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BILL C-19 IS AMENDED TO SIMPLIFY FUNDING OF NON-QUALIFIED DONEES

By Terrance S. Carter & Theresa L.M. Man*

A. INTRODUCTION

Significant amendments have been made to Bill C-19, *Budget Implementation Act, 2022, No. 1* ("Bill C-19") after the charitable sector expressed serious reservations regarding the original content of the Bill. Bill C-19 was tabled on April 28, 2022, and, as explained in greater detail in *Charity & NFP Law Bulletin No. 511*, many in the charitable sector were concerned that it "perpetuate[d] the colonial relationship between charities and groups without charitable status" and increased the administrative burden for most Canadian charities.[1] After Bill C-19 completed Second Reading on May 10, 2022, it was studied by the Standing Committee on Finance, which heard from numerous stakeholders in the charitable sector. Several amendments to Bill C-19 were then adopted when the House of Commons passed Bill C-19 on its Third Reading on June 9, 2022. Bill C-19 was subsequently passed by the Senate without further changes to these amendments and received Royal Assent on June 23, 2022.

Because of the technical nature of many aspects of Bill C-19, this Bulletin explains the changes made to Bill C-19 adopted at Third Reading in the House of Commons and the effect of those changes. This Bulletin also provides a summary of key issues of Bill C-19 as it relates to the charitable sector.

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[1] Tim Harper, "For the philanthropic sector, a step forward on 'direction and control,' but more work ahead" (12 May 2022), online: *The Philanthropist* <https://thephilanthropist.ca/2022/05/for-the-philanthropic-sector-a-step-forward-on-direction-and-control-butmore-work-ahead/>.

B. BACKGROUND: REGULATION OF CHARITIES UNDER THE *INCOME TAX ACT* AND CALLS FOR CHANGE

The legal reality for charities working with non-QDs prior to Bill C-19 had been criticized by many in the sector as administratively intense, colonial, and out of step with global best practices.[2] This was because under the *Income Tax Act* ("ITA") charities could only use their resource in two ways: (1) making gifts to qualified donees ("QDs"), and (2) devoting their resources to charitable activities carried on by the charities themselves (referred to as a charity's "own activities"). The Canada Revenue Agency ("CRA") administers the own activities provision in the ITA by requiring charities to conduct activities that are directly under the charities' direction and control, and for which the charities can account for any funds or other resources expended.

There have been many calls for changes to how registered charities can work with non-QDs. Some of the most notable examples of these calls for change include the charitable sector's support and advocacy for Bill S-222, *An Act to amend the Income Tax Act (use of resources)* and its successor legislation, Bill S-216, *An Act to amend the Income Tax Act (use of resources of a registered charity)*. Both Bill S-222 and Bill 216 proposed to eliminate the requirement for "own activities" and the corresponding requirement for "direction and control." Bill S-216 passed through the Senate and received Second Reading in the House of Commons on May 16, 2022, but has now been supplanted by Bill C-19.

Further background information leading up to Bill C-19 is explained in *Charity & NFP Law Bulletin No. 511*.

C. NEW REGIME OF "QUALIFYING DISBURSEMENTS" TO "GRANTEE ORGANIZATIONS" IN BILL C-19

Despite promises in Budget 2022 (released on April 7, 2022) that amendments to the ITA would be in the "spirit of Bill S-216", the charitable sector expressed serious concern that the first draft of Bill C-19 did not achieve this goal. Bill C-19 introduced a new secondary regime of "qualifying disbursements" and "grantee organizations" to allow charities to make disbursements by way of a gift or by otherwise making resources available to QDs and non-QD grantee organizations.[3] Where the gift or resources are made to

[2] Open Letter to The Honourable Chrystia Freeland, Deputy Prime Minister and Minister of Finance (17 May 2022), online (pdf): <https://cooperation.ca/wp-content/uploads/2022/05/DC-Open-Letter-v202205_Final_EN.pdf>.

[3] Bill C-19 defines a "grantee organization" to include "a person, club, society, association or organization or prescribed entity but does not include a qualified donee." C-19, *Budget Implementation Act, 2022, No.1*, 1st Sess, 44th Parl, 2022 (second reading in Senate 14 June 2022) at s. 16(3).

non-QDs, the disbursements would need to meet three requirements: (1) the disbursement must further a charitable purpose of the funder charity; (2) the funder charity must ensure that the disbursement is exclusively applied to charitable activities in furtherance of the funder charity's charitable purpose; and (3) the disbursement must meet "prescribed conditions."

1. Concerns About "Prescribed Conditions"

One of the main concerns regarding Bill C-19 as originally drafted was that the "prescribed conditions" requirement was too onerous. The prescribed conditions (set out under proposed Regulation 3703) would have required a detailed written agreement between a funder charity and a recipient grantee organization, as well as pre-disbursement due diligence, ongoing monitoring, review of a final report, and fulfillment of obligations to take "adequate remedial action" if the written agreement was not complied with.[4] While the prescribed conditions in Regulation 3703 were similar to the guidelines set out in the CRA's direction and control guidances CG-002 and CG-004,[5] these conditions would have become mandatory legal requirements, to be followed regardless of the circumstances. In many instances, the prescribed conditions were more onerous than the direction and control regime.[6]

2. The Elimination of "Prescribed Conditions" and Introduction of "Sufficient Documentation"

In light of the concerns regarding the prescribed conditions, the charitable sector engaged in significant and coordinated advocacy of the Federal Government. Representatives from organizations, such as Imagine Canada and Samaritan's Purse voiced the sector's concerns before the Standing Committee on Finance,[7] while more than 60 Canadian global development and humanitarian organizations sent an open letter through Co-operation Canada to The Honourable Chrystia Freeland, Deputy Prime Minister and Minister of Finance.[8] Following these advocacy efforts, amendments to the text of Bill C-19 were adopted

[4] An in-depth analysis can be found in Terrance S. Carter & Theresa L.M. Man, "Bill C-19 Budget Implementation Act, 2022, No. 1 Proposes Major Changes to Legislative Framework Governing Charities" *Charity & NFP Law Bulletin No. 511* (25 May 2022), online (pdf): *Carters Professional Corporation* <https://www.carters.ca/pub/bulletin/charity/2022/chylb511.pdf>.
[5] CG-002 "Canadian registered charities carrying on activities outside Canada" (27 November 2020), online: Government of Canada <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/guidance-002-canadian-registeredcharities-carrying-activities-outside-canada.html>; CG-004 "Using an intermediary to carry on a charity's activities within Canada" (27 November 2020), online: Government of Canada <https://www.canada.ca/en/revenue-agency/services/charitiesgiving/charities/policies-guidance/using-intermediary-carry-a-charitys-activities-within-canada.html>.
[6] Carter & Man, *supra* note 4.
[7] See Standing Committee on Finance, 44th Parl, 1st Sess, Meeting 44 on Monday May 16, 2022 and Meeting 48 on Thursday May 19, 2022. Additional comments were offered by a representative of the Native Women's Association of Canada at Meeting 48.
[8] Open Letter, *supra* note 2.

on June 9, 2022, which deleted proposed Regulation 3703 and replaced requirement #3 (that a qualifying disbursement meet prescribed conditions) with a new less onerous requirement.

Now that the amended Bill C-19 has received Royal Assent, charities will be able to use their resources in three ways, by (a) conducting their "own activities" under their "direction and control", (b) making qualifying disbursements of gifts and other resources to QDs, and (c) making qualifying disbursements of gifts and other resources to non-QD grantee organizations. Under the new regime in the third category, three requirements must be met:[9]

> (1) the disbursement must further a charitable purpose of the funder charity;
>
> (2) the funder charity must ensure that the disbursement is exclusively applied to charitable activities in furtherance of the funder charity's charitable purpose; and
>
> (3) the funder charity must maintain documentation sufficient to demonstrate the purpose for which the disbursement was made and that the disbursement was exclusively applied by the grantee organization to charitable activities in furtherance of the funder charity's charitable purposes.

It is difficult to say how the new qualifying disbursement regime will be administered by the CRA in practice. As the regulator of registered charities, the CRA often provides guidances which, while not carrying the force of law, are highly persuasive in determining how charities are to comply with the ITA. It is expected that the CRA will release a guidance in the coming months to clarify details of the new qualifying disbursement regime. Until a CRA guidance becomes available, it would be premature to speculate how the CRA will administer the new regime. As such, charities that wish to make qualifying disbursements in the short term should consider waiting until the guidance from the CRA becomes available or otherwise consult with their legal counsel for advice.

[9] When these amendments come into force, they will be found at subsection 149.1(1) of the *Income Tax Act*, under the definition of "qualifying disbursement". They are set out at subclause 16(3) of Bill C-19, *supra* note 3.

D. KEY ISSUES TO CONSIDER GOING FORWARD

Bill C-19 adds to and modifies certain aspects of the existing federal tax regime regulating charities. As explained in this Bulletin, Bill C-19 improves the current tax regime by allowing charities to make qualifying disbursements to non-QD grantee organizations. However, unlike Bill S-216, Bill C-19 does not remove the "own activities" requirement from the ITA, leaving that portion of the legislation unchanged. Bill C-19 also amends existing rules to allow charities to make qualifying disbursements (which may be either gifts or other resources) to QDs, instead of simply making gifts to QDs under the previous regime.

While the amendments to Bill C-19 are definitely an improvement over the original text of the Bill, there nevertheless remain several aspects of Bill C-19 that will be potentially confusing or concerning for charities. Some of these concerns were explained in *Charity & NFP Law Bulletin No. 511*, and readers should refer to that Bulletin if they are looking for details beyond the scope of the summary below.

1. Concerns about Making Qualifying Disbursements to Grantee Organizations

There are two concerns regarding qualifying disbursements to grantee organizations that amendments to Bill C-19 did not address.

The first concern is that the proposed "anti-directed gifts" provision in Bill C-19 was not amended. Bill C-19 amends paragraph 168(1)(f) of the ITA to provide that a registered charity may have its charitable status revoked if it accepts a gift, the granting of which was expressly or implicitly conditional on the charity making a gift to "another person, club, society, association or organization." The intention of this provision is to prevent charities from acting as conduits to other organizations.[10] Until the CRA releases a guidance regarding how this provision will be interpreted and enforced, it is difficult to say which activities will or will not be caught by this new provision. In this regard, it is likely that charities will be prevented from fundraising where it is clearly communicated that proceeds will go to support a particular non-QD grantee organization. This will in effect preclude a charity from acting as a "shared platform" for fundraising purposes for other organizations that are non-QDs. However, subject to what the CRA may have to say in their forthcoming guidance, there would not appear to be a problem with a Canadian charity

[10] "Budget 2022" (7 April 2022), online: *Government of Canada*: <https://budget.gc.ca/2022/report-rapport/toc-tdm-en.html> and Department of Finance Canada, "Explanatory Notes Relating to the Income Tax Act and Other Legislation" (April 2022) online: *Government of Canada* <https://fin.canada.ca/drleg-apl/2022/nwmm-amvm-0422-n-eng.pdf>.

fundraising for one of their particular charitable programs (such as providing humanitarian aid for refugees who have been forced to leave a particular war zone — like those currently fleeing the war in Ukraine), provided there is no mention in the charity's fundraising communications about any non-QDs for which the charity intends to work with as grantee organizations.

A second concern for charities is the T3010 reporting requirements introduced in Bill C-19 under Regulation 3704. Regulation 3704 requires charities to report certain information about grantee organizations to which the charity has given more than $5,000 in qualifying disbursements in a taxation year, including the grantee organization's name and the amount and purpose of the qualifying disbursement. Most sections of the T3010 information return are available to the public, while certain sections are specifically held confidential (such as Section F and Schedule 4 of Form T3010) but may still be shared by the CRA with other government agencies and departments. It is not clear at this point whether information reported under Regulation 3704 will be made available to the public. If the information may be available to the public, it could put certain grantee organizations at risk where, for example, organizations are carrying out charitable activities at great risk to themselves, such as advocating for women's rights in certain countries. Further clarification from the CRA in this regard would be helpful.

2. Concerns about Making Qualifying Disbursements to Qualified Donees

As mentioned above, Bill C-19 modifies the existing tax rules that allow charities to make gifts to QDs. Under the changes introduced in Bill C-19, charities will continue to be able to make gifts to QDs, but such gifts are now included as part of the funder charities' qualifying disbursements. In other words, a qualifying disbursement applies to the making of gifts and other resources to both QDs and non-QD grantees.

However, Bill C-19 provides that qualifying disbursements to QDs are subject to a new subsection 149.1(6.001) in the ITA which provides that "disbursements of income of a charitable organization by *way of gifts* to a qualified donee" [emphasis added] cannot exceed 50% of the funder charitable organization's income for that year. It also provides that disbursements over the 50% limit "are not qualifying disbursements."

The combined effect of these amendments means that it is unclear if there is a qualifying disbursement limit which applies to some disbursements (*i.e.*, gifts) but not others (*i.e.*, other resources). In addition, if

a charitable organization does make a disbursement in excess of the qualifying disbursement limit, such a disbursement (which is neither a qualifying disbursement nor intended for the charity's own activities) would be grounds for the Minister of National Revenue to revoke the charity's charitable status.[11]

3. Concerns for Foundations with a Singular Purpose

Some foundations in Canada may have a singular charitable purpose to permit them to only make gifts to QDs. Such a purpose would not be broad enough to allow those foundations to make qualifying disbursements to grantee organizations, because grantee organizations are not QDs. As a result, these foundations may wish to consider updating their charitable purposes if they wish to make qualifying disbursements to grantee organizations.

Although simply changing their sole purpose from "making gifts to QDs" to "making qualifying disbursements" would continue to allow foundations to make gifts to QDs, this would not allow them to make qualifying disbursements to non-QD grantee organizations because of how "qualifying disbursements" is defined in Bill C-19. Specifically, the definition of "qualifying disbursement" requires a gift (or resources otherwise made available) must be "in furtherance of a charitable purpose" of the grantor charity and that the disbursement must be "exclusively applied to charitable activities in furtherance of a charitable purpose" of the grantor charity.[12] This means that when the purpose of the grantor charity is to make qualifying disbursements, the words in Bill C-19 would require the recipient grantee organization to likewise use the gift or resources from the grantor charity for that same purpose, i.e., to make qualifying disbursements to other entities. This is because making qualifying disbursements to grantee organizations is a means to an end of achieving a charitable purpose, but is not an actual charitable purpose in itself. As such, if a foundation that has a singular charitable purpose of only making gifts to QDs would like to start making qualifying disbursements to grantee organisations, it would need to add active charitable purposes to its constating documents.

4. Other Changes of Note

Budget 2022 announced that the disbursement quota rate for charities would increase from 3.5% to 5%. However, this change was not incorporated as part of Bill C-19 and is therefore expected to be introduced

[11] See Bill C-19, *supra* note 3 at subclauses 16(4)-(6) which would amend the language in paragraphs 149.1(2)(c), (3)(b.1) and (4)(b.1) of the *Income Tax Act*.
[12] See Bill C-19, *supra* note 3 at subclause 16(3) which would add the definition of "qualifying disbursement" in subsection 149.1(1) of the *Income Tax Act*. See especially "qualifying disbursement" at (b)(i), (ii), and (iii)(B).

in future budget implementation legislation in the fall. Nevertheless, Bill C-19 amends portions of the ITA to reflect that qualifying disbursements will be included in calculating whether a charity has met its disbursement quota obligations and also updates the definition of disbursement excess. The language in some of these provisions is somewhat confusing as it references "*gifts* made by [a charity] that are qualifying disbursements" [emphasis added] when qualifying disbursements may be both gifts or other resources made available.[13] Despite this ambiguity, the important takeaway for charities is that qualifying disbursements will be included as a credit in meeting their disbursement quota requirement.

E. CONCLUDING COMMENTS

Although Bill C-19 is not without issues, the amendments made to the original wording of Bill C-19 has resulted in a remarkable improvement. The amendments are clearly a result of the effective and coordinated lobbying efforts by many within the charitable sector. While the complete elimination of the own activities and direction and control regime (as proposed in Bill S-216) would have been ideal, the addition of the qualifying disbursement regime in Bill C-19 nevertheless provides a workable alternative mechanism for charities wanting to work with non-QDs.

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[13] Bill C-19, *supra* note 3 at subclauses 16(4)-(6), (10). These sections modify the ITA at paragraphs 149.1(2)(b), (c); 149.1(3)(b), (b.1); 149.1(4)(b), (b.1), and subsection 149.1(21) respectively.