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Editor: Terrance S. Carter

CRA RELEASES NEW POLICY ON MEETING THE PUBLIC BENEFIT TEST

By Terrance S. Carter, B.A., LL.B. and Karen J. Cooper, B. Soc. Sci., LL.B., LL.L.
Assisted by Nancy E. Claridge, B.A., M.A., LL.B., and Derek B.M. Ross, LL.B. Candidate

A. INTRODUCTION

To be charitable at common law, an organization must not only engage in activities that are intended to achieve its charitable purpose, but such activities must also result in a benefit to the public, or a sufficient section of it. The meaning and significance of this notion of "public benefit," however, has been surrounded with much confusion, leading charitable organizations and legal commentators to express concerns with its lack of clarity and certainty. In response to this confusion, Canada Revenue Agency ("CRA") finally released on March 10, 2006, its long-awaited policy on meeting the public benefit test, entitled "Guidelines for Registering a Charity: Meeting the Public Benefit Test" ("Guidelines").[1] The Guidelines attempt to clarify the meaning of the term "public benefit" and explain how it factors into CRA's determination of charitable status. Thus, the Guidelines will be of great interest to both potential and current charitable organizations, as they set out the CRA's requirements for meeting and maintaining its standards with respect to the public benefit test, which is described in the Guidelines' introduction as being "at the heart of every inquiry into an organization's claim to charitable status." What remains to be seen is whether the Guidelines will serve their intended purpose of providing clarity to the notion of "public benefit." This *Charity Law Bulletin* examines the substance of these requirements, summarizes their content, and comments on some of their more important aspects.

[1] The Guidelines are available on the CRA website at http://www.cra-arc.gc.ca/tax/charities/policy/cps/cps-024-e.html.

B. THE PUBLIC BENEFIT TEST

Under the *Income Tax Act* ("ITA"), organizations seeking the special tax privileges given to charities must register with the CRA. To do so, they must be found to be charitable at common law, which involves meeting two fundamental requirements. First, the organization's purposes must be exclusively charitable (and within the limits of the law), as determined by whether they fall within one or more of the four recognized categories of charity:

- relief of poverty
- advancement of education
- advancement of religion, and
- other purposes beneficial to the community in a way the law regards as charitable.[2]

Although this fourth category of charity is commonly confused with the broader test of public benefit, the Guidelines stress that the two are different. The fourth category above focuses on what is being provided by the organization and can usually only be determined by finding an analogy to other accepted charitable purposes. Conversely, the broader public benefit test, which is the subject of the Guidelines and this *Charity Law Bulletin*, centers on who will benefit from the organization.

The second fundamental requirement for being found to be charitable at common law is that the organization be established for the benefit of the public or a sufficient segment of the public.[3] This consists of two parts, commonly referred to as the Public Benefit Test, and applies to all four charitable categories:

1) a tangible benefit must be conferred, directly or indirectly; and
2) the benefit must have a public character.

C. PROVING A TANGIBLE BENEFIT

According to the Guidelines, the extent of proof required to establish a tangible benefit will vary according to a number of factors, including:

- the nature of the proposed charitable purpose and the category it falls under;
- the social and economic conditions of the time;

[2] As set out by Lord MacNaghton in *Commissioners for Special Purposes of Income Tax v. Pemsel*, [1891] A.C. 531 (H.L.).

- the extent to which the benefit can be quantified;
- the existence of any harmful impact of the undertaking; and
- the relationship between the purpose and the intended beneficiaries.

Perhaps the most significant factor, however, is the charitable category that the proposed purpose falls under. Currently, there is a legal presumption that a public benefit exists where an organization's purposes fall within the first three categories of charity (i.e. relief of poverty, advancement of education or advancement of religion). According to the Guidelines, however, this presumption would be open to challenge if "the contrary is shown" or the charitable nature of the organization is called into question. In such instances, the burden will shift to the organization to prove benefit. However, the criteria for triggering this reverse onus, that the "charitable nature of the organization is called into question," is vague, and it is unclear under which circumstances it could be invoked.

Earlier drafts of the policy suggested that the presumption of public benefit could be challenged where a religious organization promotes beliefs that tend to undermine accepted foundations of religion or morality. This appeared to be in direct conflict with established case law, such as *Re Watson*, in which the court held that "a religious charity can only be shown not to be for the public benefit if its doctrines are adverse to the foundations of all religion and subversive of all morality."[4] Fortunately, CRA has backed away from this position which would otherwise have been detrimental to charitable organizations whose purposes include advancing religion.

Interestingly, while Canada seems to be maintaining the rebuttable presumption of public benefit for the first three heads of charity, England seems to be moving towards the complete removal of the presumption. Proposed charities legislation drafted by the United Kingdom government in May 2004 would have removed the existing common law presumption of public benefit for the relief of poverty, advancement of education, and advancement of religion. Although this Charities Bill was dropped in mid April 2005 when a new election was called, it has since been reintroduced in the U.K. Parliament.[5]

[3] *McGovern v. A.G.*, [1982] 3 All E.R. 439.
[4] [1973] 3 All E.R. 678.
[5] See Bill 83, *Charities Bill*, http://www.publications.parliament.uk/pa/pabills.htm. At the time of writing, the bill had passed through the House of Lords and is due to be debated in the House of Commons in 2006. First Reading in the House of Commons occurred on 9 November 2005.

The requirements of the Public Benefit Test are somewhat different for organizations falling under the fourth category of charity: "other purposes beneficial to the community in a way the law regards as charitable." To establish benefit, it must be shown that the organization's purposes are analogous to those which have previously been determined charitable. However, this burden primarily arises only in circumstances where the proposed purposes are novel or unrecognized; if they are similar or identical to an accepted charitable purpose, proof of benefit will generally not be required, for example the promotion of health and protection of animals. Thus, the CRA concludes that there are effectively only three situations in which tangible benefit needs to be proved by the applicant:

1) when there are novel purposes to be considered;
2) when the presumption of benefit under the first three categories of charity has been disputed; and
3) when a presumption of benefit under the fourth category would be considered charitable but for the concerns raised.

In such cases, the Guidelines suggest that applicants will be required to establish the following three elements:

1. Benefit must be generally shown to be tangible

The Guidelines maintain that, in most cases, an organization's charitable purpose must confer a benefit which is objectively measurable or capable of being proved. This is a direct reference to the English case of *Gilmour v. Coates*,[6] in which it was held that a gift to a contemplative order was not charitable, as it did not provide a discernable public benefit. The requirement that the benefit be recognizable and capable of being proved may be problematic for some organizations, particularly religious ones, as many activities performed by such groups, including worship, prayer, and other rituals, may not be considered to have "practical utility" by those outside the religion.

The CRA acknowledges that intangible benefits, including "promoting the moral or spiritual welfare of the community," may still be acceptable, but only where there is a "clear general consensus that the benefit exists." However, Canadian courts have concluded that consideration of such evidence may be inappropriate, as the courts are not equipped to "assess public consensus, which is a fragile and volatile

[6] [1949] 1 All E.R. 848.

concept."[7] The Guidelines specifically recognize that intangible benefits can be found in charitable purposes arising under the advancement of education, but have not done the same for charitable purposes arising under the advancement of religion, despite references to a "general category of purposes directed to the mental and moral improvement of mankind, or promoting the moral or spiritual welfare of the community."[8] Given the case law on the presumption of public benefit for religious organizations, as discussed above, the absence of a recognition of organizations under the auspices of advancing religion having intangible benefits is certainly peculiar, as well as being risky for religious organizations that, for example, promote beliefs that are not congruent with popular opinion, as the presumption of benefit may more readily be challenged by opponents.

2. Benefit must be generally shown to be direct

CRA examiners consider whether a benefit arises as a direct result of the organization's activities and whether, under the circumstances, that benefit can be reasonably achieved. However, the CRA will also accept purposes which confer indirect benefits so long as they are not too remote to the charitable purpose. The protection of animals, for example, has long been recognized as a charitable purpose on the basis that it benefits the community at large under the fourth category.

3. There must be a net benefit for the public

Finally, in evaluating public benefit, CRA examiners will consider any potential harm that may arise from the proposed activity. The benefit must outweigh that harm in order for the purpose to be considered charitable.

The Guidelines require that these three elements be demonstrated through evidence, the extent and nature of which may vary according to the purpose the organization is seeking to have recognized. For example, additional evidence may be required where the charitable purpose is novel or there is some type of restriction on the beneficiary class. The Guidelines suggest that applicants submit some of the following documents in order to demonstrate public benefit:

[7] *Everywoman's Health Centre v M.N.R.*, [1992] 2 F.C. 52 at 68-69, Decarie J.

[8] For more discussion on this issue, see Terrance S. Carter, assisted by Anne Marie Langan, "Advancing Religion as a Head of Charity: What are the Boundaries?" (Paper presented to the Canadian Council of Christian Charities and Christian Legal Fellowship, September 2005), available at www.charitylaw.ca.

- Needs assessment studies by academics, government bodies, or non-profit organizations that document the existence of the need in the community which will benefit from the services;
- Project and/or funding proposals that address how the proposed activities are best suited to meet the needs of and provide benefit to the community;
- Program evaluations showing that similar programs or this specific proposed program has been demonstrated to benefit the community by meeting the needs of the community effectively;
- Identification of government programs addressing the community need in question along with details on how the program complements or supplements the government program;
- Identification of explicit statements of government policy that may be consistent with the goals and objects of their organization;
- Demonstration of existing public sources of financial support for the organization;
- Identification of new or recent legislative initiatives consistent with the proposed purpose; and
- Any other types of objective material that supports the proposal.

Although such documents may assist in proving a public benefit, the Guidelines warn that they are not determinative. The Guidelines further caution that legislative initiatives promoting the same purposes as those pursued by an applicant will not automatically prove that the organization is pursuing a public benefit, though such evidence may be influential.

D. THE MEANING OF "PUBLIC"

Once it has been established that an organization's purpose confers a tangible benefit, the applicant must still show that the benefit has a public character. The welfare of the public as a whole, as opposed to a select, closed group of individuals, must be sought. The Guidelines suggest that organizations that restrict their services on the basis of personal connections or in a way unrelated to their charitable purpose will not be granted status. Generally, restricting services will violate the public benefit test, unless it can be shown that such restrictions are "rationally connected" to the organization's charitable purpose.

1. Restricting a Benefit

According to the Guidelines, the nature of the restriction must be clearly linked to the proposed benefit. Some restrictions may be a part of the charitable purpose and will be allowed: for example, an organization that assists victims of ovarian cancer will necessarily restrict its services to women, whereas an organization assisting victims of prostate cancer will necessarily restrict its services to men.

Otherwise, organizations must demonstrate why their proposed restriction is "necessary in relation to the charitable purpose proposed." The CRA refers to Viscount Simond's comments in *Inland Revenue Commissioner v. Baddeley*[9] to support this proposition. However, some commentators have suggested that these comments were "probably *obiter*" and that "it is not possible to claim, based on this decision, that the 'rational connection' test forms part of the law of Canada."[10] It is further argued that there is nothing in the classic formulations of the public benefit test prohibiting a charity from favouring "a particular segment of the community identified, for example, by culture or religion."[11]

CRA warns that any proposed restrictions cannot be illegal or contrary to public policy, as such restrictions are incapable of providing a public benefit. The Guidelines suggest that organizations with discriminatory purposes may not meet the Public Benefit Test because their purposes offend the norms in the *Canadian Charter of Rights and Freedoms* or contravene the various human rights codes ("Charter norms"), which some commentators have suggested is a reference to judicial pronouncements under the Charter's equality provisions. However, it has been suggested that an amorphous phrase such as "Charter norms" is not helpful to the public benefit analysis because cases dealing with Charter equality issues say little or nothing about charity law. Of particular concern is the effect this may have on organizations that fall within the "advancing religion" head, and the question of whether traditional religious views may result in the loss of charitable status. As such, concern has been expressed by some commentators that this CRA policy may have unnecessarily broadened the circumstances in which the presumption of public benefit under advancement of religion could be challenged. Given the wide-range of religious beliefs on many different issues, it is possible that some organizations will be subject to a challenge of their presumed public benefit because one or more of their promoted beliefs might be significantly different from those which the CRA views as accepted Charter norms.[12] However, one provision in the *Civil Marriage Act* may provide some measure of comfort to charities under the advancing religion head, as it adds the following protection under the ITA:

> 149.1 (6.21) For greater certainty, subject to subsections (6.1) and (6.2), a registered charity with stated purposes that include the advancement of religion shall not have its registration revoked or be subject to any other penalty under Part V solely because it or

[9] [1955] A.C. 572
[10] David Stevens, "Advancing Religion: A Commentary on the Law's Approach to Understanding Religion as a Charitable Good" (Paper presented to the Ontario Bar Association and the Continuing Legal Committee of the Canadian Bar Association, May 2005) at 10.
[11] *Ibid*. at 9.
[12] For further details, see Terrance S. Carter, *supra* note 8.

> any of its members, officials, supporters or adherents exercises, in relation to marriage between persons of the same sex, the freedom of conscience and religion guaranteed under the *Canadian Charter of Rights and Freedoms*.[13]

The Guidelines acknowledge that some restrictions are acceptable, but that a number of factors need to be considered in order to determine if the restriction is justifiable, including:

- the logical connection between the restriction and the benefit provided;
- whether the restriction precludes the delivery of services to some individuals or parts of the community that also have an identified need;
- whether the services provided are irrelevant to excluded persons;
- whether the organization is particularly expert in the proposed service for the proposed restriction;
- whether the restriction can be supported by evidence of service being more effective if targeted (needs assessment / social science research);
- whether the restriction arises from an intention to use resources to address a specific acute disadvantage or need identified with a particular group or a particular region; and
- the restriction is due, in part, to financial considerations and there is willingness to lift the restriction if the organization becomes better-resourced over time, or a provision of referral to other organizations that offer equivalent or more suitable services.

When an applicant organization fails to establish that the restriction is necessary to fulfill the organization's purpose, the CRA may still allow it to focus its services to a narrow community so long as they are still made available and accessible to the public at large.

In addition to outlining the circumstances in which an organization may restrict the scope of its beneficiary class, the Guidelines also examine whether certain types of organizations can be considered charitable, including member/self-help groups, organizations which confer private benefits to individuals, and organizations which charge fees for services:

[13] *Civil Marriage Act*, S.C. 2005, c. 33, s. 11.1. These issues are dealt with more extensively in Terrance S. Carter and Jacqueline M. Connor, "Advancing Religion as a Charity: Is it Losing Ground?" in *Charity Law Bulletin* No. 58 (10 November 2004), available at www.charitylaw.ca; and Terrance S. Carter, *supra* note 8.

2. Members Groups and Self-Help Organizations

The Guidelines describe members groups as organizations which are established in part for their members and that provide programs and/or benefits directly to their members. Generally, such organizations are not considered charitable at law because of their exclusive nature. However, there are some exceptions. For example, member groups with the charitable purpose of promoting racial equality may be considered charitable.[14] The reasoning behind this is that, although members do have a personal stake in the matter, the benefit may still extend to all others who are affected by the targeted problem.

Another exception is granted to "self-help" groups because membership is generally open to any individual who meets the charitable need. Additionally, CRA recognizes a public benefit because members are drawn from the community at large.

3. Public versus Private Benefit

The Guidelines make it clear that a charitable organization cannot be established to confer benefits to private individuals. However, they maintain that some private benefit may be acceptable if it is a minor and incidental by-product of the organization's charitable purpose. Ultimately, the public benefit conferred by an organization must outweigh the private benefit. CRA sets out three factors it will consider in determining whether private benefit is acceptable:

- the extent to which private benefits are considered incidental;
- the degree to which the private benefits further the charitable purpose and not a collateral purpose; and
- the amount of private benefit, ancillary and incidental to the charitable purpose, should also be reasonable.

According to the Guidelines, a private benefit will be acceptable if it is provided "in the delivery of a reasonable charitable benefit to a properly chosen beneficiary." The example of a religious institution holding social activities for the benefit of members is provided. Conferring such a private benefit on the members is acceptable as it is incidental to the main purpose of advancing religion.

[14] See the CRA "Political Activities Policy Statement" available at http://www.cra-arc.gc.ca/tax/charities/policy/cps/cps-022-e.html. This Policy Statement was also the subject of *Charity Law Bulletin No. 25* available at www.charitylaw.ca.

The Guidelines also suggest that CRA examiners will consider whether any private benefit is more than is necessary to achieve the charitable purpose.

4. Charging Fees

According to the Guidelines, charging fees for services will not disqualify an organization from receiving registered status, unless doing so would have the effect of excluding members of the public. A number of guidelines are set out regarding a charitable organization's ability to charge fees:

- charges should be reasonable (i.e. below market value and aim only at recovering costs) though exceptions may be made to generate a surplus to help fund the other charitable programs and activities;
- charges should not be set at a level that deters or excludes a substantial portion of the beneficiary class; and
- there should be a sufficient general benefit to the community from the existence of the service.

E. CONCLUSION

CRA's clarification of this difficult area of charity law is of great assistance to current and potential charitable organizations and those who advise them. However, concerns remain over the application of this policy to certain types of organizations, the full implications of which may not be known for some time. In particular, the ambiguity surrounding when an organization will be required to prove a benefit and what constitutes a "Charter norm" may need to be addressed in the future.

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Orangeville (519) 942-0001
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