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**OSGOODE HALL LAW SCHOOL**  
**CLE Program**  
Legal Risk Management for  
Charities and Not-for-Profit Organizations

**Toronto – October 5, 2011**

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**The Federal Government Budget and Its  
Implications for Charities and NPOs**

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**By Karen J. Cooper, LL.B., LL.L., TEP**

kcooper@carters.ca  
1-866-388-9596

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|   | <b>Osgoode Hall Law School<br/>CLE Program<br/>Toronto – October 5, 2011</b>  |
| <b>The Federal Government Budget and Its Implications for Charities and NPOs</b>  |   |
| By <b>Karen J. Cooper, LL.B., LL.L., TEP</b><br>kcooper@carters.ca<br>1-866-388-9596<br>© 2011 Carters Professional Corporation |   |
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| <b>OVERVIEW</b>   |                                  |
| <ul style="list-style-type: none"><li>• The 2011 Federal Budget ("Budget") was initially introduced on March 22, 2011</li><li>• The Budget died on the order paper with the vote of non-confidence on March 25, 2011</li><li>• The Budget was reintroduced and tabled on June 6, 2011 and was passed on June 7, 2011</li><li>• The June 6, 2011 Budget is the same as the March 22, 2011 Budget with a few changes described below</li><li>• The Budget contains significant changes to the regulation of charities and other qualified donees</li><li>• For more information on the Budget see Charity Law Bulletin #245 and #253 at <a href="http://www.carters.ca/pub/bulletin/charity/2011/chylb245.pdf">http://www.carters.ca/pub/bulletin/charity/2011/chylb245.pdf</a></li></ul> |                                  |
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| <ol style="list-style-type: none"><li>1. New Regulatory Regime For Qualified Donees<ul style="list-style-type: none"><li>• "Qualified donees" is a term defined in the ITA to include various types of entities that may issue official donation receipts for gifts and receive gifts from registered charities</li><li>• The Budget proposes to extend to the following types of qualified donees certain regulatory requirements in the interest of fairness that currently apply only to registered charities<ul style="list-style-type: none"><li>– Registered Canadian amateur athletic associations ("RCAAs")</li><li>– Municipalities in Canada</li></ul></li></ul></li></ol> |                                  |
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- Municipal and public bodies performing a function of government in Canada
- Housing corporations in Canada constituted exclusively to provide low-cost housing for the aged
- Prescribed universities outside of Canada, the student body of which ordinarily includes students from Canada
- Certain other charitable organizations outside of Canada that have received a gift from Her Majesty in right of Canada in the current or preceding year

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- The remaining qualified donees that are not impacted by the new rules include the following:
  - The Government of Canada
  - The provincial and territorial governments in Canada
  - The United Nations and its agencies
- Registered national arts service organizations are deemed to be "registered charities" and are therefore currently subject to the same requirements that apply to registered charities
- The effective date of these proposals is to be the later of January 1, 2012 and the date of Royal Assent for the enacting legislation

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- The requirements that are proposed to apply to certain qualified donees listed above on the previous slides are:
  - Qualified donees will be identified in a publicly available list maintained by CRA (The July 16, 2010 Technical Amendments already proposed this for RCAAAs)
  - If a qualified donee does not issue donation receipts in accordance with the ITA and its regulations, it may be subject to suspension of receipting privileges or revocation of qualified donee status
  - Monetary penalties associated with improper issuance of receipts that currently apply to registered charities will be extended to RCAAAs

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- Qualified donees will be required to maintain proper books and records and provide access to those books and records to CRA when requested
  - If a qualified donee fails to do so, CRA may suspend its receipting privileges or revoke its qualified donee status
- Monetary penalties associated with failing to file an information return that apply to registered charities will be extended to RCAAAs

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- The Budget proposes to extend the following additional regulatory requirements (which currently apply to registered charities) to RCAAAs:
  - The Budget proposes that RCAAAs be required to have the promotion of amateur athletics in Canada on a nation-wide basis as their *exclusive* purpose and *exclusive* function, rather than their primary purpose and primary function

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- The Budget proposes that if an RCAA provides an undue benefit to any person (e.g. excessive compensation to staff, professional fundraiser or any individual or company with whom it does business), it may be subject to monetary penalties, suspension of its receipting privileges, or revocation
- The Budget proposes to authorize CRA to make available to the public certain information and documents in respect of RCAAAs, in the same manner as applies to registered charities, e.g. governing documents, annual information returns, applications for registration and the names of directors

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2. New Governance Regime For Registered Charities And RCAAAs

- The Budget identifies a CRA concern that there is a recurring problem with applications for charitable status being submitted by individuals who have been involved with other charities and RCAAAs that have had their status revoked for serious non-compliance
- Currently CRA does not have the ability to refuse to register or revoke the status of a registered charity or RCAAA based upon any of these grounds

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- The Budget gives CRA the discretion to refuse or to revoke the registration of a charity or a RCAAA or to suspend its authority to issue official donation receipts, if 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 or RCAAA:
  - Has been found guilty of a criminal offence in Canada or similar offence outside of Canada relating to financial dishonesty (including tax evasion, theft or fraud), or any other criminal offence that is relevant to the operation of the organization, for which he or she has not received a pardon ("relevant criminal offence")

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- Has been found guilty of an offence in Canada within the past five years (other than a "relevant criminal offence"), or similar offence committed outside Canada within the past five years relating to financial dishonesty (including offences under charitable fundraising legislation, convictions for misrepresentation under consumer protection legislation or convictions under securities legislation) or any other offence that is relevant to the operation of the charity or RCAAA ("relevant offence")

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- Has been a member of the board of directors, a trustee, officer or equivalent official, or an individual who otherwise controlled or managed the operation of a charity or RCAA during a period in which the organization engaged in serious non-compliance for which its registration has been revoked within the past five years
- Has been at any time a promoter of a gifting arrangement or other tax shelter in which a charity or RCAA participated and the registration the charity or RCAA has been revoked within the past five years for reasons that included or were related to its participation

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- All of these individuals are described in the Budget as "ineligible individuals"
- These measures are to be effective on the later date of January 1, 2012 and Royal Assent of the enacting legislation
- The Budget states that CRA will look at the "particular circumstances" of a charity or RCAA but does not state what those circumstances are
- The budget does state that CRA will take into account whether "appropriate safeguards have been instituted to address any potential concerns"
  - However, there is no explanation of what these safeguards might be
  - Other board members will want to know what safeguards to take

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- The practical question that arises is what sort of due diligence will a charity or a RCAA be required to undertake to ensure that an "ineligible individual" does not become involved or continue to be involved as a board member, trustee, officer or equivalent official, or one who controls or manages the organization
- Although the Budget states that a charity or a RCAA will not be required to conduct background checks, the issue that charities will need to address is whether a questionnaire is necessary and if so, how frequent is a questionnaire to be used, how broad should the questions be and to whom should it apply?

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3. Recovery Of Tax Assistance For Returned Gifts

- The Budget provides clarification with respect to what happens when a charity returns a donation as it relates to compliance with the ITA
- The Budget permits CRA to reassess a taxpayer outside the normal reassessment period and disallow a taxpayer's claim for a credit or deduction in any situation where the gifted property is returned to a donor in order to ensure "that tax assistance is not improperly retained"
- Where a qualified donee had issued an official donation receipt in respect of a gift of property and subsequently returns that property to the donor, if the value of that returned property is greater than \$50, the qualified donee must issue a revised donation receipt with prescribed information and file a copy with CRA

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- With respect to the return of donated property, the Budget provides rules which address various scenarios that could occur on the return of a gift
  - If the transfer of the original property was a gift, the person is deemed not to have made a gift of the original property nor to have disposed of the property at the time the gift was made
  - If the transfer of the original property was not a gift, for greater certainty, the person is considered not to have disposed of the original property at the time that it was provided to the qualified donee

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- If the returned property is identical to the original property, the returned property is deemed to be the original property
- If the returned property is not the same property or identical property, the person is deemed to have disposed of the original property at the time that the person acquires the returned property
- These measures are to apply in respect of a gift of property returned on or after March 22, 2011
- The Budget provisions do not address the fundamental issue of whether or not a gift can be returned to the donor at law
- Legal advice should be sought in this regard

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4. Gifts of Non-qualifying Securities

- Budget proposes modifications to the rules regarding donations by a taxpayer of a non-qualifying security ("NQS") to a registered charity
- A NQS is defined, generally, to include a share, a debt obligation, or other security issued by a taxpayer or by a person not dealing at arm's length with a taxpayer, but does not include publicly listed securities and deposit obligations of financial institutions

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- These rules previously applied only to donations of NQS to private foundations and other registered charities not at arm's length to the donor but have now been extended by the Budget to apply to all gifts of NQS to all registered charities
- Tax recognition will now be deferred until the recipient charity disposes of the NQS for consideration that is not another NQS of any person as opposed to another NQS of the donor as was previously the case
- If the NQS is not disposed of by the charity within the five-year period following the date of the gift, there will be no tax recognition of the gift

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- The Budget has also proposed new anti-avoidance rules to catch situations whereby, through a series of transactions, a donor avoids the application of the above NQS rules, but at the end of the series of transactions the charity receives a NQS
- These measures are to apply in respect of securities disposed of by donees on or after the March 22, 2011

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5. Granting Of Options To Qualified Donees

- The Budget proposes to delay the recognition of a gift to a qualified donee of an option to acquire property
- Previously, where a donor granted an option to purchase property to a qualified donee, the gift was recognized on the date of the gift for the fair market value of the option and a receipt could be issued immediately
- The Budget proposes to delay this until the option is exercised by the qualified donee, e.g. the property is purchased

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- The taxpayer will be allowed a credit or deduction at the time of acquisition by the donee based on the amount by which the fair market value of the property at that time exceeds the total of amounts, if any, paid by the donee for the option and the property
- The new rules are designed to coincide with the proposed split-receipting rules, in particular the proposed rule providing that where an advantage associated with a gift exceeds 80 per cent of the value of the property transferred, there is no gift
- These measures are to apply in respect of options granted on or after March 22, 2011

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6. Donations of Flow-thru Shares

- Since the elimination by the 2006 Budget of the tax on capital gains accruing on donations of publicly-traded securities to registered charities, donation tax shelter structures involving gifts of flow-thru shares ("FTS") have increased substantially
- A taxpayer can acquire FTS issued by corporations in the oil and gas, mining and renewable energy fields and claim the benefit of "flow-thru" income tax deductions of certain expenses
- As these deductions are claimed, the adjusted cost base ("ACB") of the shares is reduced (usually to nil) such that when the FTS are sold, the full amount of the sale proceeds are taxed as a capital gain

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- If, instead, the FTS are donated to charity, the taxpayer gets the benefit of a tax credit or deduction based on the value of the share at the time of the donation and can also claim the benefit of the exemption from capital gains tax on the disposition
- The combined effect of the deduction of the “flow-thru” expenses, the elimination of the capital gains tax, and the charitable donation deduction or credit substantially reduces or virtually eliminates the after-tax cost of making a charitable donation
- The Budget proposes to limit the availability of the exemption from tax on capital gains where FTS are donated to a qualified donee

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- The exemption from tax on the capital gain that arises from the donation of FTS will only apply to the extent that the cumulative capital gains in respect of the gift exceeds the original cost of the FTS
- This will have the effect of substantially reducing the tax benefits of a gift of FTS so that they are generally no more attractive an option than any other gift of shares or cash
- The Budget also contains anti-avoidance provisions in order to avoid attempts to structure around these changes
- The proposed rules are to apply where a taxpayer acquires shares issued pursuant to a flow-through share agreement entered into on or after March 22, 2011

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7. Supporting Social Partnerships

- Budget states that the Government will encourage the development of government/community partnerships enabling communities to tackle local challenges and test new approaches to improve performance

8. Study of Charitable Donation Incentives

- Motion 559, which was sponsored by the MP for Kitchener-Waterloo on March 22, 2011 was adopted by the House of Commons and is now being supported by the government. The Motion calls for the House Standing Committee on Finance to study charitable donation incentives

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