
THE OTTAWA REGION
Charity & Not-for-Profit Law Seminar

Ottawa – February 2, 2012

**“Ineligible Individuals” and
Other Issues from the 2011 Budget**


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A. OVERVIEW

- The 2011 Federal Budget contains significant changes
- This presentation will provide an overview of the changes that will be of concern to all churches, charities and other qualified donees:
 - A new regulatory regime for qualified donees
 - A new governance regime for charities and registered Canadian amateur athletic associations (“RCAAs”)
 - Clarification on returning charitable gifts returned to donors
 - Changes to the rules around gifting non-qualifying securities, options to acquire property and flow-thru shares
 - The examination of charitable donation incentives

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B. FEDERAL BUDGET 2011

- The 2011 Federal Budget (“Budget”) was initially introduced on March 22, 2011 and was reintroduced on June 6, 2011 in almost identical form
- Bill C-13 was introduced Oct. 4, 2011 and received Royal Assent on Dec. 15, 2011
- For more information on the Budget see Charity Law Bulletin #245 at <http://www.carters.ca/pub/bulletin/charity/2011/chylb245.pdf> and Charity Law Bulletin #253 at <http://www.carters.ca/pub/bulletin/charity/2011/chylb253.pdf>
- For more information on “Ineligible Individuals” see Charity Law Bulletin #269 at <http://www.carters.ca/pub/bulletin/charity/2011/chylb269.pdf>

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- 1. New Regulatory Regime for Qualified Donees
 - “Qualified donee” is a term defined in the *Income Tax Act* (“ITA”) – it is an entity that may issue official donation receipts for gifts and may receive gifts from registered charities
 - The Budget proposes to extend certain regulatory requirements, that currently apply only to charities, to the following types of qualified donees:
 - RCAAAs
 - Municipalities in Canada

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- Municipal or 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, where the student body 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 affected 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,” so they are already subject to the same regulatory requirements
- These changes are effective as January 1, 2012

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- The regulatory requirements that will apply to those qualified donees listed above are:
 - Qualified donees must be registered and identified in a publicly available list maintained by CRA
 - If a qualified donee does not issue donation receipts in accordance with the ITA and its regulations, it could have its receipting privileges suspended or its qualified donee status revoked

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- RCAAAs will be subject to monetary penalties if they issue improper receipts or fail to file an information return
- 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

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- Bill C-13 extends additional regulatory requirements (which currently apply to registered charities) to RCAAAs:
 - Definition will be changed to require them 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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- If an RCAA provides an undue benefit to any person, it may be subject to monetary penalties, suspension of receipting privileges, or revocation, e.g. excessive compensation to staff, professional fundraiser or any individual or company with whom it does business
- CRA is now authorized to make available to the public information and documents in respect of RCAAs, that are currently available in respect of 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 RCAAs

- The Budget identified a CRA concern that applications for charitable status are being submitted by individuals who have been involved with other charities and RCAAs that have had their status revoked for serious non-compliance
- Prior to C-13, CRA did not have the ability to refuse to register or revoke the status of a registered charity or RCAA based on these grounds

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- Bill C-13 has given CRA the discretion to refuse or revoke the registration of a charity or RCAA, or to suspend its receipting privileges, if
 - a member of the board of directors,
 - a trustee,
 - officer or like official, or
 - any individual who otherwise controls or manages the charity or RCAAis an "ineligible individual"

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- An “ineligible individual” is a person who:
 - Has been convicted 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 convicted 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 that relates to financial dishonesty or any other offence that is relevant to the operation of the charity or RCAA (“relevant offence”)
 - Such offences include offences under charitable fundraising legislation, consumer protection legislation or securities legislation

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- Has been a director, a trustee, officer or like official of, 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 and for which its registration has been revoked within the past five years
- Has been at any time a promoter of a tax shelter that involved a registered charity or RCAA, the registration of which was revoked within the past five years for reasons that included or were related to its participation in the tax shelter

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EXAMPLE

- Charity X has a 25 member board of directors. One of these directors, Carter, was employed as the manager of another charity, Charity Y, in 2001-2002
- Charity Y is audited in 2004 in respect of the 2001 and 2002 taxation years
- In February 2006, Charity Y loses its status for substantial non-compliance, as a result of the imprudent actions of Charity Y's board of directors, actions which Carter strongly objected to and which ultimately caused Carter to resign in 2002

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- Because Carter managed a charity that lost its status for substantial non-compliance, Carter is now an "ineligible individual"
- He is an ineligible individual for the period of 5 years from the date of revocation in February 2006
- The charitable status of Charity X could now potentially be revoked because an ineligible individual was/on its board of directors

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- 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

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- 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 the management of the charity?
- The Budget states that a charity will not be required to conduct background checks, but even if the charity wanted to, out of an abundance of caution, the information required to independently assess whether an individual is “ineligible” may not be publicly or easily available:

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- Possible to search for relevant criminal offences in Canada, but abroad?
- Many relevant offences are not tracked in publicly available databases in Canada, and unlikely abroad
- Names of Board members and like officials of revoked charities not maintained in a single database
- Not likely that “an individual who otherwise controlled or managed the operation” would be identified in publicly available documents – likely information solely in CRA’s control

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- Since most of the information is only available to CRA, the onus should be on CRA to maintain a list of “ineligible individuals” (which may exist internally for the purpose of enforcing these provisions) and making it publicly available (unlikely because of privacy and other legal concerns)
- Onus is shifted to charities to comply in a situation where it is impossible to ensure 100% compliance because the necessary information is not available
- This new cause for revocation is similar to a strict liability offence – no due diligence defence is available in the legislation

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- Charities will be required to undertake other forms of due diligence and hope CRA will excuse any inadvertent non-compliance?
- Are all charities going to be required to conduct police checks even if not dealing with vulnerable individuals a simple matter of due diligence?
- One 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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- Likely all directors, trustees, officers and like officials
- Who is an individual who otherwise controls or manages the charity - likely all senior staff ?
- How does a charity deal with a director or officer that is an ineligible individual – usually only the members or directors can remove a director?
- How does a charity remove staff that is an ineligible individual – could have important employment law ramifications?

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3. Clarification on Charitable Gifts Returned to Donors

- The Budget clarifies the effect of a charity returning a donation with respect to the ITA
- CRA will be able to reassess a taxpayer outside the normal reassessment period and disallow a taxpayer's claim for a credit or deduction when gifted property is returned to a donor
- Where a charity has issued an official donation receipt for donation and subsequently returns the gift to the donor, if the value of the returned property is greater than \$50, the charity must file an information return with CRA (e.g. a letter) with prescribed information and provide a copy of the return to the donor

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- These measures 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

- Bill C-13 modifies the rules regarding donations by a taxpayer of a non-qualifying security ("NQS") to a registered charity
- A NQS is generally a share, debt obligation, or other security (but not publicly listed securities and deposit obligations of financial institutions) of a corporation that is not at arm's length to the donor

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- Tax recognition of a gift of a NQS will now be deferred until the recipient charity disposes of the NQS for payment
- 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
- Bill C-13 also contains new anti-avoidance rules to catch situations where, through a series of transactions, the charity receives a NQS and the donor avoids the application of the above NQS rules

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5. Granting of Options to Qualified Donees

- Bill C-13 delays the recognition of a gift of an option to acquire property given to a qualified donee
- Previously, where a donor granted an option to purchase property to a qualified donee, the gift was recognized on the date of the gift and a receipt could be issued immediately for the fair market value of the option
- Bill C-13 delays recognition until the option is exercised by the qualified donee, e.g. the property is purchased

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6. Donations of Flow-thru Shares ("FTS")

- Previously, 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 reduced or virtually eliminated the after-tax cost of making a charitable donation of FTS
- Bill C-13 limits the availability of the exemption from tax on capital gains where FTS are donated to a qualified donee
- These rules apply where a taxpayer acquires shares issued pursuant to a FTS agreement entered into on or after March 22, 2011


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7. Examination of Charitable Donation Incentives

- The Government of Canada is looking at changing the way it finances charities and non-profit organizations to increase accountability of these organizations and to change public expectations
- 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
- Hearings are expected to begin soon

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