

2012 NATIONAL CHARITY LAW SYMPOSIUM

May 4, 2012

**NEW INELIGIBILITY REQUIREMENTS FOR DIRECTORS, OFFICERS
AND STAFF OF REGISTERED CHARITIES**

**Karen J. Cooper
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INTRODUCTION

Under the rubric of “Strengthening the Charitable Sector,” the 2011 federal Budget Plan,¹ which received Royal Assent on December 15, 2011,² contained several provisions that will have a substantial impact on the governance of registered charities and registered Canadian amateur athletic associations (RCAAs). These provisions introduced a number of amendments to the *Income Tax Act*³ (ITA), the principal regulatory regime affecting registered charities. One of the most significant of these amendments is the introduction of provisions rendering certain individuals ineligible to serve on the board of or in a senior capacity within a registered charity.

The “ineligible individual” provisions came into force January 1, 2012, but the consequences of their implementation have yet to be felt in the charitable sector. In light of the significance and the uncertainty with respect to practical implementation of the amendments, the purpose of this paper is to promote discussion about the provisions and their potential

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¹ Minister of Finance, *The Next Phase of Canada’s Economic Action Plan: A Low-Tax Plan for Jobs and Growth* (Ottawa: Public Works and Government Services Canada, 2011) [Budget Plan]

² Bill C-13, Keeping Canada’s Economy and Jobs Growing Act, 1st Sess, 41st Parliament, 2011.

³ RSC 1985, c 1 (5th Supp) [ITA].

consequences. In order to achieve this, we first provide an overview of the “ineligible individual” provisions in Canada followed by a description and discussion of parallel provisions that have been recently implemented in both the United Kingdom and New Zealand. Finally, we examine the provisions from a constitutional law perspective.

Because the intent of the paper is to provide a brief overview of the issues to promote discussion, this paper will necessarily have certain limitations. Firstly, while the provisions in question will also affect RCAAAs, for the purpose of simplicity and cross-jurisdictional comparison, the implications of the provisions for RCAAAs will not be addressed specifically. Secondly, though we will be addressing constitutional issues, this is as a non-expert discussion with a view to simply raising legal issues and suggesting some questions that could be asked of constitutional law scholars.

THE “INELIGIBLE INDIVIDUAL” PROVISIONS

(a) History of the Provisions

Canadian charities are governed by several different statutes, which vary depending on the province in which the charity operates, whether the charity is incorporated, and if so, whether the charity is incorporated federally or provincially. However, regardless of location or fact of incorporation, every registered charity in Canada operates as a charity by virtue of the ITA.⁴ Though other statutes, such as Ontario’s *Charities Accounting Act*,⁵ affect the operation of charities, the ITA is the single instrument that grants registered charities the authority to issue tax

⁴ Note that though there is a distinction between a “charity” at common law and a “registered charity” under the ITA, for the purposes of this paper, any reference to “charity” means “registered charity”.

⁵ RSO 1990, c C10.

receipts for donations and exempts them from income tax.⁶ The granting of this receipting authority is achieved through the registration process and ongoing registration requirements, which are administered by the Canada Revenue Agency (CRA). CRA similarly has the ability to suspend a charity's receipting authority or to revoke a charity's charitable registration entirely. As a result of the importance of donations as a source of revenue for most charities, CRA, through the ITA, effectively regulates the operation of charities in Canada.

The "ineligible individual" provisions came as a result of concerns from CRA, as expressed by the Department of Finance in the Budget Plan, that it had no authority to refuse applications for charitable status based on the identity of the applicant for charitable status. That is, CRA did not have the ability to refuse an application for charitable registration from individuals who had previously been involved with charities that had their charitable status revoked for serious non-compliance or from individuals with criminal records for offences relating to a breach of public trust, like fraud or misappropriation.⁷ The new provisions are intended to provide CRA with the necessary authority to withhold or remove charitable status in situations where such potential risk factors for abuse are present.

(b) Description of the "Ineligible Individual" Provisions

Generally, the "ineligible individual" provisions will enable CRA to withhold or revoke the charitable status of organizations that have ineligible individuals on the board of directors or serving as a senior manager, in order to better "safeguard charitable assets."⁸ These new provisions were effected through amendments to sections 149.1(1), 149.1(4.1), 149.1(25) and

⁶ ITA ss. 110.1 and 118.2 and 149(1)(f).

⁷ Budget Plan, *supra* note 1 at 296.

⁸ Budget Plan, *supra* note 1; *CRA 2011 Budget News*, online: Canada Revenue Agency <<http://www.cra-arc.gc.ca/gncy/bdgt/2011/menu-eng.html>>.

188.2(2) of the ITA, which provide that CRA has the discretion to refuse⁹ or revoke¹⁰ the charity's charitable status or to suspend the charity's authority to issue charitable receipts¹¹ if an "ineligible individual" is a member of the board of directors, a trustee, officer or equivalent official, or any individual who otherwise controls or manages the operation of the charity.

Ineligible individuals include persons who:

- have been convicted of a "relevant criminal offence" for which a pardon has not been granted – such offences include both offences under Canadian criminal law and similar offences outside Canada relating to financial dishonesty, including tax evasion, theft, fraud or any other criminal offence that is relevant to the operation of the charity;
- have been convicted of a non-criminal "relevant offence" in Canada or outside Canada within the past five years – such offences relate to financial dishonesty, such as offences under fundraising legislation, consumer protection legislation or securities legislation, as well as any other offence that is relevant to the operation of the charity;
- have been a member of the board of directors, a trustee, officer, or an individual who otherwise controlled or managed the operation of a charity or RCAA during a period in which the organization engaged in conduct that constituted a serious breach of the requirements for registration, for which the charity or RCAA had its registration revoked within the past five years – such conduct includes improper receipting arrangements, abusive tax shelters, or providing undue private benefit to directors; or

⁹ *ITA*, *supra* note 3 at s.149.1(25)(a) and (b).

¹⁰ *Ibid* at s.149.1(4.1)(e).

¹¹ *Ibid* at s.188.2(2)(d).

- have been, at any time, a promoter of a gifting arrangement or other tax shelter in which a charity participated and the registration the charity has been revoked within the past five years for reasons that were related to participation in the tax shelter.¹²

The CRA has clarified, however, that a charity will not necessarily have its charitable status refused or revoked simply because CRA has determined that an “ineligible individual” is on the board or manages the operation of the organization. CRA has indicated that a charity will be given an opportunity to address any concerns CRA may have with an ineligible individual. The charity might put in place necessary safeguards over financial management, remove the individual in question or explain why it is appropriate for the individual to hold the position in question. CRA has also indicated that it will be developing detailed administrative guidance on how it will use these new provisions, but this guidance has not yet been made public.¹³

(c) Implications of the “Ineligible Individual” Provisions

The “ineligible individual” provisions will potentially have extremely far-reaching and unintended consequences. Consider the following example:

- Charity X has a 25 member board of directors
- Carter is a director on the board of Charity X and has been since 2010
- Carter was also employed as the manager of another charity, Charity Y, in 2002-2003
- Charity Y is audited in 2005 in respect of the 2002 and 2003 taxation years

¹² *Ibid* note 3 at s.149.1(1).

¹³ Safeguarding Charitable Assets through Good Governance: Eligibility Requirements for Individuals who are Directors or Control or Manage Registered Charities and Registered Canadian Amateur Athletic Associations or Applicants for such Status, online: Canada Revenue Agency <<http://www.cra-arc.gc.ca/gncy/bdgt/2011/qa22-eng.html>>.

- In February 2007, Charity Y loses its status for substantial non-compliance, as a result of the imprudent actions of Charity Y's board of directors, actions to which Carter strongly objected and that ultimately caused Carter to resign in 2002
- Because Carter managed a charity that lost its status in 2006 for substantial non-compliance that occurred in 2002, Carter is now an "ineligible individual"
- He is an ineligible individual for the period of 5 years from the date of revocation in February 2007
- The charitable status of Charity X could now potentially be revoked because an ineligible individual was/is on its board of directors

It is not clear what sort of due diligence will be required by a charity to ensure that an "ineligible individual" does not become involved or continue to be involved in its management. Though a charity will not be required to conduct background checks,¹⁴ if the charity wanted to do so from a risk management perspective and out of an abundance of caution, the information required to independently assess whether an individual is "ineligible" may not be publicly or easily available. For instance, there are challenges in discovering whether an individual has been convicted of a criminal offence outside Canada or whether an individual has been convicted of a relevant non-criminal offence that is not provided in publicly available databases in Canada and abroad.

Perhaps an even greater challenge will be learning the names of Board members and like officials of charities and RCAAAs, during a period in which the organization "engaged in conduct that can reasonably be considered to have constituted a serious breach of the

¹⁴ Budget Plan, *supra* note 1 at 298.

requirements for registration,”¹⁵ in order to assess whether an individual is ineligible. While it is possible to ascertain how many and which charities have had their charitable status revoked “for cause”, within a particular time period, from the CRA website¹⁶, and the directors listed on each charity’s T3010 are provided, this is hardly an effective or reliable method of determining a list of potentially “ineligible” individuals. This is primarily problematic because there is no way to search all directors during this period so a charity-by-charity search would be required, for the five years prior to the day on which an individual’s eligibility is being ascertained.

Practically speaking, if the eligibility of an individual is being determined on January 1, 2012, this would require a search of the 213 charities that had their registration revoked since January 1, 2007.¹⁷ Once a charity is able to determine that an individual was a director of a charity that had its status revoked within the past five years, it still would have to determine whether that individual was a director during the period of time in which the charity engaged in the problematic conduct. Further complicating the matter is that the names of senior staff “who otherwise controlled or managed the operation” of a revoked charity rarely appear in a T3010. In fact, it is likely that the availability of much of this information is solely under CRA’s control. As such, even if it were possible to determine whether an individual was previously a director of a charity whose registration was revoked for cause, it would still not be possible if the individual was an employee of such a charity during this same period.

Additional consequences of the “ineligible individual” provisions are their application to paid staff. As senior employees would likely be included in the category of individuals who control or manage a charity, charities will certainly have to be concerned with whether any of

¹⁵ *ITA*, *supra* note 3 at s.149.1(1) (definition of “ineligible individual”).

¹⁶ See <http://www.cra-arc.gc.ca/chrts-gvng/lstngs/menu-eng.html>.

¹⁷ Canada Revenue Agency, *Charities Listings*, online: CRA < <http://www.cra-arc.gc.ca/chrts-gvng/lstngs/menu-eng.html>>.

their staff are “ineligible individuals”. Assuming an employee’s ineligibility could be ascertained, the charity is then faced with the challenge of how to respond. Employees cannot necessarily be terminated simply because they are ineligible. Employees’ rights under common law, employment standards and human rights legislation will have to be respected in dealing with the “ineligible individual” issue and may very well lead to a substantial financial cost for termination. Though it may be possible to implement a screening process for employee ineligibility during the hiring process, charities will still have to respect human rights legislation in doing so.

Given the above discussion, it is clear that most of the necessary information on “ineligible individuals” is likely only available to CRA so consideration should be given to imposing the onus on CRA to maintain a list of “ineligible individuals”. Such a list may already exist internally for the purpose of enforcing these provisions, however, it is unlikely that such a list could be made publicly available because of privacy and other legal concerns. Therefore, the onus is shifted to charities to comply in a situation where it is virtually impossible to ensure compliance because the necessary information is not available.

At best, charities will be required to implement some sort of screening mechanism in determining who will be asked to serve and/or can continue to serve on boards of directors or as senior staff. Charities will also have to consider how to deal with issues involving current directors, including whether, how and how often they should be screened. For instance, charities may want to develop a parallel questionnaire for current board members and require that the questionnaire be completed on an annual basis or as a condition of re-election to the Board. Charities will also want to consider how current board members are to be removed if they do become “ineligible individuals.” Typically, only the members of the charity are able to remove directors from the board.

Further, whatever due diligence a charity undertakes may be insufficient, because if CRA decides to revoke charitable status on the basis of the involvement of an “ineligible individual”, there is no express due diligence defence available in the legislation.

CONTEXT FROM THE UNITED KINGDOM AND NEW ZEALAND

(a) New Zealand

The charitable registration system in New Zealand is still fairly new. The relevant legislation, the *Charities Act 2005*,¹⁸ only came into force in 2005 and the registration of charities only began in 2007 when the register was begun.¹⁹ The *Charities Act* established the Charities Commission, which creates and maintains the registration and monitoring system for charities.²⁰ Similar to the Canadian system, registration generally entitles a charity to be exempted from paying income tax; however, it does not necessarily entitle them to issue charitable donation tax receipts. To be entitled to issue donation tax receipts, charities must be separately approved for donee status by New Zealand Inland Revenue, which considers whether the charity meets the requirements for donee status in the *Income Tax Act 2007*.²¹ In order to be granted donee status, an organization must use its funds primarily for charitable, benevolent, philanthropic or cultural purposes, it must generally use its funds in New Zealand and the organization must not provide any private benefits to members.²² Interestingly, benevolent or

¹⁸ (NZ), 2005/39 [*Charities Act*].

¹⁹ Charities Commission, *Guide to the Charities Act*, (2012), online: <
<http://www.charities.govt.nz/assets/docs/information-sheets/guide-to-the-charities-act.pdf>>.

²⁰ *Ibid.*

²¹ (NZ), 2007/97.

²² Inland Revenue, *Charitable Organizations and Donee Organizations*, IR 255 (April 2012), online: <
<http://www.ird.govt.nz/forms-guides/title/forms-c/ir255-guide-charitable-organisations.html?id=righttabs>>.

philanthropic organizations need not be charitable at law in order to qualify as donees; and organizations that are charitable at law may not necessarily qualify as donees.²³

Though registered charities are not automatically considered donees, Inland Revenue has indicated that it will automatically consider granting donee status to registered charities that indicated on their applications for registration that donations are a part of their income, without the need for a separate application to Inland Revenue.²⁴ Further, Inland Revenue has indicated that so long as the registered charity will be spending its funds within New Zealand, donee status for charities will be granted.²⁵ Therefore, as a practical matter, whether or not a charity is registered significantly impacts its ability to issue charitable donation tax receipts.

Although the *Charities Act* has recently undergone some amendments, since its inception it has contained provisions that are similar to Canada's "ineligible individual" provisions. Prior to the amendments, these provisions only applied to members of the board of directors or governing body. However, since the enactment of the *Charities Amendment Act 2012*²⁶ in February of 2012 the provisions now apply to all members of a charity's highest governing body as well as individuals in a position to have significant influence over a charity's management or administration, including staff and volunteers.²⁷

The comparable New Zealand provisions, found at section 16 of the *Charities Act*, specify the qualifications for "officers" of charities. Subsection 16(2) provides that the following persons are disqualified from being officers:

²³ *Ibid.*

²⁴ Inland Revenue, *Operational Statement: Interaction of Tax and Charities Rules, Covering Tax Exemption and Donee Status*, OS 06/02 (December 2006), at para 28, online: < <http://www.ird.govt.nz/technical-tax/op-statements/os-interaction-tax-charities-rules.html>>.

²⁵ *Ibid.*

²⁶ (NZ), 2012/4.

²⁷ Charities Commission, *Recent Changes to the Charities Act*, online:< <http://www.charities.govt.nz/news/charities-act-changes/>>.

- (a) An individual who is an undischarged bankrupt;
- (b) An individual who is under the age of 16 years;
- (c) An individual who, or a body corporate that, has been convicted of a crime involving dishonesty (within the meaning of section 2(1) of the *Crimes Act 1961*) and has been sentenced for that crime within the last 7 years;
- (d) An individual who is prohibited from being a director or promoter of, or being concerned or taking part in the management of, an incorporated or unincorporated body under the *Companies Act 1993*, the *Securities Act 1978*, the *Securities Markets Act 1988*, or the *Takeovers Act 1993*;
- (e) An individual who, or a body corporate that, is disqualified from being an officer of a charitable entity under section 31(4);
- (f) An individual who is subject to a property order made under the *Protection of Personal and Property Rights Act 1988*, or whose property is managed by a trustee corporation under section 32 of that Act;
- (g) A body corporate that is being wound up, is in liquidation or receivership, or is subject to statutory management under the *Corporations (Investigation and Management) Act 1989*; and
- (h) In relation to any particular entity, an individual who, or a body corporate that, does not comply with any qualifications for officers contained in the rules of that entity.²⁸

In relation to paragraph (e) above, an individual or body corporate is disqualified under subsection 31(4) if a charity has been deregistered and an officer is ordered by the Charities Commission to not be an officer of a charity for a period not exceeding five years. As noted above, the following individuals are considered to be “officers”, in relation to a charity:

- i. A member of the board or governing body of the entity if it has a board or governing body; and
- ii. A person occupying a position in the entity that allows the person to exercise significant influence over the management or administration of the entity (for example, a treasurer or a chief executive).²⁹

In summary, the New Zealand provisions that are comparable to the Canadian provisions provide that a person is not eligible to hold a position of substantial control within a charity if the

²⁸ *Charities Act*, *supra* note 18 at s.16.

²⁹ *Ibid* at s. 4(1).

person has been convicted of a crime involving dishonesty and has been sentenced for that crime within the last 7 years, as provided in paragraph (c) of subsection 16(2) or if the person has been disqualified as an officer by the charities commission, as provided under paragraph (e) of subsection 16(2). It is noteworthy, however, that the Charities Commission is given the power to waive an officer's disqualification under subsection 16(4). Under subsection 17(b) of the *Charities Act* a charity must certify that all of its officers are qualified under section 16 of the Act in order to obtain charitable registration. Further, paragraph 40(1)(ca) provides that charities must notify the Charities Commission if an officer becomes disqualified. The charity would then have to take immediate action because a registered charity will cease to qualify for registration if a disqualified officer is in place.³⁰

(b) The United Kingdom

Similar to the tax benefits for charities in Canada, tax relief for charities in the UK is achieved under the *Finance Act 2010*³¹ and is administered by Her Majesty's Revenue and Customs (HMRC). However, comparable to New Zealand, UK charities are not regulated by the tax authority, but instead by the Charity Commission, which operates under the *Charities Act 2006*.³² The Charity Commission maintains the charity register and regulates the conduct charities. The Commission does not have the power investigate tax matters, but if such matters arise, it will instead report them to the appropriate authorities. However, if other regulators are investigating such matters, and it appears that there has been misconduct or mismanagement in

³⁰ Charities Commission, *Disqualified Officers: What you Should do if One of your Officers Becomes Disqualified under the Charities Act 2005*, (February 2012) at 2, online: <<http://www.charities.govt.nz/news/information-sheets/disqualified-officers/>>.

³¹ (UK), c 13 sched 6 [*Finance Act*].

³² (UK), c 50 [*Charities Act*].

the administration of the charity, the Charity Commission is able to use its temporary protective powers to safeguard charitable assets.³³

The UK provisions that parallel Canada's "ineligible individual" provisions are contained in the definition of the term "charity" in the *Finance Act*, which provides that, in order to be a charity, a body must meet the management condition provided in paragraph 4 of the Act.³⁴ The management condition at paragraph 4 provides as follows:

Management condition

- (1) A body of persons or trust meets the management condition if its managers are **fit and proper persons** to be managers of the body or trust.
- (2) In this paragraph "managers", in relation to a body of persons or trust, means the persons having the general control and management of the administration of the body or trust.

Essentially, whether an organization is at risk of not meeting the definition of a charity or of losing its entitlement to charity tax relief depends on whether its managers are deemed to be "fit and proper". Interestingly, the term "fit and proper" is not defined in the legislation. However, HMRC has released some guidance on how it will apply the "fit and proper person" test.³⁵ Though HMRC describes its own guidance as detailed, this guidance is somewhat vague in that it does not provide the test that it will apply in order to determine if a manager is "fit and proper". Further, though the HMRC provides a list of factors that may cause it to determine that a person is not "fit and proper", it also indicates that there may be other (unlisted) factors that may lead it to its decision. However, the guidance lists the following factors that may lead HMRC to determine that a manager is not "fit and proper":

³³ Charity Commission, *Statutory Inquiries into Charities: Guidance for Charities and their Advisors*, CC46 (February 2012) at pp 6-8, online: <<http://www.charitycommission.gov.uk/publications/cc46.aspx>>.

³⁴ *Ibid* at sched 6, part I, s 1(1)(d).

³⁵ Her Majesty's Revenue and Customs, *Detailed Guidance on the Fit and Proper Persons Test*, [detailed guidance] online: <<http://www.hmrc.gov.uk/charities/guidance-notes/chapter2/fp-persons-test.htm>>.

- Individuals with a history of tax fraud;
- Individuals with a history of other fraudulent behaviour including misrepresentation and/or identity theft;
- Individuals for whom HMRC has knowledge of involvement in attacks against or abuse of the tax repayment systems; and
- Individuals who are barred from acting as a charity trustee by a charity regulator or court, or being disqualified from acting as a company director.³⁶

HMRC does however provide some firm guidance by indicating that if the charity regulator determines that an individual is not suitable to be the trustee of a charity, this person will not be “fit and proper” for the purposes of HMRC. However, a regulator’s determination that a person is suitable does not necessarily mean that HMRC will conclude that the trustee is fit and proper. Nevertheless, the HMRC guidance indicates that it starts from the assumption that all managers appointed by charities are fit and proper unless there is evidence to the contrary.³⁷

Similar to New Zealand, the “fit and proper” test applies to all persons who have general control and management of a charity. As such, all trustees and directors must be fit and proper, as well as “certain employees who are able to determine how a significant proportion of the charity’s funds are spent”.³⁸ HMRC indicates that the position that a person holds is extremely significant because “those with greater control over how the charity tax reliefs are claimed, processed and used will clearly present a greater risk than those with no such control.”³⁹

As a corollary, a person who has no control over the spending of charitable funds, even if the person is not “fit and proper”, will likely not qualify as a manager for the purpose of the test.

³⁶ *Ibid.*

³⁷ *Ibid.*

³⁸ *Ibid.*

³⁹ *Ibid.*

HMRC provides the following example relating to charities concerned with the rehabilitation of offenders who knowingly appoint ex-offenders to management positions within the charity:

If the person might not be considered to be a fit and proper person but is not able to exert control over the charity's finances and tax affairs then HMRC will consider that a person cannot affect the charitable purposes of the charity and the charity would be treated as meeting the management condition. For example this would happen if the person was on the management committee but not on the finance committee of the charity, had no access to charity funds and could not authorise expenditure without the approval of the full management committee and was not in a position to otherwise unduly influence financial decision making.⁴⁰

In addition, the HMRC also has the discretion to treat the “management condition” as being met, even where one or more managers of a charity are not “fit and proper”, in circumstances where it is just and reasonable to do so. This may occur, for instance, in situations where a charity unknowingly appoints a person who is not “fit and proper” to a management position. In such situations, if the charity moves the individual to another role that is not considered management for the purposes of this provision, or if the charity implements close supervision of the person in relation to his or her financial activities, then HMRC can choose to treat the charity as having met the “management condition”. Further, in situations where a person who is not “fit and proper” is innocently appointed to a management positions and this person misapplied charitable funds, the charity will not necessarily lose its charity tax relief. So long as the charity can show that it had taken reasonable steps to ensure that the person was “fit and proper” and so long as the charity was not a party to the wrongdoing, HMRC can use its discretion to allow the charity retain its tax position.⁴¹

⁴⁰ *Ibid.*

⁴¹ *Ibid.*

Finally, though an person may be determined by HMRC to not be “fit and proper”, there is a process for the person to seek review of this decision. Though the details of the review process are beyond the scope of this paper, it is sufficient to note that there are several levels of review available before a decision is considered final. If review is sought, the charity will only be informed of HMRC’s decision if the decision is upheld and the person will not remove him or herself from the position of manager.⁴²

A CONSTITUTIONAL LAW PERSPECTIVE

The constitutional issues that relate to the “ineligible individual” provisions arise from the *Constitution Act, 1867*.⁴³ This statute, which united the provinces under the Dominion of Canada, divides various powers between those that would be under the legislative authority of Parliament and those that would be under the authority of a province. The management of charities, likely to include the power to prescribe their governance, falls under a provincial head of power, as provided in subsection 92(7) of the *Constitution Act*:

92. In each Province the Legislature may exclusively make Laws in relation to Matters coming within the Classes of Subjects next hereinafter enumerated; that is to say,
...
 7. The Establishment, Maintenance, and Management of Hospitals, Asylums, Charities, and Eleemosynary Institutions in and for the Province, other than Marine Hospitals.⁴⁴

However, the provisions that are the subject of this discussion are implemented by the federal government through the exercise of its power over taxation under subsection 91(3). This

⁴² *Ibid.*

⁴³ (UK), 30 & 31 Vict, c 3, reprinted in RSC 1985, App II, No 5.

⁴⁴ *Ibid.*

section provides that the legislative authority of Parliament extends to “...the raising of Money by any Mode or System of Taxation.”⁴⁵ It is therefore uncertain whether the federal government is validly exercising its power of taxation or whether it has overstepped its authority by prescribing rules regarding the management of charities that are outside of its jurisdiction. If the courts were to find the latter, the provisions would be declared *ultra vires* and would therefore be invalid.

From the perspective of a non-expert, it would seem that the Canadian courts have been dealing with questions of the constitutionality of legislation in relation to the division of powers since 1867 and that they have ironed out a particular analysis that should be undertaken to arrive at a resolution. In order to determine the constitutionality of legislative provisions in such situations, the analysis begins with characterizing the provisions as either valid or invalid by undertaking a “pith and substance” analysis.⁴⁶ This initial analysis is an examination of the “true nature” of the provisions in order to determine the “matter to which it essential relates.”⁴⁷ If the pith and substance of the provisions relates to a matter that is within the jurisdiction of the government who enacted it, then the provisions are valid. If they relate to a matter that is outside the jurisdiction of that government, then the provisions are invalid. The pith and substance of provisions is determined by examining both the purposes and effects of the provisions in question. In examining the purpose of the provisions, the objective is to ascertain the true purpose and not simply its apparent or stated purpose. In examining the effects of the provisions, the object is to determine their legal effect.⁴⁸

⁴⁵ *Ibid.*

⁴⁶ *Canadian Western Bank v Alberta*, 2007 SCC 32 at para 25 [CWB].

⁴⁷ *Ibid* at para 26.

⁴⁸ *Ibid* at para 27.

With respect to the “ineligible individual” provisions in question, their pith of substance depends on whether provisions that prescribe the qualifications of individuals who can direct or manage charities relates to the management and regulation of charities, under the power of the province, or taxation, under the power of Parliament. An examination of both the purpose and effect of the provisions results in the likely conclusion that the provisions relate primarily to the management and regulation of charities – CRA and the Department of Finance are seeking to control the characteristics of those that control and manage charities. Jurisprudence has indicated that in order to assess the purpose of a law, intrinsic evidence, such as the legislation’s purpose clauses or preamble can be used.⁴⁹ A brief review of the 2011 federal Budget Plan reveals the stated purpose of the “ineligible individual” provisions.⁵⁰ This document describes the impugned provisions and the need for such provisions under the heading “Safeguard Charitable Assets through Good Governance.”⁵¹ The positioning of the document in this manner clearly implies that the purpose of such provisions is indeed to safeguard charitable assets. While this is an important purpose, it is not a purpose that relates to taxation in the sense of raising revenue, but instead it relates more properly to the management and regulation of charities.

An examination of the effects of the impugned provisions is even more revealing of a pith and substance that relates to the provincial head of power over the management of charities. The effect of the provisions is clearly regulatory in that charities risk losing their status if they do not abide by requirements relating to director and manager eligibility. While the power to register and deregister charities falls under the purview of the federal government because it

⁴⁹ *CWB*, *supra* note 46 at 27.

⁵⁰ Budget Plan, *supra* note 1.

⁵¹ *Ibid* at 296.

directly relates to the taxation of charities and their donors, it does not follow that such a power can be used to prescribe the unrelated internal governance of charities. The distinction between taxation and regulation was recognized by the Supreme Court of Canada in *Attorney-General for Alberta v Attorney-General for Canada*.⁵² In that decision, the Court held that the effects of provincial taxation on banks were so great that they revealed an attempt to regulate and control the banks, a matter under a federal head of power, instead of an attempt to raise revenue through taxation, which, in this case, was a provincial power.⁵³

Though it appears that both the purpose and effects of the impugned provisions indicate that their pith and substance is the management of charities and not taxation, it is important to note that recent jurisprudence, *International Pentecostal Ministry v Canada (Minister of National Revenue)*,⁵⁴ from the Federal Court of Appeal addressed the question of whether the registration and deregistration of charities under the ITA relates to the regulation of charities or taxation.⁵⁵ The court held that the registration and deregistration provisions related to federal taxation as “both the advantages of registration and the drawbacks of revocation relate solely to the tax treatment of charities and their donors. They do not impermissibly affect the affairs of charities in any other way, nor do they impede provinces from otherwise regulating charities.”⁵⁶ However, this decision could be distinguished from the present discussion on the basis that the “ineligible individual” provisions would not be challenged on the basis of the power to register and revoke charities, but on the basis of the use of the registration process to achieve the effect of prescribing the qualifications of the directors and managers of charities.

⁵² [1939] AC 117.

⁵³ Note that the *Constitution Act, 1867* provides that both the provinces and the federal government can raise money through taxation.

⁵⁴ 2010 FCA 51.

⁵⁵ *Ibid* at para 7.

⁵⁶ *Ibid* at para 8.

Notwithstanding that the pith and substance analysis suggests that the “ineligible individual” provisions may be *ultra vires* the federal government, the extent of the encroachment or overflow from one jurisdiction to the other must also be examined.⁵⁷ This examination is required because of the doctrine of constitutional analysis known as the “ancillary powers doctrine” which provides that “legislative provisions which, in pith and substance, fall outside the jurisdiction of the government that enacted them, may be upheld on the basis of their connection to a valid legislative scheme.”⁵⁸ In order for provisions to be upheld on this basis, the relationship between the severity of the intrusion on the other level of government and the importance of the impugned provisions within the statute must be examined.⁵⁹ The more a provision intrudes on the other legislator’s power, the more necessary the provision must be. Where an incursion is less serious, the provision will have to have a rational and functional connection to the statute and where an incursion is more substantial, the provision will have to be necessarily incidental to the statute.⁶⁰

The Supreme Court of Canada addressed the non-exhaustive factors that should be considered in determining the severity of intrusion in *General Motors of Canada Ltd v City National Leasing*.⁶¹ These factors are: the scope of the heads of power in play; the nature of the impugned provision; and the enacting bodies history of legislating on the matter in question.⁶² With respect to the scope of the heads of power in play, the intrusion on the powers of the other level of government is more serious where the head of power intruded on is a narrow one

⁵⁷ *Reference re Assisted Human Reproduction Act*, 2010 SCC 61 at 189 [Reference].

⁵⁸ *Ibid* at para 126.

⁵⁹ *Ibid* at para 192.

⁶⁰ *Ibid* at para 127.

⁶¹ [1989] 1 SCR 641 [*General Motors*].

⁶² *Ibid*.

“because it threatens to obliterate that head of power”.⁶³ Applying this to the matter at hand, the intrusion would be considered more serious because the provincial head of power, in dealing primarily with charitable institutions, is quite narrow, particularly when compared to other broad powers like the provincial power over property and civil rights, provided under subsection 92(13) of the *Constitution Act 1867*.⁶⁴ Indeed, the incursion on the power of the province to establish, maintain and manage charities is arguably so significant that the “ineligible individual” provisions could potentially threaten the province’s ability to exercise its power with respect to charities entirely. In this regard, it is particularly noteworthy that Ontario is currently the only province engaged in any significant exercise of this power in regards to charities generally and that it has not seen fit to prescribe any rules regarding the qualifications of individuals that control or manage charities beyond the general requirements found in corporate law applicable to all directors.

With respect to the second factor, the nature of the impugned provision, intrusions on the powers of the other level of government are considered less serious where the impugned provisions are of limited scope, do not create rights and when the provision is meant to coexist or supplement legislation at the other level of government.⁶⁵ Applying this factor to the incursion of the “ineligible individual” provisions, the intrusion may again be considered to be more serious even though it does not create substantive rights. The incursion may be considered serious under this factor because the provisions are of such a significant scope that it does not appear that they are meant to supplement provincial legislation, but are instead meant to replace it. In fact, there are no indications in the impugned provisions that there is any intention for them to operate in

⁶³ *Reference, supra* note 57 at 129.

⁶⁴ *Ibid* at para 134.

⁶⁵ *Ibid* at para 130.

conjunction or addition to any provincial legislation. To the contrary, the significant impact of the provisions on the operation of charities, in that registration can be refused or revoked if governance conditions are not met, suggest that the provisions are intended to operate independent of and primary to any other charities regulation.

Finally, with respect to the third factor, the history of legislating on the matter in question, a history of the enacting body legislating in the area will suggest that the intrusion is less serious.⁶⁶ Though Parliament has a history of legislating in the area of charities through taxation, it has historically done so to a less intrusive extent. The “ineligible individual” provisions represent a novel area of legislation with respect to charities that is primarily concerned with the internal governance of, and employment within, charities.

Given the above discussion of the severity of intrusion of the impugned provisions into the powers of the provincial government, it appears possible that a court could determine the incursion to be substantial. A court would then be required to consider whether the provisions are necessarily incidental to the ITA. In order to be considered necessarily incidental, and thus a constitutionally valid intrusion on the province’s power, the court would assess the degree of integration of the impugned provision. This assessment was addressed by the Supreme Court in *Reference re Goods and Services Tax*⁶⁷ as follows: “in substance what is required is a high degree of integration between a scheme enacted pursuant to a valid federal objective, and those portions of the scheme which impinge upon provincial jurisdiction.”⁶⁸ As the ITA is a statute designed to raise money through taxation, it seems unlikely that the “ineligible individual” provisions regulating the governance or charities are necessarily incidental to that statute. This should be

⁶⁶ *Ibid* at para 131.

⁶⁷ [1992] 2 SCR 445.

⁶⁸ *Ibid* at 31.

distinguished from the general power to register and deregister charities which would likely be considered necessarily incidental to the issuance of tax credits, deductions and exemptions under the ITA.

CONCLUSION

The new “ineligible individual” provisions create another burden on charities that is not imposed upon any other private entity and seems far beyond the federal government’s jurisdiction over taxation. This additional burden appears to have been justified on the basis that charities are quasi-public entities and should be held to higher standard because they are supported by public funds, both through individual donations and as a result of the government forgoing taxes through tax credits, deductions and exemptions.⁶⁹ However laudable this goal may be, the means through which the government seeks to achieve it may not be justified. As discussed above these provisions introduce substantial risks for charities who now risk losing their charitable status through inadvertence. The effects of the implementation of these provisions are not yet known, however it is foreseeable that charities will now be required to undertake additional expenses to attempt to ensure that they are not governed by “ineligible individuals”. It is with no small amount irony that charities will thus be required to use their charitable assets in order to protect themselves from the risk of revocation. At the very least, charities will be required to implement some sort of screening process for current and future members of their boards of directors in order to protect themselves, which may become a disincentive for individuals to serve on the boards of charities.

⁶⁹ Budget Plan, *supra* note 1.

A review of comparable provisions in United Kingdom and New Zealand reveals that other jurisdictions have more detailed provisions than those provided under the ITA. Of particular note is the ability to have a decision of director/manager ineligibility reviewed under the UK system. However, the UK and New Zealand provisions are not without their critics with respect to the expense that will be incurred by the charities and the necessity of such provisions.⁷⁰ Notwithstanding the increasing adoption of governance provisions in commonwealth countries, it remains to be seen whether the ends justify the means.

⁷⁰ David Ainsworth, "Campaign Against the 'Fit and Proper Person' Test", *Third Sector* (10 May 2010) online: ThirdSector <[http:// www.thirdsector.co.uk](http://www.thirdsector.co.uk)>.