
FEDERAL BUDGET 2015: IMPACT ON CHARITIES

*By Ryan M. Prendergast, Linsey E.C. Rains and Terrance S. Carter**

A. INTRODUCTION

On April 21, 2015, Finance Minister Joe Oliver introduced the Economic Action Plan 2015 (“Budget 2015”).¹ Budget 2015 contains a number of important proposed amendments of benefit to the charitable and not-for-profit sector, which the Budget describes as “an engine of economic activity, employing some two million Canadians across the country”. These amendments include a capital gains tax exemption for individual and corporate donors upon disposition of private shares or real estate; permitting registered charities, including private foundations and registered Canadian amateur athletic associations (“RCAAs”) to invest in limited partnerships; and the introduction of the Social Finance Accelerator Initiative, a program to encourage social finance in Canada.

Although Budget 2015 contains good news for the charitable sector, it is worth noting that the Budget did not include the Stretch Tax Credit for Charitable Giving proposed by Imagine Canada, or an administrative mechanism to provide an extension of the 36-month period announced in the 2014 Federal Budget in which an estate donation can be treated as a gift in a terminal return as many in the charitable sector had hoped for. Nor was there any follow up to the 2014 Federal Budget announcement that there would be a review of the tax exemption status for non-profit organizations (“NPOs”) under subsection 149(1)(l) of the *Income Tax*

* Ryan M. Prendergast, B.A., LL.B., is an associate practicing in the area of charity and not-for-profit law. Linsey E.C. Rains, B.A., J.D. is an associate of Carters Professional Corporation, who practices charities and not-for-profit law at Carters’ Ottawa office. Terrance S. Carter, B.A., LL.B., TEP, Trade-Mark Agent, is the managing partner of Carters, and counsel to Fasken Martineau DuMoulin LLP on charitable matters. The authors would like to thank Bart Danko, B.Sc.(Hons), M.E.S., J.D., Student-at-Law, and Anna M. Du Vent, B.A., M.A., J.D., Student-at-Law, for assisting in preparing this bulletin.

¹ The full text of the Budget 2015 document can be viewed at <http://www.budget.gc.ca>.

Act (“ITA”), and most importantly, there were thankfully no new compliance requirements imposed on charities, as there have been in previous Federal Budgets.

This *Charity Law Bulletin* provides a summary and commentary of these and some of the other more significant provisions from Budget 2015 as they affect charities and NPOs.

B. SUMMARY OF 2015 BUDGET

1. Budget 2015 Implements Measures to Exempt Capital Gains on Donations of Private Shares and Real Estate

Although new tax incentives for charities were not expected from the Federal Government given its desire to introduce a balanced budget, Budget 2015 introduces some welcome exemptions for capital gains which many within the charitable sector have been advocating for since 2012.

In this regard, Budget 2015 introduces a new capital gains exemption for private shares and real estate when these assets are sold and the proceeds donated to a registered charity, subject to the anti-avoidance measures discussed below. These measures are stated in Budget 2015 as being in response to earlier recommendations made in the February 2013 Report of the Standing Committee on Finance’s study on Tax Incentives for Charitable Giving in Canada (the “Tax Incentive Study”).² In this regard, Donald K. Johnson, a prominent philanthropist, and numerous other representatives of the charitable sector, including the Canadian Association of Gift Planners (“CAGP”), argued for the implementation of the measures found in the Tax Incentive Study. In addition to his submission for the Tax Incentive Study,³ Mr. Johnson had also advocated for the implementation of the exemption from capital gains on publicly listed shares in 2006.

Budget 2015 proposes to exempt individual and corporate donors from tax on the sale of private shares or real estate to an arm’s length party if the proceeds are donated to a registered charity within 30 days

² Report of the Standing Committee on Finance, “Tax Incentives for Charitable Giving in Canada”, February 2013, 41st Parliament, 1st Session,

<http://www.parl.gc.ca/HousePublications/Publication.aspx?Language=E&Mode=1&Parl=41&Ses=1&DocId=5972482&File=0>

³ Donald K. Johnson, “Stimulating Charitable Giving While Reducing the Deficit”, submission to the House of Commons Standing Committee on Finance, Hearings on Tax Incentives for Charitable Donations,

http://www.parl.gc.ca/Content/HOC/Committee/411/FINA/WebDoc/WD5340612/411_FINA_TIFCD_Briefs%5CJohnsonDonaldKE.pdf

of the disposition. Where a portion of those proceeds is donated, the capital gains exemption would apply only to that portion.

Budget 2015 notes that certain donations of shares or real property already receive beneficial tax treatment, e.g., donations of publicly listed shares as noted above, together with donations of ecologically sensitive land and certified cultural property gifted to certain qualified donees. An issue of concern for providing beneficial tax treatment for donations of private shares or real estate may have been that valuation issues might arise in these transactions making them susceptible to tax avoidance. Such concern has been addressed by the measures proposed in Budget 2015 by making the exemption available only where:

...cash proceeds from the disposition of the private corporation shares or real estate are donated to a qualified donee within 30 days after the disposition; and

the private corporation shares or real estate are sold to a purchaser that is dealing at arm's length with both the donor and the qualified donee to which cash proceeds are donated.

As such, valuation issues on the gift are avoided by requiring that the private shares or real estate are sold and the proceeds or a portion of those proceeds are transferred to the registered charity, and that the purchaser be at arm's length from both the donor and the qualified donee. These measures are generally consistent with the recommendations made by Mr. Johnson, the CAGP, and other advocates making submissions to the House of Commons Standing Committee on Finance.

In addition, Budget 2015 proposes further anti-avoidance rules in order to address other possible opportunities for tax avoidance where, within five years after the disposition:

the donor (or a person not dealing at arm's length with the donor) directly or indirectly reacquires any property that had been sold;

in the case of shares, the donor (or a person not dealing at arm's length with the donor) acquires shares substituted for the shares that had been sold; or

in the case of shares, the shares of a corporation that had been sold are redeemed and the donor does not deal at arm's length with the corporation at the time of the redemption.

Where these rules apply, Budget 2015 indicates that the exemption from capital gains will be reversed by including the exempted amount in the income of the donor in the year of the re-acquisition by the donor or non-arm's length person, or redemption of the shares.

There remains some uncertainty concerning exactly how these rules are to apply, as the proposed implementing legislation contained in the Notice of Ways and Means Motion states only that “[t]he Act (*Income Tax Act*) is modified to give effect to the proposals relating to Donations Involving Private Corporation Shares or Real Estate described in the budget documents tabled by the Minister of Finance in the House of Commons on Budget Day.” While this budgetary hand-waving will allow the Federal Government more time to fine-tune how the ITA will be amended to implement these provisions, only the final form of the implementing legislation will detail how these provisions will be put in place.

What is interesting, though, is that Budget 2015 states that these measures, “will apply in respect of dispositions occurring after 2016.” Presumably, this wording about timing was chosen because it is more appealing than saying that this measure will have no impact until 2017 notwithstanding that the Federal Government is able to take credit for this proposed reform more than one and half years before it will be of any benefit to registered charities.

2. 2015 Budget Provides Charities with More Flexibility to Diversify through Investing in Limited Partnerships

A key measure of Budget 2015 responds to the charitable sector's requests for clarity on the issue of whether registered charities, including private foundations, can invest in limited partnerships without risking their charitable status. CRA's current position relies on partnership law and is set out in paragraph 16 of its policy statement CPS-019, *What is a Related Business?*⁴ CRA's position is that charities who become limited partners in a limited partnership are carrying on a business rather than merely making a passive investment. Two significant results of CRA's current position are that (1) the limited partnership's business must meet the definition of a related business in order for the investment to be acceptable and (2) private foundations are prohibited from making such investments because they are prohibited from carrying on any type of business under the ITA. In this regard, Budget 2015

⁴ CRA Policy Statement, CPS-019, *What is a Related Business?* (31 March 2003), online: <<http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cps/cps-019-eng.html>>.

proposes amendments to the ITA which will allow all registered charities (including private foundations) and RCAAAs to passively invest in limited partnerships.

Budget 2015 directly attributes the introduction of this measure to the Tax Incentive Study, which, in turn, refers to the early 2012 submissions of Philanthropic Foundations Canada⁵ and Community Foundations of Canada.⁶ Since then, a number of other sector representatives, including the National Charities and Not-for-Profit Law Section of the Canadian Bar Association,⁷ the Pension Investment Association of Canada and the Canadian Association of University Business Officers,⁸ have also lobbied for changes to the limited partnerships guidelines. Accordingly, the proposed ITA amendments are described in Budget 2015 as having a two-fold purpose, to enable “charities to diversify their investment portfolios to better support their charitable purposes” and to give charities “the flexibility to use more innovative approaches to address pressing social and economic needs,” which will be welcomed by many in the sector.

The Supplementary Information and Notices of Ways and Means Motions contained in Budget 2015 propose to amend sections 149.1 and 253.1 of the ITA. New subsection 149.1(11) is deemed to have come into force on April 21, 2015 and establishes how the fair market value of a member’s interest in a partnership is to be determined for the purposes of the section 188.1 penalties and the section 149.2 excess corporate holdings rules. Subsection 253.1(2), which will apply to investments made after April 20, 2015, is being introduced to establish that a registered charity or RCAA with an interest in a partnership will not be seen as carrying on a business if the following conditions are met:

by operation of any law governing the arrangement in respect of the partnership, the liability of the member as a member of the partnership is limited;

⁵Philanthropic foundations Canada, Submission to the Standing Committee on Finance (January 2012), online: http://www.parl.gc.ca/Content/HOC/Committee/411/FINA/WebDoc/WD5340612/411_FINA_TIFCD_Briefs/PhilanthropicFoundationsCanadaE.pdf.

⁶Community Foundations Canada, Letter to the Standing Committee on Finance (2 February 2012), online: http://www.parl.gc.ca/Content/HOC/Committee/411/FINA/WebDoc/WD5340612/411_FINA_TIFCD_Briefs/CommunityFoundationsCanadaE.pdf.

⁷Canadian Bar Association, National Charities and Not-for-Profit Law Section, Submission to the Standing Committee on Finance – Pre-budget Consultations 2013, online: http://www.parl.gc.ca/Content/HOC/Committee/412/FINA/WebDoc/WD6264805/412_FINA_PBC2013_Briefs/CanadianBarAssociationE.pdf; Canadian Bar Association, National Charities and Not-for-Profit Law Section, Pre-budget Consultation 2015, online: http://www.parl.gc.ca/Content/HOC/Committee/412/FINA/WebDoc/WD6615327/412_FINA_PBC2014_Briefs/CanadianBarAssociation-e.pdf.

⁸ Pension Investment Association of Canada, Submission to the Minister of Finance (16 March 2015), online: <http://www.piacweb.org/files/15-03-16-Finance-with-CAUBO-re%20ITA-Section-253.1.pdf>.

the member deals at arm's length with each general partner of the partnership; and

the member, or the member together with persons and partnerships with which it does not deal at arm's length, holds interests in the partnership that have a fair market value of not more than 20% of the fair market value of the interests of all members in the partnership.

Budget 2015 indicates that charitable organizations and public foundations can continue to carry on related businesses through limited partnerships in addition to making passive investments in accordance with the ITA amendments. As well, future ITA amendments are anticipated in order to have the rules for non-qualifying securities and loanbacks that currently apply to donations of shares also apply to donations of interests in limited partnerships. Finally, the ITA's excess corporate holdings rules referenced in sections 149.1, 149.2, and 188.1 will likely undergo further amendment to accommodate Budget 2015's intention that these rules "look through" limited partnerships" to place similar restrictions on registered charities and RCCCA's interests in limited partnerships.

3. Gifts to Foreign Charitable Foundations

On January 1, 2013, the ITA was amended as a result of measures proposed in the 2012 Federal Budget to allow foreign charitable organizations that receive a gift from the Government of Canada to apply for qualified donee status if they pursue activities related to disaster relief, urgent humanitarian aid, or in the national interest of Canada.

Budget 2015 now proposes to further amend these provisions by expanding those foreign entities eligible for registration as a "qualified donee" to include "foreign charitable foundations". Under the ITA, qualified donees can generally issue donation tax receipts for gifts received from individuals and corporations, and are also eligible to receive gifts from other qualified donees, including registered charities. Currently, subsection 149.1(26) permits "a foreign organization" that has received a gift from Canada and meets the other applicable requirements to apply for qualified donee status. This allows donors in Canada to make gifts to these foreign organizations and receive the same tax treatment for those gifts as if the foreign organization was a Canadian registered charity. Currently, however, paragraph 149.1(26)(a) of the ITA requires that the foreign organization be a "charitable organization". In this regard, CRA has required that foreign organizations applying for qualified donee status in

Canada meet the definition of a “charitable organization” under the ITA, i.e., that it “have purposes and activities that are exclusively charitable, and mainly carry on its own charitable activities.”⁹

A likely unintended consequence of this provision is that foreign organizations that do not meet the definition of “charitable organization” in Canada, because they do not generally carry on their own activities and gift more than 50% of their income to other charities, are not eligible for qualified donee status. As such, Budget 2015 will amend these provisions to change the wording in the ITA from “the foreign organization is a charitable organization that is not resident in Canada” to “foreign charity is not resident in Canada”. Presumably, since “foreign charity” is not defined in the ITA, this will expand qualified donee status to foreign organizations that would be “charitable foundations” within the meaning of the law in Canada.

While it is not clear why these recent provisions needed this fine tuning, presumably the Federal Government had a foreign organization in mind to donate to that would not have been eligible for qualified donee status despite receiving a gift from it. Budget 2015 indicates that these measures will apply on Royal Assent to the enacting legislation.

4. Social Finance Accelerator Initiative

Budget 2015 includes a commitment by the Federal Government to “support social entrepreneurs with innovative solutions” by announcing “the implementation of a social finance accelerator initiative to help develop promising social finance proposals.” In this regard, Budget 2015 defines “social finance” to mean “an innovative approach to mobilizing multiple resources of capital that delivers both a social value and an economic return.”

While short on details, Budget 2015 states that Employment and Social Development Canada will launch a programme entitled “Social Finance Accelerator Initiative” to assist social entrepreneurs in having their social finance proposals become “investment ready” in order to better attract private investment through initiatives such as workshops, advisory services, mentorship, networking opportunities, and investor introductions. As Budget 2015 provides no further explanation of what the

⁹ CRA, Foreign charitable organizations that have received a gift from Her Majesty in right of Canada, <http://www.cra-arc.gc.ca/chrts-gvng/qlfd-dns/gftsfrmhrmjsty-eng.html>

initiative will involve, interested social entrepreneurs will have to wait for more details to be released by the Federal Government.

The announcement of this initiative follows previous policy commitments by the Federal Government to support social finance in the 2014 Federal Budget, which described the Federal Government's commitment to partner with organizations, businesses, and NPOs to build momentum in Canada around the use of social finance.¹⁰ Hopefully, more details will be forthcoming from the 2015 Budget commitment to social finance than what resulted from the earlier commitments made in the 2014 Federal Budget.

5. Cooperative and Non-Profit Social Housing

Budget 2015 proposes to spend \$150 million towards social housing providers that wish to pre-pay long-term and non-renewable mortgages without penalty. This initiative is slated to start in 2016-2017 and stretch over four years. The initiative aims to address the problem that non-profit housing providers run into when holding long-term and non-renewable loans at interest rates above the national average, making it difficult for them to refinance their outstanding mortgage balance, or access funds for capital repairs, without significant penalties.

In this regard, Budget 2015 proposes to eliminate the mortgage prepayment penalty on long-term, non-renewable loans held with Canada Mortgage and Housing Corporation, allowing non-profit housing providers to access private sector loans at current lower rates, freeing up funds that may ultimately be used to improve the conditions and quality of affordable housing offered by co-operative and non-profit social housing providers.

6. Improving Canadians' Access to Computer Equipment and Digital Skills

Starting in 2016-2017 and extending over two years, Budget 2015 proposes spending \$2 million towards expanding the Computer for Schools Program originally founded in 1993 by Industry Canada and the TelecomPioneers.¹¹ The program is set to be renamed to reflect this expansion. The Computers for Schools Program operates in cooperation with all provinces and territories in collecting and

¹⁰ For more information about Budget 2014, read our summary in *Charity Law Bulletin No. 330*, online: <http://www.carters.ca/pub/bulletin/charity/2014/chylb330.pdf>.

¹¹ "Computers for Schools" Industry Canada, online: <https://www.ic.gc.ca/eic/site/cfs-ope.nsf/eng/Home>.

donating refurbished government computer equipment to organizations, including NPOs. NPOs that currently take part in the program include those that support low-income Canadians, seniors, and new Canadians. The expanded funds are proposed to increase the number of NPOs eligible for participation.