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# THE 2006 ANNUAL CHURCH & CHARITY LAW™ SEMINAR

Toronto – November 8, 2006

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## Recent Income Tax Issues Affecting Churches and Charities

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By Theresa L.M. Man, B. Sc., M.Mus., LL.B.

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OVERVIEW OF TOPICS

- Gifts
- Clergy
- Receipts
- Donation tax shelters
- CRA administrative procedures
- Operations of charities
- Miscellaneous cases and CRA interpretations
- Disbursement quota

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ELIMINATION OF CAPITAL GAINS ON  
CERTAIN GIFTS

- Generally, a taxpayer who disposes of property by way of gift is deemed to have received proceeds of disposition equal to the FMV of the property at that time. If the FMV exceeds its adjusted cost base, the taxpayer will realize a capital gain as a result of the disposition. For most gifts of property, 50% of the capital gain is included in income for the year and subject to tax
- In the May 2006 federal budget, the government removed the capital gains tax on publicly listed securities and ecologically sensitive land donated to charities

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- For purposes of valuation, determine the date of the gift of publicly traded shares - certificate being hand-delivered, mailed, or electronically transferred
- Because the Act does not provide guidance in determining how a gift of shares should be valued, CRA has accepted the use of the closing bid price of the share on the date it is received or the mid-point between the high and the low trading prices for the day, whichever provides the best indicator, given the circumstances, of fair market value on normal and active market trading

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- Other factors to consider:
  - the size of the block of shares
  - the volume traded
  - the attributes of the shares
  - whether the donor had control or was a minority shareholder
  - whether there were any restrictions on the transferability of the shares
  - whether the shares were thinly traded

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- Ontario tax treatment of donations of publicly-traded shares and ecological gifts will parallel the federal measures and both would be exempt from the corporate minimum tax
- Charities should develop a policy in respect of receipt of donations of publicly traded shares
- Should continue to monitor changes to the Act in this area with respect to the extension of these measures to private foundations and to other types of property, in particular to real property
- See Charity Law Bulletin #89 and #94, and Charity Law Update September 2006

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**DONATIONS OF PREMIUM POINTS**

- In July 2006, CRA released a technical interpretation (2006-019326) with regard to donations to charities of airline tickets obtained through the redemption of airline reward points
- Where a premium points program gives an individual the right to redeem points accumulated through the program for benefits (e.g. airfare), those points constitute property and can be the subject of a gift, as long as the points may be transferred and their fair market value reasonably estimated

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- A charity which receives premium points as a gift must include the value of the points in determining its income, and may issue an official tax receipt for the gift
- If a tax receipt is issued, the value of the premium points will be included in the calculation of the charity's disbursement quota
- The points should be used before their value diminishes or expires, otherwise there could be problems from a valuation perspective, or the charity could be exposed to sanctions for failing to devote its resources to charitable activities
- See Charity Law Bulletin #99

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**CLERGY – VARIOUS ISSUES**

- Clergy residence deduction - *Pereira v. The Queen* (September 21, 2006) – The taxpayer was a lay person holding the position of pastoral leader for a health and social service centre. He was appointed by the Archbishop of the diocese of Quebec. The Tax Court of Canada decided that he did not qualify for a clergy residence deduction because he was neither “a member of the clergy or of a religious order”, nor “a regular minister of a religious denomination.” See CRA IT-141R “(Consolidated) Clergy Residence Deduction” and *Registered Charities Newsletter #23*

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- Annual membership dues deduction – CRA Technical Interpretation (2006-0168311E5) – The deduction of annual membership fees as “professional fees” (under paragraph 8(1)(i)(i)) paid by members of the clergy who were required to be “licensed and commissioned” in order to perform marriage ceremonies as part of the duties of their employment was permissible provided that the Marriage Act for a particular province contains wording that indicates the status of pastors and ministers is recognized

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- Retired minister with part-time duties - CRA Technical Interpretation (2005-0160401M4, December 28, 2005) – A retired minister who continues to have part time duties would qualify for clergy housing deduction, as long as that person meets the status test and ministering to congregations is an integral part of the employment responsibilities and expectations

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**SPLIT-RECEIPTING**

- New split-receipting rules
- Eligible Amount of Gift = FMV – Advantage
- A gift will now permit some consideration to be received by the donor
- Complicated new rules to curtail tax shelter schemes
- Charities will need to make inquiries to ensure receipts are accurate
- Different proposed changes have different effective dates, some are retroactive

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- British Columbia Supreme Court in *Richard v. Stewards' Charitable Foundation* in 2005, upheld on appeal to British Columbia Court of Appeal in 2006 (see Charity Law Bulletin #68 and Charity Law Update January 2006)
- CRA ruling 2006-017039 (in French) applied the split-receipting rules in relation to the donation of a work of art to a museum which provided a loan-back of the work to the donor for the remainder of his or her life

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- CRA technical interpretation 2005-014243 - applied the split receipting rules to receipts involved in a "Texas Hold'um" poker tournament (such tournaments may not be legal because not fall within the "charitable gaming" exception in the *Criminal Code*)
- See PowerPoint on split-receipting for Church and Charity Law Seminar 2005
- See Charity Law Bulletin #76, 80, 83, papers on "When is an Advantage not an Advantage" and "Intermediate Penalty for Charities: Improper Donation Receipts" posted on [www.charitylaw.ca](http://www.charitylaw.ca)

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**CRA PROVIDES SAMPLE DONATION RECEIPTS**

- On October 3, 2005, CRA released four sample official donation receipts as a guide to charities. Although receipts issued by charities do not need to appear exactly as presented in the samples, the receipts must contain all relevant information set out in the sample receipts
- The four samples are for:
  - Cash gift with no advantage
  - Cash gift with advantage
  - Non-cash gift with no advantage
  - Non-cash gift with advantage

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**NEW REQUIREMENT ON DONATION RECEIPTS**

- CRA announced on December 2, 2005 that registered charities are required to include the name Canada Revenue Agency and the website address [www.cra-arc.gc.ca/charities](http://www.cra-arc.gc.ca/charities) on all official donation receipts
- It is acceptable to include this information by means other than normally required printed (e.g., sticker, stamp, handwritten)
- CRA expects all registered charities to include the new information as of January 1, 2006

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**CASES RELATING TO RECEIPTS**

- *Nassar et al v. The Queen* (February 9, 2006) – FCA disallowed donations made to the Order *antonien libanais des maronites* and imposed penalties because the taxpayer participated with the Order in a scheme to generate receipts not reflecting the amount of donations made
- *Her Majesty the Queen v. Mark Doubinin* (2005) – FCA allowed donor’s claim for a donation made to a charity, but not the inflated donation credit 4 times the amount of donation made as a result of a complex donation scheme

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- *Benquesus et al v. the Queen* (March 24, 2006) – A father transferred funds on behalf of his children to a charity as interest-free loans. The children later forgave part of the loans and the court accepted that donation receipts could be issued for the part of the loans that were forgiven

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**DONATION TAX SHELTERS**

- As a result of the Federal Court of Appeal decisions in Nash and Klotz, registered charities and donors should be wary of the valuations provided by promoters of donation tax shelters
- Nash decision coincided with CRA’s November 2005 Taxpayer Alert reminding potential investors to exercise caution with respect to certain donation arrangements, such as: (1) gifting trust arrangements; (2) leveraged cash donations; and (3) buy-low donate-high arrangements

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- On October 31, 2006, CRA issued a warning to the public of the risks involved in participating in donation tax shelters, e.g. gifting trust arrangements, leveraged cash donations and that CRA has been auditing thousands of tax shelters and taxpayers, and disallowing millions of donations
- See Charity Law Bulletin #87 and paper on donation tax shelters posted on [www.charitylaw.ca](http://www.charitylaw.ca) (Charity Law Update September 2006)

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**CASES RE CRA SEEKING DONOR INFORMATION**

- *All Saints Greek Orthodox Church v. MNR* (2006) – CRA obtained donor list of persons who donated comic books and trading cards during the course of an audit so that CRA may use the donor list in its tax avoidance investigation
- *MNR v. Redeemer Foundation* (October 10, 2006) – After auditing the foundation, CRA obtained a list of donors from the foundation that operated a “forgivable loan program” so that CRA may reassess them

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**NEW T1030 FORM**

- New T3010 form implemented as a result of new DQ and split-receipting rules
- On October 5, 2006, CRA announced unforeseen delays in mailing out T3010s for charities with fiscal periods that ended in July, August and September 2006
- Important to ensure the T3010 is completed accurately
- T3010s are posted on CRA’s website for review by the public
- e.g. Toronto Star article “Charity and the councilor” October 26, 2006

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**CRA’S NEW RE-REGISTRATION PROCESS**

- On August 25, 2006, CRA announced new process for re-registration of charities whose charitable status has been revoked for failure to file annual T3010 Information Return
- \$500 penalty to re-register
- New re-registration process covering three different situations, depending on the charity’s taxation year and when it received the Notice of Intent to Revoke

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**CRA REVISED FORMS**

- The revised *Registered Charities: Application for Re-Designation* (form T2095) and the revised *Registered Charities: Application to Reduce Disbursement Quota* (form T2094) are now available at the CRA website

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**FOUNDATIONS INCURRING DEBT**

- Foundations can incur “debts incurred in connection with the purchase and sale of investment”
- CRA was of the view that these types of debts would only include a miscellaneous type of debt, such as brokerage fees or other incidental amounts related to the purchase or the sale of investments, but not debts for the purpose of purchasing investments, or using the loan proceeds to discharge debts which were, when incurred, permitted under the ITA

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- In October 2005, CRA issued technical interpretation (2005-0154751I7) and revised its position to allow a foundation to incur debts for the purpose of acquiring investment
- It is also now permitted for a foundation’s directors and members to give interest-free loans to the foundation to enable the foundation to acquire investments, pay current operating expenses or expend on charitable activities

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- CRA indicated that they would continue to review debt arrangements, especially those involving non arm’s length parties, in order to ensure that there are no other issues, such as personal benefit
- See Charity Law Bulletin #86

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**CRA NEW POLICY – PUBLICATION OF MAGAZINES**

- On February 3, 2006, CRA issued Policy Commentary CPC – 027 - granting charitable status to organizations that publish magazines in furtherance of educational purposes
- The Policy was adopted by CRA as a result of their granting charitable status to The Walrus Foundation, established to publish the Walrus Magazine
- See Charity Law Bulletin No. 92

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**PRIVATE FOUNDATIONS INVESTING IN LIMITED PARTNERSHIPS**

- CRA technical interpretation on June 27, 2006 (2006-016742)
- A private foundation which acquires a limited partnership interest will be subject to revocation because it would be considered to be carrying on a business

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**CRA GUIDE - MEETING THE PUBLIC BENEFIT TEST**

- CRA released its final form of guidelines in March 2006 to clarify the meaning of the term "public benefit" (CPS-024)
- An organization is only charitable if it meets the definition of charity at common law - part of that definition requires that in order for an organization to be considered charitable, it must be established for public benefit
- The broader public benefit test, which is the subject matter of these guidelines, is principally related to the question of "who" will benefit
- See Charity Law Bulletin #93

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**OTHER RECENT COURT CASES AND CRA TECHNICAL INTERPRETATIONS**

- *Bayit Lepletot v. MNR* (March 28, 2006) – FCA confirmed CRA’s requirement that charities carrying on charitable activities outside of Canada (Israel in this case) through an agent must ensure that the agent is actually carrying on the charitable work of the Canadian charity and subject to the control of the Canadian charity
- *A.Y.S.A. Amateur Youth Soccer Association v. CRA* (April 5, 2006) – FCA denied application of an organization established to promote amateur sport to be a charitable organization. Case being appealed to SCC

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- Rental of parkade as related business (CRA ruling 2005-0160481R3) – The renting (on a for-profit basis) of excess parking capacity in a parkade being built by a charity to provide low-cost parking to its members was a related business of the charity.
- *Travel Just v. CRA* (October 24, 2006) – FCA reviewed whether the object of promoting eco-tourism is charitable.

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- Meaning of “charitable activities” as it applies to charitable organizations (CRA interpretation 2006-0168601E5) – CRA confirmed that even when a charity incurred management and administrative expenses, the charity can still be regarded as devoting *all* of its resources to charitable activities. This is consistent with the DQ rules that only 80% of receipts are required to be expended on charitable programs or on gifts to qualified donees. Where an expenditure is partly charitable and partly administrative, it will need to be allocated between the two when completing the charity’s T3010. CRA is reviewing its policy on how to allocate such expenses

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**DISBURSEMENT QUOTA**

- New complicated rules enacted May 13, 2005
- A + A.1 + B + B.1
- Generally applies to taxation years that begin after March 22, 2004
- Reduce the 4.5 DQ on investment assets to 3.5%
- Introduced new concepts of “enduring property” and “capital gains pool”

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- Extended the application of the 3.5% DQ to charitable organizations – For charitable organizations registered before March 23, 2004, apply for taxation years beginning after December 31, 2008
- See colour DQ chart in Charity Law Bulletin #67, see also Charity Law Bulletin #69
- See PowerPoint on DQ for Church and Charity Law Seminar 2005 and PowerPoint on DQ presentation to University of Ottawa on October 23, 2006 posted on [www.charitylaw.ca](http://www.charitylaw.ca)

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