" instead of borrowing money from a lender (debt financing). Equity financing is the issuance of shares in the corporation for money. Unlike debt financing, equity financing need not be repaid, but instead grants shareholders a degree of control over the corporation. Conversely, any debt borrowed by a partnership will be considered a personal loan of the partners individually and collectively.

Characteristics	Partnerships	Corporations
Formation	<ul style="list-style-type: none"> Partnerships are formed when persons carry on a business in common with a view to profit, or if they sign a partnership agreement 	<ul style="list-style-type: none"> Corporations are formed by filing articles of incorporation with the appropriate governing body
Lifetime	<ul style="list-style-type: none"> Unless provided otherwise in the partnership agreement, a partnership is dissolved when the business in common is concluded, a partner dies or is disabled, or by agreement of the partners 	<ul style="list-style-type: none"> Corporations have an unlimited lifetime
Ownership Structure	<ul style="list-style-type: none"> Two or more legal persons – partners can be individuals or corporations 	<ul style="list-style-type: none"> Subject to any limitations in the articles of incorporation, corporations can have unlimited owners/shareholders – shareholders can be individuals or corporations
Business Name Registration Requirements	<ul style="list-style-type: none"> If operating under the partners' full names, no business name registration is necessary 	<ul style="list-style-type: none"> A NUANS search report is required during the incorporation process and ensures the business name



	<ul style="list-style-type: none"> If operating under any other business name, the name must be registered in compliance with the <i>BNA</i> 	<ul style="list-style-type: none"> The corporation's name must indicate its status as a separate legal person and comply with the requirements in the Act under which it incorporated
Separate Legal Personhood	<ul style="list-style-type: none"> The business is not legally distinct from the partners – contracts must be signed in the partners' names 	<ul style="list-style-type: none"> A corporation is legally distinct from its shareholders and directors – a corporation can sign contracts and own property
Liability	<ul style="list-style-type: none"> Partners have unlimited joint and several liability for the debts of the partnership – each partner is personally liable for the obligations of the other partners within the partnership 	<ul style="list-style-type: none"> Absent some circumstances involving fraudulent, illegal or improper purpose, shareholder and directors are not liable
Employees	<ul style="list-style-type: none"> The partnership can hire employees, but the partners cannot be employees themselves 	<ul style="list-style-type: none"> An individual can be a shareholder, a director, and an employee simultaneously
Taxes	<ul style="list-style-type: none"> Income from the partnership "flows through" to the partners as business income Profit is shared either equally between partners, or in accordance with the partnership agreement 	<ul style="list-style-type: none"> Corporations are taxed separately from shareholders on any income they earn Income can be distributed to shareholders through dividends, and shareholders will be taxed on the receipt of those dividends
Governing Law	<ul style="list-style-type: none"> Partnerships are governed by the <i>PA</i> and must comply with the <i>BNA</i> 	<ul style="list-style-type: none"> Corporations are governed by the Act under which they were created. For example, federally incorporated businesses are governed by the <i>Canada Business Corporations Act</i>

3.6. Limited Partnerships

Limited partnerships are related to partnerships but allow for passive investment. Limited partnerships consist of one or more “general partner(s)” and one or more “limited partner(s)”. In Ontario, Limited Partnerships are governed by a different legislative act, the *Limited Partnerships Act* (“LPA”). Unlike a partnership, limited partnerships must be registered in accordance with the LPA and will never arise inadvertently.

The general partner in a limited partnership is very similar to the general partner of a partnership. They remain liable for all the debts and obligations of the partnership, without limit. However, limited partnerships are “limited” in the sense that their liability for any debts of the partnership is capped at their investment in the corporation. For example, if you invest \$1,000 in a partnership, you will only have to pay \$1,000 if creditors demand payments from the partnership. In exchange for this limitation of liability, limited partners cannot take part in the management of the business. A limited partner may contribute money and other assets to the limited partnership, but cannot offer services. Where the limited partner actively manages the affairs of the business, the limited partner will lose the benefit of limited liability. One other difference between the two types of partners is that a limited partner can be an employee of the business (and enjoy the benefits of employee protections), while general partners cannot.

As limited partnerships must be registered before coming into existence, part of the registration includes a partnership name. Therefore, limited partnerships are exempt from the business name registration requirements of the *BNA*. Lastly, limited partnerships lapse every five years, and must be renewed. This form of business vehicle can be attractive when you are looking to have partners who are not interested in the management of the business, or when employees wish to invest into a partnership.

3.7. Limited Liability Partnerships

Limited liability partnerships (“LLPs”) are a special subset of partnerships, which have features of a corporation and a partnership. Despite the name, limited liability partnerships are not a subset of limited partnerships. In Ontario, limited liability partnerships are governed by the *PA*. Limited liability partnerships are intended to be a way for professionals to pool their resources, while not being liable for another partners’ professional negligence. Corporations are not normally available to the professions to prevent a professional from limiting their liability, hence the creation of limited liability partnerships. Partners in a limited liability partnership are still generally liable for all business obligations of the partnership but would not be liable for one partner’s tortious acts in carrying out their practice.

Limited liability partnerships offer many benefits over general partnerships. However, the ability to create a limited liability partnership is heavily restricted in Ontario. The *PA* limits this type of business vehicle to professions where the act governing the profession explicitly allows the formation of a limited liability partnership. Thus, limited liability partnerships are mostly limited to lawyers, accountants and medical professionals.



Characteristics	Partnerships	Limited Partnerships	Limited Liability Partnerships
Formation	<ul style="list-style-type: none"> Partnerships are formed when persons carry on a business in common with a view to profit, or if they sign a partnership agreement 	<ul style="list-style-type: none"> Limited Partnerships cannot be formed inadvertently and are formed by registering in accordance with the <i>LPA</i> 	<ul style="list-style-type: none"> Limited Liability Partnerships are a type of partnership that is formed by registering under the <i>Partnership Act</i> Limited Liability Partnerships can only be formed by professionals such as lawyers, accountants and medical professionals
Lifetime	<ul style="list-style-type: none"> Unless provided otherwise in the partnership agreement, a partnership is dissolved when the business in common is concluded, a partner dies or is disabled, or by agreement of the partners 	<ul style="list-style-type: none"> Registration of a limited partnership lapses every five years and must be renewed 	<ul style="list-style-type: none"> Registration of a limited liability partnership lapses every five years and must be renewed
Ownership Structure	<ul style="list-style-type: none"> Two or more legal persons – partners can be individuals or corporations 	<ul style="list-style-type: none"> Two or more legal persons – partners can be individuals or corporations General partners manage the business, while limited partners contribute 	<ul style="list-style-type: none"> Two or more legal persons – partners must be individuals



		financially but do not take part in the management of the partnership	
Business Name Registration Requirements	<ul style="list-style-type: none"> If operating under the partners' full names, no business name registration is necessary If operating under any other business name, the name must be registered in compliance with the <i>BNA</i> 	<ul style="list-style-type: none"> A limited partnership's business name is registered during the registration under the <i>LPA</i> 	<ul style="list-style-type: none"> The partnership's name must be registered in compliance with the <i>BNA</i>
Separate Legal Personhood	<ul style="list-style-type: none"> The business is not legally distinct from the partners – contracts must be signed in the partners' names 	<ul style="list-style-type: none"> The business is not legally distinct from the partners – contracts must be signed in the partners' names 	<ul style="list-style-type: none"> The business is not legally distinct from the partners – contracts must be signed in the partners' names
Liability	<ul style="list-style-type: none"> Partners have unlimited joint and several liability for the debts of the partnership – each partner is personally liable for the obligations of the other partners within the partnership 	<ul style="list-style-type: none"> General partners have unlimited joint and several liability for the debts of the partnership, while limited partners have limited liability up to the amount they invested into the partnership If a limited partner takes part in the management of the partnership, they will lose their limited liability 	<ul style="list-style-type: none"> In Ontario, partners are not liable for claims made against other partners in the partnerships, whether those are contractual claims or negligence claims Partners still have unlimited personal liability for their own wrongful acts



Employees	<ul style="list-style-type: none"> The partnership can hire employees, but the partners cannot be employees themselves 	<ul style="list-style-type: none"> The partnership can hire employees, but the partners cannot be employees themselves 	<ul style="list-style-type: none"> The partnership can hire employees, but the partners cannot be employees themselves
Taxes	<ul style="list-style-type: none"> Income from the partnership “flows through” to the partners as business income Profit is shared either equally between partners, or in accordance with the partnership agreement 	<ul style="list-style-type: none"> Income from the partnership “flows through” to the partners as business income Profit is shared in accordance with the limited partnership agreement 	<ul style="list-style-type: none"> Income from the partnership “flows through” to the partners as business income Each partner is taxed on their own income earned within the partnership
Governing Law	<ul style="list-style-type: none"> Partnerships are governed by the <i>PA</i> and must comply with the <i>BNA</i> 	<ul style="list-style-type: none"> Limited Partnerships are governed by the <i>LPA</i> 	<ul style="list-style-type: none"> Partnerships are governed by the <i>PA</i> and must comply with the <i>BNA</i>

3.8. Quick Chart Summary - Advantages and Disadvantages

Type of Entity	Advantages	Disadvantages
Sole Proprietorship	<ul style="list-style-type: none"> Easy and inexpensive to set up Regulatory burden is very light Direct control of decision making Enjoys tax advantages in certain scenarios No profit/loss sharing – owner bears all the benefits and risks alone 	<ul style="list-style-type: none"> Unlimited personal liability Income from the business is taxed using the personal income tax rate Lack of continuity – business dissolves upon the disability or death of the sole proprietor Raising capital from traditional sources may be difficult
Corporation	<ul style="list-style-type: none"> Limited liability for shareholders 	<ul style="list-style-type: none"> Initial cost of incorporation Annual filing requirements



	<ul style="list-style-type: none"> • Ability to raise equity capital for the business • Continuous existence and transferability • Indemnification of directors • Tax benefits such as the Small Business Deduction, Lifetime Capital Gains Exemptions for Canadian-Controlled Private Corporations and the ease of estate planning 	<ul style="list-style-type: none"> • Residency requirements for directors • Dissolving a corporation is more complex than other business structures • Fiduciary duties owed by directors • Disclosure requirements of directors • Duty of care owed by directors • Potential of directors' personal or statutory liability
<p>General Partnership</p>	<ul style="list-style-type: none"> • Fairly easy to set up – can be set up informally or upon entering into a partnership agreement • Start-up costs can be split between partner(s) • Some tax advantages in certain scenarios (e.g. partnerships may avoid potential tax liability by “rolling over” their assets to the partnership, which shifts the tax liability to the partnership instead of the contributing partner • A partnership agreement gives you flexibility to deviate from many default rules and create your own rules 	<ul style="list-style-type: none"> • Potential uncertainty as it may arise inadvertently • Partners are subject to unlimited personal liability • The partnership has no legal personality, a partner is always acting on behalf of himself/herself • Partners are jointly and severally liable for the actions of each partner • A person may continue to be liable for losses and debts of the partnership after leaving the partnership or upon their death, which were acquired when the person was still a partner • Partner cannot be an employee of the partnership
<p>Limited Partnership</p>	<ul style="list-style-type: none"> • Partners can invest without exposing themselves to unlimited liability • Partnership does not need to register under the <i>BNA</i> • Clear when it exists, limited partnerships will never arise inadvertently • Limited partners can be employees of the partnership 	<ul style="list-style-type: none"> • Must be registered as a limited partnership, and renewed every five years • Limited partners may inadvertently take control and be liable as general partners • You cannot contribute services to the business as a limited partner • Often requires a limited partnership agreement to avoid ambiguities



	<ul style="list-style-type: none">• No burden of managing the business because general partners has control	
Limited Liability Partnership	<ul style="list-style-type: none">• Partners are not liable for any professional wrongs of the other partners• Not liable for any other debt or obligations of the LLP	<ul style="list-style-type: none">• Limited to select professions• Partners are still jointly liable for all the obligations of the partnership as a whole

3.9. Conclusion

Like a sole proprietorship, partnership is relatively easy and inexpensive to form as the start-up cost is relatively low. However, partnerships might be formed inadvertently if the relationship is one where two or more persons carrying on a business with a view to profit. Unlike a sole proprietorship, there are governing legislations for partnerships. Therefore, having a partnership agreement in place is not only beneficial for clearly outlining the partners' duties and obligations, but it also allows you to tailor the business relationship to reflect your needs.

Whether you are looking to start a partnership with others or you are looking to join a partnership, it is important that you understand the benefits and drawbacks of a general partnership, a limited partnership, and a limited liability partnership. This part of the Playbook offers an overview of the three. Should you require additional legal advice specific to your situation, the QBLC will be happy to assist you.



Business Law Playbooks

Part 4 – Incorporating a For-Profit Corporation

Prepared by the Queen's Business Law Clinic in collaboration with Queen's Partnerships and Innovation

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4 Incorporating a For-Profit Corporation

For the purposes of this Playbook, we will only be discussing the “for-profit” version of a corporation, but the vehicle is available for other business models. Other forms of corporations will have their own unique challenges. For other forms of corporations, please refer to the corresponding Playbook for non-profit or charitable corporations.

4.1. Features of a Corporation

Corporations have six key features that distinguish the business vehicle from all others. These are:

1. Separate Legal Personality
2. Perpetual Existence
3. Limited Liability for Shareholders
4. Transferability of Shares
5. Ability to Centralize Management
6. Shareholder Control over Management.

Each of these features comes with its own implications.

4.1.1. Separate Legal Personality

One of the most important notions of incorporation is that corporations have all the legal rights of a natural person. This means that corporations are free to enter into contracts using their own name, borrow money on their own credit, own property, and declare bankruptcy, along with suing and being sued in their own capacity.

4.1.2. Perpetual Existence

The longest-running businesses are generally corporations for a reason. As they are their own legal person, the existence of a corporation is not tied to any one person's natural life. Though the founders and shareholders of a corporation may pass away, the corporation itself remains able to conduct its own business affairs through its directors and officers. Corporations only cease to exist when they fail to comply with their governing legislation, or when the decision is made to dissolve the corporation.

4.1.3. Limited Liability

The most attractive feature of incorporation is the limitation of liability for shareholders. As the corporation is a legal entity in and of itself, the corporation bears the ultimate responsibility for any liabilities it incurs, whether voluntarily (through contracts) or involuntarily (through tortious conduct). If for any reason the corporation is unable to meet its obligations with the assets and equity it owns, the shareholders cannot be sued for any outstanding balances. That being said,

there are specific circumstances where the shareholders can be held liable for debts of the corporation; for example, when the corporation is being used as an engine for fraud.

4.1.4. *Transferability of Shares*

Unless otherwise stated by the corporation, the shares of a corporation are transferrable. This allows for the creation of both “private” and “public” corporations. Private corporations are those where the ability to transfer shares is restricted, while the shares of a public corporation can be purchased by anyone. The shares of public corporations are normally listed on stock exchanges, like the Toronto Stock Exchange or the New York Stock Exchange. While the availability and transferability of shares make corporations an attractive business vehicle, in addition to the legislation that governs the incorporation of a company, the issuance of shares is governed by securities legislation. Unless a corporation issues shares through an exemption, the company will become a Reporting Issuer and be required to file a prospectus which is a very onerous and expensive undertaking.

Due to the transferability of shares, corporations also gain a unique ability different from all other business vehicles. This is the ability to perform what is known as “equity financing”, which is the raising of money through the offering of new shares. The converse to this is “debt financing”, where money is borrowed and repaid over time with interest.

4.1.5. *Ability to Centralize Management*

Due to the ability to disperse shares over a vast number of owners in the case of public companies, the ability to centralize management is crucial. Hence, corporations are run by the board of directors. The board of directors manage the direction of the corporation and are ultimately responsible for the decisions of the corporation. These directors can appoint officers to manage the day-to-day operations of the corporation.

4.1.6. *Shareholder Control over Management*

While shareholders do not exert direct control over the corporation, they can exert their influence in multiple ways. Chief among these is that the election of directors is done by the shareholders. Additionally, shareholders are entitled to vote on certain fundamental matters, and if enough shareholders support a decision, the board of directors can be compelled to implement that decision.

4.2. The Incorporation Process

The incorporation process is highly formalized, and many factors must be considered. It is best for you to consult with a legal professional to ensure that you set up a corporation that meets your needs. The following steps are among some of the considerations when incorporating a business.

4.2.1. *Step 1: Choose a Jurisdiction*

The process of incorporation starts with deciding on where you would like to incorporate. In Canada, businesses have the option of incorporating federally, provincially, or territorially. Each

province and territory has its own governing legislation, while federally incorporated companies are governed by the *Canada Business Corporations Act* (“CBCA”). For the purposes of this Playbook, we will only be discussing incorporation under the CBCA and the *Ontario Business Corporations Act* (“OBCA”).

A business only incorporates once. However, if you decide to incorporate federally, you must also register provincially or territorially depending on where you plan to conduct your business. For example, if you are an Ontario-based business that decided to incorporate federally, you must also register your business with the province of Ontario. In general, incorporating provincially does not bar your corporation from conducting business in the rest of Canada.

Incorporating federally gives some advantages, like Canada-wide name protection, the perceived value of a “Canadian” corporation, and a cheaper incorporation fee. However, ongoing management fees for federal corporations, like the fee to file the corporation’s annual return, are slightly higher.

On the other hand, a provincial corporation has some advantages as well, including a reduced amount of annual reporting obligations and its corresponding costs, as well as a lower hurdle when it comes to securing a unique name in the province. Some disadvantages include a higher upfront cost for incorporation, no Canada-wide name protection, and the perception of being a less prestigious entity compared to a “Canadian” corporation.

4.2.2. Step 2: Choose a Name

A corporation may choose to use a numbered name (e.g. 123456 Canada Inc.), or may opt to use a worded name. If you opt for a worded name, a name search will also have to be conducted to ensure that the name is not already taken. Regardless of whether the name is a number or word, a legal suffix must be attached to the name, like “Inc.,” “Ltd.” or “Corp.” The legal suffix is required to place the world on notice that the organization is a corporation, and the shareholders are not personally liable for the actions of the corporation. All contracts that a corporation enters must be under its formal name. However, like sole proprietorships and partnerships, a corporation can carry on business in Ontario under a different name if it registers under the *Business Names Act* (“BNA”).

4.2.3. Step 3: Prepare and File Your Incorporation Documents

Regardless of your decision to incorporate federally or provincially, two documents need to be filed; (1) the Articles of Incorporation and (2) the Notice of Initial Registered Office and First Board of Directors.

The articles of incorporation dictate the core structure of your corporation. This document will contain the share classes and their attached rights (more on that later), the corporation’s head office, the minimum and maximum number of directors, the powers granted to the directors, as well as any restrictions on the kinds of business the corporation can conduct. The Notice of Initial Registered Office and First Board of Directors is required to indicate the location of the

corporation (i.e. where corporate documents will be delivered), and to indicate the first director(s) to serve on the board.

Once you have successfully filed for incorporation, either Corporations Canada or Service Ontario (depending whether you incorporated federally or provincially) will send you a certificate of incorporation along with some other important information regarding your new corporation.

4.2.4. Step 4: Post-Incorporation Steps

After incorporating, there are several post-incorporation steps for the corporation to take. The corporation must draft and maintain its minute book, as well as its by-laws. Unlike the articles of incorporation, by-laws of a corporation dictate how the corporation will manage its affairs internally. Both shareholders and directors must meet to pass organizational resolutions. Among other requirements, the directors need to have a meeting to ratify the incorporation documents and pass by-laws. The shareholders must also have a meeting to adopt the by-laws and appoint the Directors in addition to other essential steps. Lastly, shares must be issued and paid for, a fiscal year end date set, and directors appointed.

For those businesses which were operating as a sole proprietorship or partnership before deciding to incorporate, one additional step is needed. The contracts which you may have entered (with suppliers, customers or licensors) before incorporating should be “assigned” to the corporation, where your obligations are assumed by the corporation. Until the contracts are assigned to the corporation, the sole proprietor or partners remain personally liable.

4.3. Maintaining a Corporation

Similar to a natural person, corporations need to be maintained. Every year, a corporation must file their annual returns with their respective governing bodies and hold an annual shareholders’ meeting to conduct corporate governance activities (e.g. elect directors). Corporations must also hold regular directors’ meetings and audit the account books. Other ongoing obligations include keeping a corporate minute book up-to-date, which requires steps including keeping minutes of any directors’ meetings, a shareholder ledger, and a copy of the corporation’s by-laws.

4.4. The Board of Directors

The board of directors has a wide range of powers. Unlike sole proprietorships and partnerships, the board of directors chooses the direction that the corporation will take, and they can appoint officers to run the day-to-day operations of the corporation. Shareholders normally exert control over the corporation by electing directors. However, it is not uncommon for the owner(s) of a start-up to be the shareholder, director, and officer of the corporation.

While the corporation is a legal person, the corporation needs natural persons to act for it. Hence, the directors are ultimately responsible for the actions of the corporation. Only shareholders have the benefit of limited liability, not the directors. Directors may be personally liable for past wages and criminal actions like fraud. In specific circumstances, directors of a corporation can

even be held liable for the business decisions of the corporation if they unfairly disregard the concerns of a stakeholder.

Under most Canadian corporation statutes, corporations may indemnify and purchase insurance to protect directors and former directors against liabilities incurred by reason of them acting as directors, provided the director was acting consistently with their fiduciary duties and had reasonable grounds for believing their conduct was lawful. It is also common to put director indemnity provisions in a corporation's by-laws.

4.5. Shareholder Rights

Despite the popular belief, shareholders do not own a corporation, or any of its property. As a legal person, the corporation is "owned" by itself, and owns its own property. However, shareholders are granted a bundle of rights to the corporation. The primary rights that are given to the shareholders are the right to dividends, the right to vote, and the right to a portion of the corporation's property upon dissolution.

Dividends are the primary method in which a corporation returns its profits to its shareholders. Whether a shareholder receives dividends and when dividends are issued will depend on which class(es) of shares that a shareholder owns. Information about what classes of shares can be found in a corporation's articles of incorporation. The right to vote also gives a shareholder substantial control over the affairs of the corporation, being given a say in fundamental matters as well as the ability to elect the directors of a corporation.

The right to vote is also important to consider when deciding to become a shareholder. There are some fundamental changes to a corporation that require shareholder voting (e.g. electing new directors, amending the articles of incorporation, amending the share structure, etc.). The right to vote essentially gives the shareholder control when it comes to voting on matters that set the boundaries in which directors can manage within.

Lastly, if the corporation is wound up or dissolved, shareholders may be entitled to a share of the liquidated assets as a return of their invested capital. Whether you receive a share of liquidated assets will depend on whether you hold shares that entitle you to such a distribution of assets.

The right to dividends, to vote, and to the assets upon dissolution must be assigned to at least one class of shares, but all three need not be given to each class. This means you can create a class of non-voting shares in exchange for more dividends or even a share class with vastly increased voting power to enable the founders to retain control.

4.6. Corporations vs Sole Proprietorships and Partnerships

The decision on whether to operate as a sole proprietorship or a partnership versus a corporation will depend on your plans for the business. Some factors to consider include:



- Are you planning to run the business by yourself, with a small group of people, or would you like to allow many people to have a say in it? The more people you would like to have partaking in the operation of the business, the more attractive incorporation becomes.
- What are your capital needs? Will you need to attract investors? The more capital-intensive your business, the more you should consider incorporating.
- How important is limited liability? Are you in a position to personally cover the liabilities of the business? If not, you may value the benefit of limited liability more heavily and should incorporate.
- Are you planning to pass on or transfer your business? Businesses that rely on personal services (e.g. hairdressers) where the owner is an important part of the business are less suited to incorporation, while a technology start-up is more suited to incorporating.

4.7. Conclusion

The decision to incorporate will depend on your plans for your business. Incorporating comes with many benefits, like limiting liability and the ability to raise vast amounts of capital, as well as being handed down or otherwise sold. These advantages are not free, and in exchange for these benefits there are many more maintenance costs and other compliance measures. Whether the benefits of incorporating outweigh the costs will depend on your personal situation. If you believe you are ready to incorporate, you may wish to contact the QBLC for assistance with the incorporation process.



Business Law Playbooks

Part 5 – Incorporating a Not-For-Profit (NFP) Corporation

Prepared by the Queen's Business Law Clinic in collaboration with Queen's Partnerships and Innovation

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Queen's Partnerships and Innovation ("QPI") aims to advance research, innovation, and knowledge mobilization to strengthen Queen's local, national, and global impact. QPI provides faculty, students, post-doctoral fellows, and other members of the Queen's community with a variety of services and resources to facilitate strategic initiatives and research partnerships. QPI is also proud to work with external organizations (both industry and not-for-profits) to connect them with expertise, resources, and incubation support.

About Queen's Business Law Clinic

The Queen's Business Law Clinic ("QBLC") is a free legal clinic which was established in 2009 to provide year-round legal services to a wide variety of individuals, businesses and non-for-profit organizations in southeastern Ontario. The QBLC aims to help individuals and businesses who would otherwise have difficulty affording legal counsel, while providing Queen's Law students with practical legal experience working with clients, while instilling in them the values of community service and the pro bono tradition. The QBLC is proud to have contributed to the economic growth and social well-being of Kingston and its surrounding communities by helping entrepreneurs, small businesses, charities and not-for-profit organizations with their legal needs.

Why do you need a Playbook?

For many people with little or no previous business or entrepreneurial experience, understanding the relationship between law and business – and how it may affect the success or failure of their business idea – is a very important step. In this series of Playbooks, we seek to provide general information on the legal concepts that should be considered by the entrepreneur starting out their business venture.

Disclaimer

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5 Incorporating a Not-For-Profit (NFP) Corporation

For the purposes of this Playbook, we will only be discussing NFP corporations. Other forms of corporations will have their own unique features. Please refer to the corresponding Playbook for for-profit corporations and registered charities.

5.1. What is an NFP?

An NFP corporation is a corporation without share capital that carries on activities without net profit. These activities include almost every type of voluntary association, church, trade, professional association, and advocacy organization.

An NFP corporation may not be operated for the gain of its members, directors, or officers. An NFP can raise revenue that produces a profit, but all profits must be used or distributed in furtherance of the NFP's objectives and for the benefit of the NFP. The NFP Corporation can carry on activity so long as it pertains to its objective and is not operated in a net profit situation. These objectives are defined in the incorporation documents, which will be addressed later in this section.

5.2. Is an NFP corporation right for you?

Incorporating an NFP is not the only way to achieve your organization's goals. Instead, a charitable trust or an unincorporated association may also be viable options, depending on your organization's goals. The benefits of incorporating an NFP include a formal management structure, limited liability, and perpetual existence. However, the benefits of incorporation are not free. In exchange, there are formalities that need to be complied with, both in the process of incorporation and in maintaining the NFP. Some of these formalities include maintaining corporate records (such as registers of members, directors, or officers), filing an annual return, reporting any changes to the directors or registered office address, keeping your articles up to date, and sending copies of any new by-laws or changes to your by-laws to Corporations Canada.

5.3. Not for Profits and Charities

Charities are not a distinct business vehicle, but a designation under the *Income Tax Act* (“ITA”). Many charities are NFP corporations and many NFP corporations have the intention of gaining charitable status, but both are distinct designations. In simple terms, NFPs provide to the community as a public benefit, but its focus is not on obtaining donations to support those endeavours. Contrastingly, with a charitable corporation much of the focus is to gain financial donations to support the endeavours. Registered charities must use their resources for charitable activities and have charitable purposes that fall into one or more of the following categories:

- 1) The relief of poverty (e.g. Food bank)
- 2) The advancement of education (e.g. Research institute)
- 3) The advancement of religion (e.g. Missionary organizations)
- 4) Other purposes that benefit the community (e.g. Animal shelter)

NFPs are associations, clubs, or societies that are not charities and are organized and operated exclusively for social welfare, civic improvement, pleasure, recreation, or any other purpose except profit. Examples of NFPs include:

- Amateur sports organizations (e.g. Soccer league)
- Social or recreational groups (e.g. Golf club)
- Certain festival organizations (e.g. Parades)

While NFP corporations enjoy tax exemptions, charities are able to issue donation receipts, which allow for donees of the charity to write off a portion of their taxable income.

5.4. Features of an NFP

Not-for-profit corporations are similar to for-profit corporations in the features they offer. Not-for-profit corporations enjoy the same separate legal personality, perpetual existence, and limited liability benefits.

5.4.1. *Separate Legal Personality*

One of the most important notions of incorporation is that NFP corporations have all the legal rights of a natural person. This means that NFP corporations are free to enter into contracts using their own name, borrow money on their own credit, own their own property, declare bankruptcy, sue, and be sued in their own capacity.

5.4.2. Perpetual Existence

A perpetual existence can be attractive to not-for-profits as the corporation can continue running in perpetuity, as long as it continues meeting its obligations under its governing legislation. Members and directors can come and go, but the property will be retained by the not-for-profit and the operations can continue under new directors.

5.4.3. Limited Liability

Not-for-profit corporations also have the benefit of limited liability, but this benefit is less pronounced than its for-profit counterpart. Members of the corporation are not liable for the defaults and liabilities of the not-for-profit corporation, whether it arises from contracts the corporation enters or the corporation's tortious conduct.

5.5. Structure of an NFP

5.5.1. Articles of Incorporation

The articles of incorporation (the "articles") are created during the incorporation of the NFP Corporation. The articles sets out the name of the not-for-profit, the province or territory the registered office is situated, the size of the board of directors, the statement of the purpose of the corporation, restrictions on the activities the corporation can carry on, classes of members, distribution of property upon liquidation, and any other provisions the incorporators decide on.

5.5.2. Board of Directors

The board of directors is responsible for managing the activities and affairs of the corporation, and have a wide range of powers. Directors decide the actions that the NFP Corporation will take to further the NFP's stated purposes. Directors are legally obligated to act honestly and in good faith in prioritizing the corporation's interests. Directors are required to exercise the care, diligence, and skill that a reasonably prudent person would in comparable circumstances. This means directors cannot do anything that goes against the corporation's articles, by-laws, or a unanimous member agreement. Directors have increased liability compared to members because of their position as the decision-makers in the company.

5.5.3. Members

Instead of shareholders, not-for-profit corporations have members. Classes of members are established in the articles and they oversee and approve certain director decisions. NFP corporations have the option of creating multiple classes with different conditions for each membership class. If you only have one class, all members have the right to vote. If there are multiple classes, at least one class of members must have the right to vote.

In general, members are not liable for any default of the NFP Corporation. However, members may become liable in the same way as a director, if all the members of a corporation sign a document called a "unanimous member agreement". Unanimous member agreements can take power away from directors and assign that power to the members instead. In taking power away from the directors they also assume the risk of liabilities the directors have. In most circumstances, only members in a voting class can influence business decisions by voting to

approve director actions. Examples of business decisions that voting members can affect are changing the by-laws, and electing or removing directors.

5.6. Federally Incorporated NFPs

Similar to for-profit corporations, you may choose to incorporate your NFP Corporation in a federal or provincial jurisdiction. Federally incorporated NFPs will be governed by the *Canada Not-for-profit Corporations Act* (“CNCA”) while Ontario NFPs are governed by the *Ontario Not-for-Profit Corporations Act* (“ONCA”).

There is a fee attached to the federal incorporation process for NFPs when you file online. Federal NFPs can use an automatically assigned number name (e.g. 12345678 CANADA Association) or a worded name of your choosing. Opting to use a worded name instead of a numbered corporation will also require a NUANS name search report, which will require an additional fee.

Advantages of a federally incorporated NFP include turnaround time and Canada-wide name protection. A federal incorporation is completed the next business day, and the name you choose will be yours across Canada. For example, if your NFP plans to organize events, promotions, or establish offices in other provinces, the federal NFP incorporation will provide you with the highest level of name protection and wider rights to carry on business throughout the entire country. Federal incorporation means that you are able to do business across Canada using the same business name, even if some other company is already using a similar name in some province or territory. So, if your federally incorporated business is XYZ Inc., you can do business in any province or territory as XYZ Inc., even if there are other companies operating under identical names in the same provinces or territories. Federal incorporation also has a cachet that provincial incorporation does not and gives a company global recognition.

The disadvantages of a federally incorporated NFP mostly relate to the corporation’s upkeep costs. Like federal for-profit corporations, federally incorporated NFPs need to register in their home province or territory where they carry on their activities.

Registration is different from incorporation. An NFP may incorporate only once, but registration of the federal NFP is required by its home province or territory usually within a few weeks of incorporation. There are no registration fees for home province or territory registration. Federal incorporation also requires more paperwork to be done every year as you will need to comply with corporate filing requirements. Federal NFPs need to file a Corporate Tax Return and Corporate Information Return, in addition to return of all the provinces the NFP is extra-territorially registered with. Federal incorporation may cost more because of the additional annual paperwork required, as well as the additional fees resulting from the need to register your corporation extra-provincially.

5.7. Ontario Incorporated NFPs

Incorporating provincially cannot currently be done online but needs to be applied for in-person or by mail. Just like federal NFPs, there is a cost attached to incorporation and provincial NFPs

can choose to use a numbered or worded name. The provincial name search will cost more than the federal NUANS search.

The upkeep of an Ontario NFP offers a comparative advantage over federal NFPs. The tax and annual filing requirement are done as one, reducing the associated legal and accounting fees.

The incorporation process is the major downside to incorporating provincially. While the incorporation fee is lower for provincial NFP corporations than federal NFP corporations, the wait time is vastly longer. Ontario only allows for NFPs to incorporate by mail or in-person, and takes 6-8 weeks to process (there is an expedited option to get the process completed in 7 business days). Each provincial incorporation is a standalone process. Once incorporated, your NFP's name will only be protected in Ontario. To do business in another province, you will need to register with that authority.

5.8. Soliciting and Non-Soliciting NFPs

Non-profits can be categorized as soliciting or non-soliciting NFPs under the *CNCA* (for provincially incorporated NFPs, they are instead called “public benefit corporations” and “non-public benefit corporations”). Soliciting corporations are those that receive more than \$10,000 in a calendar year from government grants, funds from another corporation that also received funds from public sources, or gifts and donations from non-members. Soliciting corporations have more stringent oversight requirements, to ensure transparency and accountability of public funds. For federally incorporated NFPs, this includes having at least two independent directors who are not officers or employees of the corporation, more stringent financial reviews, restrictions on where the property can be distributed upon the dissolution of the corporation, and a ban on unanimous member agreements. The “soliciting” status will last for three years regardless of whether or not your corporation receives \$10,000 in the two years after receiving the status.

	Soliciting Corporation	Non-soliciting Corporation
<u>Number of directors</u>	Minimum of 3 with at least 2 not being officers or employees	At least 1
<u>Financial review</u>	Under \$50,000 gross annual revenues <ul style="list-style-type: none"> • Default is review engagement*; audit or no review possible Between \$50,000 and \$250,000 gross annual revenues <ul style="list-style-type: none"> • Default is audit**; review engagement possible Over \$250,000 gross annual revenues <ul style="list-style-type: none"> • Must have an audit 	Under \$1 million gross annual revenues <ul style="list-style-type: none"> • Default is review engagement; audit or no review possible Over \$1 million gross annual revenues <ul style="list-style-type: none"> • Must have an audit



<u>Filing financial statements</u>	Yes	No
<u>Restrictions on property upon liquidation</u>	Yes – to qualified donees under the <i>Income Tax Act</i>	No restrictions
<u>Unanimous members agreement</u>	Not allowed	Allowed
<p>* Financial statements prepared by a public accountant who does not express an opinion on the fairness of the financial statements. He/she provides a limited assurance that the financial information is plausible and conforms to IFRS generally accepted accounting principles. ** Financial statements are prepared by the public accountant after examining accounting records and other evidence supporting the financial statements. He/she provides a professional opinion on whether the financial statements present a fair picture of the organization's financial position and its activities during the period the audit covered.</p>		

In Ontario, the categorization of public and non-public benefit corporations also depends on the amount of government funding or external donations received. Both Ontario and Federal NFPs that are receiving public funds will have increasingly more onerous financial reviews when receiving higher levels of public funds. This can result in requiring a full audit. Ontario NFPs are allowed to receive more public money before a full audit is required and allows for an extraordinary resolution (80% of voting members) to waive a review engagement (verifies whether the financial statements are plausible).

5.9. Charitable NFPs

If you plan to have your not-for-profit register as a charity under the *ITA*, there are additional considerations for your incorporation of a not-for-profit. There needs to be an additional restriction on the corporation in that the directors of the not-for-profit corporation cannot be compensated. The corporation must also have charitable purposes of either advancing education, advancing religion, relieving poverty, or have some other purpose that benefits the community.

5.10. Steps to NFP Incorporation

5.10.1. Step 1: Decide Which Legislation to Incorporate Your NFP Under

Before you start the NFP incorporation, you may want to consider whether an NFP corporation is the most appropriate business vehicle for you. Some factors to consider are limited liability, perpetual existence of the corporation, taxation matters, costs of incorporation and maintenance, and whether you want national presence.

Additionally, you should also consider whether you want to be federally or provincially incorporated. Are there any other third-party requirements that may affect your jurisdiction of incorporation or form of vehicle?



5.10.2. Step 2: Consider Your Corporation's Purposes

Your corporate purposes must accurately reflect the nature of your organization and it must be consistent with the intended tax status of the corporation. A NFP's purposes must be for social welfare, civic improvement, pleasure or recreation, or for any other purposes, except profit. For example, an NFP in the photography field might describe its purpose as "the establishment and operation of a photography club for the purposes of studying and promoting the art and science of photography, and such other complementary purposes not inconsistent with these objects".

5.10.3. Step 3: Conduct a Name Search

If you choose to use a unique name of your choice, you must confirm the availability of your desired name through a NUANS name search report (a Federal or Ontario-biased NUANS search, depending on your jurisdiction). When you are deciding on the name of your organization, you may want to consider whether the name reflects the nature of the organization, is easily recognizable, and whether you would want to seek trademark protection.

5.10.4. Step 4: Consider Expected Grant Funding or Donations

If you expect to receive more than \$10,000 grants, funds, or gifts and donations from non-members during a single fiscal year, you may want to structure your organization in anticipation of becoming a soliciting corporation. This includes appointing a minimum of 3 directors and preparing to file financial statements to Corporations Canada.

5.10.5. Step 5: Prepare Incorporation Application

If you choose to incorporate federally, you will need to file two documents, the Articles of Incorporation (Form 4001) and the Initial Registered Office Address and First Board of Directors (Form 4002).

When incorporating provincially, only one form is required, the Application for Incorporation of a Corporation without Share Capital (Form 2).

Both applications will require similar information: The name of the not-for-profit corporation (along with the NUANS search if needed), the head office of the corporation, the initial directors of the corporations, the purpose of the not-for-profit, and the classes of memberships that the corporation can establish.

5.11. Post-Incorporation Matters

After incorporating, there are several post-incorporation steps for the corporation to take. The corporation must draft and maintain its minute book and by-laws. Unlike the articles of incorporation which govern the corporation very generally, by-laws of a corporation dictate how the corporation will manage its affairs internally. The directors need to have a first meeting to ratify the incorporation documents and pass by-laws. The directors can also decide on how corporate records would be maintained, appoint officers, appoint an interim public accountant, authorize the issuance of debt obligations, or make banking arrangements at this first meeting

as well. Lastly, memberships must be issued, a fiscal year end date set, and the first directors appointed.

The members also need to hold their meeting, to confirm (or modify, or reject) the by-laws of the corporation and elect the directors. Provincial and territorial registrations must also be filed in every jurisdiction the business carries on its activities (if needed) along with fulfilling any other requirements such as obtaining permits or satisfying other formalities. For example, you may need a provincial permit to carry on activities in a particular sector, such as a bingo license in order to operate a bingo, or liquor permit in order to sell alcoholic beverages.

5.12. Maintaining a Not-for-Profit

Continuing a NFP corporation requires annual filings. For federal NFPs, this involves an annual return with Corporations Canada as well as a tax filing with the CRA. For provincial NFPs, the annual return with Service Ontario is included with the NFP's tax filings as one document.

Not-for-profits must also conduct regular meetings of both the board of directors and annual general meetings for the members, so directors can be elected, annual financial statements reviewed and certain matters voted on. Ongoing obligations also include keeping a corporate minute book up to date (with the corporation's by-laws) and depending on the amount of contributions from the public, an annual audit or review engagement. Other obligations may include filing a change of registered office address, reporting changes regarding directors, sending copies of changes to by-laws or the addition of new ones, and filing articles of amendments.

5.13. Conclusion

Incorporating a not-for-profit will grant your organization legal status and may be a worthwhile decision if you value the formal management structure, limited liability, and perpetual existence benefits they can bring. These benefits can come at a cost, and require you to undertake several formalities, like maintain corporate records, filing annuals returns, reporting changes to the directors, updating articles, and sending copies of new or changed by-laws to Corporations Canada. Whether the benefits of incorporating outweigh the costs will depend on your personal situation. If you believe you are ready to incorporate your not-for-profit, you may wish to contact the QBLC for assistance.



Business Law Playbooks

Part 6 – Charities and Charitable Status

Prepared by the Queen's Business Law Clinic in collaboration with Queen's Partnerships and Innovation

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Queen's Partnerships and Innovation ("QPI") aims to advance research, innovation, and knowledge mobilization to strengthen Queen's local, national, and global impact. QPI provides faculty, students, post-doctoral fellows, and other members of the Queen's community with a variety of services and resources to facilitate strategic initiatives and research partnerships. QPI is also proud to work with external organizations (both industry and not-for-profits) to connect them with expertise, resources, and incubation support.

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Why do you need a Playbook?

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6 Charities and Charitable Status

There are three forms that a registered charity can take: (1) a charitable organization, (2) a private foundation, or (3) a public foundation. The form the registered charity takes is dependent upon the structure, mode of operation, and sources of funding. With one director, official, or trustee, the registered charity will be designated as a private foundation. To be designated as a public foundation or a charitable organization, more than 50% of the directors, officials, or trustees must be at arm's length.¹

	Charitable Organization	Private Foundation	Public Foundation
Can be established as...	A corporation, trust, or under a constitution	A corporation or trust	A corporation or trust
Purposes	Only charitable purposes	Only charitable purposes	Only charitable purposes
Activities	Primarily carries on its own activities that are charitable in nature	Carries on its own charitable activities and/or funds qualified donees	Generally, gives upwards of half of its income to qualified donees annually
Directors, Officials, and Trustees	More than 50% at arm's length	More than 50% not at arm's length and/or	More than 50% at arm's length
Funding Sources	From a variety of arm's length donors	More than 50% from a person or group that control the charity	From a variety of arm's length donors

In order to register, the charity must apply to the CRA. Registered charities and non-profit-organizations both operate on a non-profit basis; however, registered charities must use their resources (financial, property, personnel) for charitable purposes that target either: poverty relief, the advancement of religion or education, or other purposes benefiting the community. Examples of registered charities include food banks, universities, missionary organizations, and animal shelters. While you can operate as a charity without registration, if you wish to be able to

¹ Canadian Revenue Agency, "Types of Registered Charities (Designations)" (2016) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/registering-charitable-qualified-donee-status/apply-become-registered-charity/establishing/types-registered-charities-designations.html>.

issue official donation receipts and not pay income tax, you must register. A charity, whether registered or unregistered, cannot be a non-profit organization.²

For a [glossary](#), please see the resources provided by the CRA.

6.1. Advantages & Disadvantages of Registration

6.1.1. Advantages

Becoming a registered charity allows an organization to issue official donation receipts, to receive CRA designation status as a charitable organization or public/private foundation, and to be exempt from paying income tax. It also makes the organization eligible to receive gifts from other registered charities, increases public credibility, and exempts many goods and services you provide from GST/HST.

6.1.2. Disadvantages

The advantages afforded by registration also come with corresponding obligations. As a registered charity, you must devote the organization's funds, personnel, and property to the pursuit of its charitable purpose and activities. You must maintain your organization's status as a legal entity, maintain the control, direction, and use of the organization's resources, and keep proper books and records.³ Furthermore, you must issue proper donation receipts, file annual forms and returns, and meet annual spending requirements. Finally, you must inform the Charities Directorate about any changes to your organization's mode of operation or legal structure.⁴

For additional [checklists](#), please see the resources provided by the CRA.

Please note that some of the documentation provided – including governing documents, financial statements, annual information returns, and public portions of the application form – will be available to the public.

² Canadian Revenue Agency, "Advantages and Obligations of Becoming a Registered Charity" (2018) DOI: Canadian Revenue Agency, "What is the difference between a registered charity and a non-for-profit organization?" (2016) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/giving-charity-information-donors/about-registered-charities/what-difference-between-a-registered-charity-a-non-profit-organization.html>.

³ Canadian Revenue Agency, "Books and Records" (2016) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/operating-a-registered-charity/books-records.html>.

⁴ <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/registering-charitable-qualified-donee-status/apply-become-registered-charity/deciding/advantages-obligations-becoming-registered-charity.html>.

6.2. Considerations⁵

Is your organization a Canadian resident?

- Your organization **must** be a resident in Canada to qualify for charitable registration in Canada. Organizations incorporated in Canada are deemed to be Canadian residents.
- If your organization is not considered a Canadian resident, you cannot register.

Does your organization meet one or more of the four categories (poverty relief, the advancement of religion or education, or other purposes benefiting the community)? Is your organization otherwise prohibited from registration?⁶

- Your organization must meet at least one of the four charitable purposes that have been identified by the common law in Canada. While the purposes or the aim of the organization must meet one of the four objectives, the activities or how the organization carries out its purposes can be different.
- If your organization does not meet one of the four categories, you will not be able to register.
- Registered charities also cannot support private benevolence or the benefit of a particular individual or private group (i.e. fundraising for a specific family who lost their house in a fire).
- The income of a registered charity cannot be used for the purpose of benefiting its members personally.
- Organizations devoting their resources, or part of their resources, to indirect or direct support or opposition of a candidate for public office or a political party will not qualify.
- Organizations with the goal of earning a profit will not meet registration qualifications.
- Related business activities promoting or accomplishing the charitable purpose are permitted for charitable organizations and public foundations. Business activities are prohibited for private foundations.
- Organizations participating in illegal activities, activities that are contrary to public policy, or that indirectly or directly support terrorism will not qualify for registration.

⁵ Canadian Revenue Agency, "Should You Apply For Charitable Registration?" (2016) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/registering-charitable-qualified-donee-status/apply-become-registered-charity/deciding/should-apply-registration.html>.

⁶ Canadian Revenue Agency, "What is Charitable?" (2019) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/registering-charitable-qualified-donee-status/apply-become-registered-charity/deciding/factors-that-will-prevent-organization-being-registered-a-charity.html>.

Does your organization meet the public benefit test?⁷

- The organization's purposes and activities must meet this test. The organization must demonstrate that the purposes and activities provide a measurable public benefit and that the people eligible for benefits are either a significant segment of the public or the public as a whole.
- The beneficiaries cannot be connected by a private association and cannot be a restricted group.

Do you plan to hire employees or recruit volunteers?

- Having employees or volunteers may be necessary for the success of the organization.
- While having employees or volunteers does not determine if you can register, if you do hire employees, you **must** submit the required payroll deductions.

Can you meet the ongoing obligations associated with registration (i.e. annual returns)? Are you aware of the penalties if you do not meet these obligations?

- To meet the ongoing obligations of registration, a registered charity must: maintain the status of a legal entity by keeping up with annual post-incorporation obligations; keep proper records and books; devote resources to the charitable purpose; file the required annual return; direct and control the use of the organization's resources; meet annual spending requirements; and issue proper donation receipts.
 - Directors or trustees of registered charities are responsible for the management and administration of the charity and ensuring that the charity follows all applicable laws and regulations.
 - The eligibility of each Board Member could impact the registration of the charity. More than 50% of the governing officials of the registered charity must be at arm's length. Furthermore, the CRA also has the authority to refuse, suspend, or revoke registration where ineligible individuals sit on the Board, control, or manage the organization.⁸
- If the ongoing obligations are not met, the charity will face consequences such as financial penalties, having the tax receipting privilege suspended, or even the loss of its registration.

⁷ Canadian Revenue Agency, "What is Charitable?" (2019) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/registering-charitable-qualified-donee-status/apply-become-registered-charity/establishing/what-charitable.html>.

⁸ Canadian Revenue Agency, "Ineligible Individuals" (2016) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/ineligible-individuals.html>.

Have you considered the consequences of the revocation of your organization's status or ending the organization's operations?

✓ If status is revoked or if operations voluntarily come to an end, the organization will not be able to issue donation receipts, will no longer qualify as income tax exempt, and must give all remaining assets to a qualified donee or pay the full value of the assets as a revocation tax.

✗ If the organization is no longer a registered charity, there are strict procedures regulating the liquidation of assets, tax implications, and the loss of the ability to issue donation receipts. Registration may be revoked voluntarily, as a result of failure to file, as the result of an audit, and for other reasons (i.e. loss of corporate status). While organizations typically do not start with their end in mind, these are relevant factors to consider. Furthermore, if your charitable registration is revoked, the name of your organization and the reason for the revocation will be published.⁹

6.3. Application Process¹⁰

6.3.1. Step 1: File the Application

- ✓ If the application is complete, you will receive an acknowledgement letter stating approximately how long the wait for review will be.
- ✗ If the application is incomplete, it will be rejected and returned.

To generate an [application document checklist](#), please visit the CRA website.

6.3.2. Step 2: Request for Additional Information

- ✓ You may be contacted for additional documentation or information. This may include the opportunity to amend your organization's purposes. If this occurs, you will usually have a period of 60 days to respond.
- ✗ The application will be denied, and a final decision issued if the purposes or activities are not demonstrated to be charitable.
- ✓ If you believe all of the necessary information has been provided, you can respond in writing accordingly and a final decision will be issued.
- ✗ If you do not respond, the application will be considered abandoned, and the file will be closed. There is no right to appeal this decision, but you will be able to reapply.

6.3.3. Step 3: Application Denied

- ✗ If the purposes or activities are found not to be charitable, a letter will be issued stating that the application has been denied.

⁹ Canadian Revenue Agency, "Types of Revocation" (2018) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/revoking-registered-status/types-revocation.html#volrev>.

¹⁰ Canadian Revenue Agency, "Application Review Process" (2018) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/registering-charitable-qualified-donee-status/apply-become-registered-charity/application-review-process.html>.

- ✘ If the application is denied, the decision can be appealed within 90 days by filing a notice of objection.

6.3.4. Step 4: Application Approved

- ✓ If the application is approved, notice of registration will be issued.

6.4. Describing Charitable Activities

One of the key portions of the application is the description of charitable purposes and activities. Within the application, you must describe each of the activities you will undertake to achieve the purpose. Fundraising is not in-and-of-itself a charitable activity and cannot become the main emphasis of the charity. You will also have to show how it benefits the public. The description will have to be extensive covering considerations such as: detailed plans, the intended object to be achieved, fees charged (if any), how beneficiaries are selected and who they are, length and frequency of the activities, any volunteer/employee involvement, how direction and control will be maintained over these activities and the organization's resources, the necessary logistics (i.e. buildings, transportation, etc.), and any other relevant information.¹¹

6.5. Supporting Documentation

Registered charities must be legally established as evidenced by articles of incorporation, letters patent, a constitution, or trust documents. As part of the registration process, an organization's governing documents as well as any amendments must be submitted. The type of documentation required depends on the form of the organization.¹²

6.5.1. Incorporation

Applicants registering as a charitable organization, or a public/private foundation can incorporate. For the advantages and disadvantages associated with incorporation, please see the appropriate Playbook. The incorporation documents will vary depending on the jurisdiction of incorporation. For-profit corporations are ordinarily inappropriate to register as a charity given that charities operate on a not-for-profit basis. These documents must have an effective date and be signed or stamped by the relevant authority.¹³

6.5.2. Constitutions

Non-incorporated organizations can seek registration under a constitution. The constitution must include, at a minimum: the organization's name and purpose, that the organization will be operated with any profits or assets being used to promote the organization's purpose, that the

¹¹ Canadian Revenue Agency, "Describing Your Activities" (2018) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/registering-charitable-qualified-donee-status/apply-become-registered-charity/apply/describing-your-activities.html>.

¹² Canadian Revenue Agency, "What is a Governing Document?" (2019) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/registering-charitable-qualified-donee-status/apply-become-registered-charity/establishing/what-a-governing-document.html>.

¹³ Canadian Revenue Agency, "Incorporation Documents" (2018) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/applying-registration/governing-documents/incorporation-documents.html>.

organization will be operated without the purpose of member gain, how the directors of the organization will be replaced, the structure of the governing body, the effective date, and the signatures of three or more of the directors of the organization.¹⁴

6.5.3. Trusts

Applicants registering as a charitable organization, or a public/private foundation can be established through a trust document. The trust document must include at a minimum: the trust name, the name of the person(s) making the declaration or the settlor(s), the trust's charitable purposes, the names of the initial trustees, how the property of the trust will be administered, an acknowledgement that the initial property of the trust has been transferred and received by the trustee(s), assurance by the trustee(s) that all property will only be used for the purposes set out in the trust document, how trustees will be replaced, the effective date, and the trustee signatures. It is also recommended that the document include a provision allowing the purposes to be amended to correspond to legislative and common law requirements for registration.¹⁵

6.6. Conclusion

If you are considering registering your charity, you may wish to contact the Queen's Business Law Clinic for assistance.

The above does not constitute legal advice regarding the validity of any of the above documents. We recommend you seek legal advice before incorporating, creating a constitution, or enacting a trust. Much of the information in this document is sourced from information published by the Government of Canada. This document has not been endorsed by, or produced in affiliation with, the Government of Canada.

¹⁴ Canadian Revenue Agency, "Constitutions" (2018) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/applying-registration/governing-documents/constitutions.html>.

¹⁵ Canadian Revenue Agency, "Trusts" (2018) DOI: <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/applying-registration/governing-documents/trusts.html>.



Business Law Playbooks

Part 7 – Non-Profit (Unincorporated) Organizations

Prepared by the Queen's Business Law Clinic in collaboration with Queen's Partnerships and Innovation

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7 Non-Profit (Unincorporated) Organizations

7.1. Introduction

A Non-Profit Organization (“NPO”) is defined by the *Income Tax Act* (“ITA”) as a club, society, or association that is not a charity and that is organized and operated solely for:

- Social welfare (social, recreational, or hobby groups – e.g. golf clubs),
- Civic improvement (some amateur sports organizations – e.g. local hockey leagues),
- Pleasure or recreation (some festival organizations – e.g. parades and seasonal celebrations), or
- Any other purpose except profit.

What is important to qualify as a NPO is that no part of its income can be made payable to or available for anyone’s personal benefit.

These types of organizations can be very informal and are very common. For example, any group of people involved in raising funds to open a local library or to assist with a tragedy or disaster relief would be considered a NPO.

Although a not-for-profit (“NFP”) corporation is also considered a NPO, when referring to a NPO in this Playbook, we are referring to unincorporated associations. Thus, a NPO is distinct and different from a NFP corporation in that the NPO has not gone through the incorporation process. More information about NFP corporations can be found in the “NFP” Playbook.

7.2. How is a NPO formed?

NPOs are generally simple and inexpensive to create. Unlike a NFP corporation, there is no legislation that governs a NPO or outlines a procedure for its formation. This means that, similar to a sole proprietor and a partnership, there are no formalities required to form a NPO. A NPO will be created when a collection of individuals act together to achieve one of the above purposes. There is no requirement for its members to form a constitution or a set of by-laws, but it is prudent for a NPO to have some sort of agreement among its members to guide decision-making and help settle disputes if one were to arise. A properly executed constitution or other agreement may become a legally binding document that a court will consider should a dispute arise.

7.3. Features of a NPO

A NPO is not a separate legal entity. This means that, unlike a corporation, a NPO is not recognized as separate from the group of individuals who are administering it. A NPO does not have independent power to enter into contracts, it cannot sue or be sued, and it cannot hold

property. Its members are not protected from liability. The individuals administering the NPO will be personally liable for all the acts, liabilities, and debts of the NPO.

Because there is no governing legislation for forming a NPO, NPOs are much more flexible in the way that they are structured. For example, NPOs are not required to have a board of directors.

It may be more difficult for a NPO to raise funds required to carry out their operations. A NPO is entirely reliant on donations from the public and contributions from its members. However, a NPO cannot issue tax receipts to donors. The ability to issue tax receipts is a huge benefit to becoming a registered charity, as it can incentivize prospective donors to donating money to the charity.

A NPO is exempt from paying tax on all or part of its taxable income, so long as it meets the definition of a NPO during that tax period. However, a NPO may still have to pay tax on property income or on capital gains.

7.4. Why Use this Vehicle?

There are a few reasons why a NPO might be an appropriate vehicle for your business idea. NPOs are exempt from paying tax and are not subject to the same level of regulatory requirements as charities or NFP corporations.

Some NPOs have no need for the legal protection from liabilities that is provided through incorporation and have more pressing needs for the limited funds available to them. For these NPOs, the initial costs, diminished structural flexibility, and increased regulatory requirements that accompany incorporation outweigh the benefits provided by incorporation. Having fewer regulatory requirements also means that the NPO will be more independent from government and public oversight, which may be attractive to some associations like trade unions and political parties.

7.5. Filing Obligations

There are some filing obligations that may be required by a NPO. A NPO will have to file *Form T1044, Non-Profit Organization (NPO) Information Return* if:

- It received or was entitled to receive taxable dividends, interests, rentals, or royalties totalling more than \$10,000 in the fiscal period,
- The total assets of the organization were more than \$200,000 at the end of the immediately preceding fiscal period, or
- It had to file an NPO Information Return for a previous fiscal period.

Note that a NPO that meets one of the first two criteria above will subsequently have to file a NPO Information Return at the end of every fiscal period for the rest of its existence, even if it no longer meets those first two criteria.

This form must be filed no later than six months after the end of each of its fiscal periods. Further, depending on the type of NPO, other tax returns may also be required. For example, A NPO will also have to file a *T3 – Trust Income Tax and Information Return* if its main purpose is to provide dining, recreational, or sporting facilities.

7.6. NPOs vs Registered Charities

Many people equate NPOs with charities and use the two terms interchangeably. However, this is not accurate. It is important to remember that the *ITA* prohibits a NPO from also being a registered charity. As a result, each type of organization is distinct.

A charity must apply to the Canada Revenue Agency (“CRA”) for registration. This will exempt it from paying income tax and will permit it to issue charitable donation receipts. A NPO is not required to register federally or provincially to acquire its tax-exempt status, but it cannot issue tax receipts for donations or membership fees. NPOs also do not have to comply with the same level of stringent CRA reporting requirements as charities.

Charities must operate to achieve a specified charitable purpose (for more information see Part 6 of this Playbook series). A NPO, on the other hand, is prohibited from operating exclusively for one of those charitable purposes. However, it can operate for any other purpose except profit.

7.7. Steps in Setting up a NPO

7.7.1. Step 1: Decide on an NPO

Decide that a NPO is the appropriate business structure – get legal and accounting advice from experts.

7.7.2. Step 2: Decide on a Name

Decide on a name for the NPO. Do some research and conduct an Enhanced Business Name Search through the Ontario Business Registry to find out whether your proposed name is available. The cost to conduct a search may vary depending on the type of search records requested. You may also conduct a preliminary name search using the opstart.ca free NUANS preliminary search option.

7.7.3. Step 3: Register Name

If your chosen name is available, register your business name in Ontario. Business name registration is effective for five years, after which you must renew it. The cost of registration varies depending on your method of filing. Payment can be made online using a Visa or MasterCard, or by mailing a cheque, money order, or cash to the Ministry of Finance.

7.7.4. Step 4: Protect Intellectual Property

Protect your trademark and purchase a domain using your preferred business name, if applicable. A trademark is a way for the public to identify that the goods or services being provided are from a certain party. This can go a long way in protecting your NPO's reputation, as well as protecting against potential trademark infringement claims. The QBLC offers its clients trademarks advice by assisting them in conducting detailed trademark searches and providing them with a legal opinion on the availability of their proposed trademarks for registration in Canada.

7.7.5. Step 5: Prepare Constitution

Write your constitution or other agreement to structure your NPO. Important things to cover in this document include:

- The purpose of the NPO
- The parties to the agreement and their respective responsibilities
- Names and contact information of the other parties to the agreement, as well as the address of the head office
- Process whereby certain business decisions will be made (unanimous, two-thirds, majority vote)
- Process whereby those in decision-making roles get those positions (Vote by the members? Appointed by certain individuals?)
- A dispute resolution process and how members of the NPO may be disciplined or expelled

7.8. Conclusion

Like a sole proprietorship or a partnership, a NPO is relatively easy and inexpensive to set up. The most important thing to remember is that the NPO's purpose must be for anything besides making a profit but cannot be exclusively for a charitable purpose.

There are significant differences in the legal features of a NPO compared to a NFP corporation or a charity. A NPO is not a separate legal entity, so it does not have powers or liabilities separate from the individuals who administer it. Unlike a charity, NPOs cannot issue tax receipts and there is no need to register to acquire their tax-exempt status. Should you require additional legal advice specific to your situation, the QBLC would be happy to assist you.



Business Law Playbooks

Part 8 – Social Enterprise in Canada

Prepared by the Queen's Business Law Clinic in collaboration with Queen's Partnerships and Innovation

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About Queen’s Business Law Clinic

The Queen’s Business Law Clinic (“QBLC”) is a free legal clinic which was established in 2009 to provide year-round legal services to a wide variety of individuals, businesses and non-for-profit organizations in southeastern Ontario. The QBLC aims to help individuals and businesses who would otherwise have difficulty affording legal counsel, while providing Queen’s Law students with practical legal experience working with clients, while instilling in them the values of community service and the pro bono tradition. The QBLC is proud to have contributed to the economic growth and social well-being of Kingston and its surrounding communities by helping entrepreneurs, small businesses, charities and not-for-profit organizations with their legal needs.

Why do you need a Playbook?

For many people with little or no previous business or entrepreneurial experience, understanding the relationship between law and business – and how it may affect the success or failure of their business idea – is a very important step. In this series of Playbooks, we seek to provide general information on the legal concepts that should be considered by the entrepreneur starting out their business venture.

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8 Social Enterprise in Canada

8.1. General Overview

Social enterprises are a “hybrid” business model that falls between charities, not-for-profit corporations, and business corporations. There is no unified definition of a social enterprise in Canada. The Ontario Government defines it as “an organization that uses business strategies to maximize its social or environmental impact,”¹⁶ while the Government of Canada defines them as “a revenue-generating organization whose objective is to have a social impact.”¹⁷

Social enterprises are created for the dual purposes of a community benefit and generating profit. The specific objectives of social enterprises tend to be employment-related, cultural and/or environmental.¹⁸ Many social enterprises focus on benefitting their local community, defined by neighborhood or city. For example, a significant percentage of social enterprises located in British Columbia, Alberta, and Ontario claim to serve Indigenous populations.¹⁹ Employment-related social enterprises focus on providing employment opportunities to individuals and groups “experiencing barriers to employment” for a variety of reasons, including rural and remote location. The dual purposes of social enterprises – a community benefit and profitability – often run the risk of conflicting and competing with each other.

Given their community objectives, social enterprises are accountable to a broader range of stakeholders than ordinary corporations are. Democratic decision-making is a key feature in many social enterprises, as it intends to engage various stakeholders in shaping the strategic direction of the enterprise. This is typically done by giving one vote to everyone instead of one vote per share. Moreover, those eligible to vote do not necessarily have to own shares.²⁰

8.2. Legal Structure

Social enterprises are not necessarily corporations, but they can be. Social enterprises exist on a spectrum between those entities that operate purely for a social purpose (charities) and entities that operate purely for a commercial purpose (commercial corporations and businesses). They can take many legal forms and include non-profit organizations and registered charities who generate revenue through a related business, as well as for-profit businesses that have social goals.

Please consult our other Playbooks for more information on how to structure your business.

¹⁶ Government of Ontario, “A Social Enterprise Strategy for Ontario” (2013), online: <<https://www.ontario.ca/page/impact-social-enterprise-strategy-ontario>> (“A business with two goals: achieve social, or environmental outcomes and maximize revenue.”) (Hereinafter “Ontario Social Enterprise Strategy”).

¹⁷ http://www.ic.gc.ca/eic/site/053.nsf/eng/h_00006.html#s1

¹⁸ Peter R Elson & Peter V Hall, “Strength, Size, Scope: A Survey of Social Enterprises in Alberta and British Columbia” (2010) at 9, online: <<https://www.mtroyal.ca/cs/groups/public/documents/pdf/socialenterprise2.pdf>>.

¹⁹ *Ibid* at 30.

²⁰ Matthew Thompson & Joy Emmanuel, “Assembling Understandings: Findings from the Canadian Social Economy Research Partnerships, 2005-2011” (Victoria, BC: University of Victoria, 2012) at 16.

8.3. Different Types of Social Enterprises

8.3.1. Charities Operating a Related Business

The “Charity” Playbook outlined how charities can be formed, and the advantages and disadvantages of registering as a charity. A consideration when registering as a charity is whether the organization will want to sell products or perform services to earn revenue towards their social goal.

Charities who wish to carry on business activities must determine whether the business they are carrying is considered acceptable or unacceptable for a charity. An acceptable business is one that is related to the charitable purpose for which the charity was registered.

There are two kinds of related businesses. The first is a business that is run substantially by volunteers. Under this type of related business, the business activities do not have to be related to the charity’s objects, but at least 90% of those employed in the business must be unpaid volunteers. In this context, “employed” is meant to refer to the people who operate the business, regardless of whether they are contractors or direct employees.

The second type of related businesses are those that are linked to a charity’s purpose and subordinate to that purpose. Under this type of related business, it is not sufficient for the profits of the business to be applied to the charitable purpose. The business activities must fit within one of these four categories to be considered “linked” to a charity’s purpose:

<p>1) A usual and necessary concomitant of charitable programs</p> <p>These are business activities that are either necessary for the effective operation of the programs or improve the quality of the service delivered in these programs. An example would be a hospital’s parking lot and cafeteria, or the gift shop of a museum.</p>	<p>2) An off-shoot of a charitable program</p> <p>In some cases, charitable programs happen to create by-products that can be exploited in a business. Examples include a church which has a famous choir and records its special Christmas services to sell to those who could not attend the service. This is a business activity, but the business is related to the charity’s purpose because the recording is merely a by-product of the church’s charitable program.</p>
<p>3) A use of Excess Capacity</p> <p>Charities may use assets and staff that are not currently needed to conduct a charitable program to gain income during those periods when the assets and staff cannot be used to their full capacity. Some examples include</p>	<p>4) The Sale of Items that Promote the Charity or Its Objects</p> <p>These are sales that are intended to advertise, promote, or symbolize the charity or its objects. This promotional purpose can be present by virtue of its design, packaging, or</p>



universities renting out unused classrooms during the summer months.

included materials. Examples include pens, t-shirts and cookies with the logo of the charity.

The business activities must always remain subordinate to the charitable purpose. This means that when looking at the charity's operations as a whole, the business activity can only receive a minor portion of the charity's attention and resources. Any business activity must be integrated into the charity's operations, and not act as a self-contained unit. Charities must ensure that their charitable goal remains the main focus of the organization and that it continues to dominate decision-making. This exclusively charitable purpose means that no elements of private benefit can enter its operations.

8.3.2. Not-For-Profit Corporations with Social Purpose

Despite their name, not-for profit corporations can engage in activities that result in income or profit. They can, for example, own businesses, such as Habitat for Humanity's ReStore retail outlets, which sells building materials. This revenue, however, can only be used in carrying out the corporation's social goals and objectives. On the continuum of social enterprises, not-for-profit corporations is one of the structures that falls closer to the social goal than the commercial goal.

8.3.3. Co-operative Corporations with Social Purpose

Co-operatives fall approximately in the middle of the spectrum, placing somewhat equal weight on achieving its social aims and its commercial goals. Traditionally, the co-operative form of business organization has been a popular one for social enterprises due to its democratic membership structure, usually one member-one vote.

In Canada, co-operatives must incorporate either federally or provincially. The most common types are consumer co-ops, which provide products or services to their members, producer co-ops, which process and market good or services produced by their members, worker co-ops, which provide employment for their members, and multi-stakeholder co-ops, which serve the needs of different stakeholder groups, typically in health and home care enterprises.

The three characteristics shared by all co-operatives are that firstly, a co-operative is owned jointly by the members who use its service. Secondly, it is democratically controlled. In contrast with the typical corporation control structure, in which each share gives a vote, in a co-operative each member gets one vote. Thirdly, any profits belong to the members. These members can decide whether these should be distributed to the members or reinvested into the company.

8.3.4. Business Corporations with Social Purpose

Some businesses may wish to operate to serve a social purpose but decide to incorporate as a for-profit corporation instead of a not-for-profit organization. These corporations do not receive the tax exemption granted to not-for-profit organizations, but they are not obligated to reinvest

their profits in the company. For-profit corporations can raise capital more easily which can help the entity grow and continue to achieve its social purpose.

8.3.5. Socially Responsible Business Corporations

In recent years, the concept of Corporate Social Responsibility (“CSR”) has gained momentum. CSR is defined as the voluntary activities undertaken by a company, over and above legal requirements, to operate in an economically, socially and environmentally sustainable manner.

These are for-profit businesses whose primary goal remains to further their commercial operations, but who go out of their way to consider and accommodate the interests of broader stakeholders. Some examples include ensuring all products and ingredients are ethically sourced, and optimizing operations to protect and sustain the environment.

8.3.6. Business Corporations Donating to Charity

Many corporations donate significant sums to charitable organizations, or fund charitable projects. This business structure’s primary aim is to make profit, but by donating money they are able to give back to the community and keep social stakeholders’ interests in mind.

8.4. Choosing a Type of Social Enterprise

There are advantages and disadvantages to each structure. Entities like charities and not-for-profit corporations enjoy considerable tax benefits, but also face significant restrictions on how they can operate their business and handle the money they earn. More commercially-minded enterprises face fewer restrictions and can raise capital much more easily, but their operations are subject to the influence of their various stakeholders, which can push the business further and further from its social aim.

8.4.1. Ownership Structure

When choosing a business type, consider what type of ownership structure best reflects your project. Social enterprises can be sole proprietorships, partnerships or corporations. Incorporation offers many benefits such as limited liability and continued existence, while unincorporated entities offer fewer formalities and increased flexibility at a lower cost. The other Playbooks in this series provide information on how these structures differ from one another and the advantages and disadvantages they offer.

8.4.2. Goals of the Enterprise

Is the business’s primary goal to earn profit, or to further a social goal? This Playbook has outlined several business structures. Determine how central the social aim is to the business and choose a business structure that reflects this. In this determination, consider the financial needs of the business. Not-for-profit organizations have more difficulty earning capital investments from outside investors, but they receive a tax-exempt status that exempts them from paying taxes under the *Income Tax Act*. Consider how the costs and benefits weight in your situation.



8.5. Conclusion

Social enterprises can be a great way to further a social cause or aim while still making profit. It is a versatile concept that can take a variety of forms to adapt to your business. When choosing your organization's structure, consider carefully its aims and its needs to ensure you choose the structure that will suit it best.

Please contact the QBLC should you require any assistance in starting a social enterprise.