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# **THE OTTAWA REGION CHARITY & NOT-FOR-PROFIT LAW SEMINAR**

**Ottawa – February 13, 2014**

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## **Top 10 Real Estate and Leasing Issues for Charities and NPOs**

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**By Terrance S. Carter, B.A., LL.B., TEP, Trade-mark Agent**

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**Top 10 Real Estate and Leasing Issues for  
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**TOPICS**

- Buying or Leasing - When to See the lawyer
- Conducting Effective Due Diligence
- Remembering Corporate Authority
- Zoning - Why Can't I Do That?
- GST/HST and the Public Service Body Rebate
- Multiple Owners - Co-Ownership Agreements
- Third-Party Facility Use
- Crunching the Numbers - Land Transfer Tax
- Donations Involving Real Property
- The Hand Shake Agreement

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**1. BUYING OR LEASING – WHEN TO SEE THE  
LAWYER**

- Both the Agreement of Purchase and Sale and an Offer to Lease are important legally enforceable documents with significant consequences
  - Engaging legal counsel early in the process can assist in avoiding some common (and not-so-common) pitfalls
  - If unable to engage legal counsel, it is important to ensure conditions are included to enable the charity or NPO to have time after the fact to obtain the legal review



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**a) The Agreement of Purchase and Sale**

- No obligation for a buyer or seller to amend the Agreement after it is finalized
  - The parties and their real estate agents may not have turned their minds to all issues that affect a charity
  - The seller's legal counsel will most likely recommend against amendments that impose a greater burden or risk of liability on their client
  - Including legal counsel at the early stages can help address issues of liability and the necessary due diligence



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- Issues for the Buyer to consider for Agreement:
  - Conditions for building inspection, environmental inspection, financing, insurance, approval of board of directors, legal counsel review
  - Representations and Warranties concerning the state of the property and the buildings
    - Toxic Mould
    - Grow-ops
    - Easements
    - Boundaries
    - Heritage designation
  - Ask for a current survey or consider getting a new one



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- Issues for the Seller to consider for Agreement:
  - Condition for approval of board of directors, legal counsel review
  - Including an as-is, where-is clause to avoid representations and warranties concerning the fitness of the property
  - Alternatively, minimizing the future impact of the representations and warranties
  - Is a Vendor Take-Back Mortgage (VTB) prudent
  - Disclosing all material facts about the property and obtaining acknowledgements from Buyer
  - Reviewing deed for trust provisions

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**b) The Offer to Lease**

- Letters of Intent or Offers to Lease are regularly used in lease negotiations
- The differences are often not understood
  - A Letter of Intent is usually not legally binding, but care must be used in drafting so it does not become legally binding
  - An Offer to Lease is intended to bind the parties, including requiring the tenant to execute the landlord's standard form of lease



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- A lease need not be signed to bind the parties
- Courts may determine a lease relationship without an executed Lease if the Offer to Lease establishes five essential elements:
  - a) the Premises are clearly defined and ascertainable;
  - b) the Parties are correctly named;
  - c) the Rent (minimum, percentage and additional) are clearly expressed;
  - d) the Term (commencement and expiry) is clear or readily ascertainable; and
  - e) all other material terms of the contract not incidental to the landlord and tenant relationship, including any covenants, conditions, exceptions or reservations

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- If Offer to Lease requires tenant to execute the Landlord's standard form of lease, there is little to no opportunity to negotiate anything more than non-financial amendments to the Lease
  - It is important to review the standard form lease prior to execution of Offer to Lease to see if terms are acceptable
- Need to consider certain issues in advance:
  - a covenant from the landlord to prohibit offensive uses of adjoining tenants
  - a right to sublet or assign, and obtain release
  - appropriate rights of renewal or extension
  - termination rights
  - right to municipal tax rebate



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- clearly delineating responsibility for maintenance, repair and replacement
  - silence is not golden
- Insurance - reviewing types and quantum with insurance broker
- carefully reviewing what is included in "operating expenses" and ensuring no duplication of those costs
  - right to annual statement and right to audit
- how is the proportional share of the operating expenses calculated and is it reasonable
- is a guarantor required



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## 2. CONDUCTING EFFECTIVE DUE DILIGENCE

- What is due diligence?
  - Many definitions available, making the "effective" part difficult to determine
  - Due diligence related to the purchase of a real property generally involves an investigation to confirm all material facts concerning the property in order to determine if the transaction should be completed or if risks should be assumed
  - This may involve a building inspection, an environmental assessment, a title search, a work order, fire department and Technical Standards and Safety Association search, zoning compliance, the *Assessment Act*, tax certificates, surveys, etc.



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- If purchasing a commercial condominium unit, obtaining and reviewing the full status certificate is very important
  - Don't skip the declaration and the by-laws
- Effective due diligence includes fully reviewing the reports obtained, and seeking professional assistance to understand the technical details
- You may not be able to afford to have a lawyer provide a full report on the contents of a status certificate or a lease so you must review these documents and ask the questions



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### 3. REMEMBERING CORPORATE AUTHORITY

- For-profit corporate statutes start with the premise that a corporation has the capacity and the rights, powers and privileges of a natural person
  - this concept has been incorporated into the new *Canada Not-for-Profit Corporations Act* and the *Ontario Not-for-Profit Corporations Act*
  - So why do lawyers talk about evidencing corporate authority?
- Directors acting outside of their scope of authority as defined by the organization's letters patent, supplementary letters patent, articles of continuance, by-laws, etc. could be exposed to liability

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- Therefore, need to look at:
  - The actual corporate authority provided for in the objects or purposes of a corporation
  - Whether directors have passed a resolution to proceed with the real estate transaction
  - Possible requirement to seek approval from the membership
  - Whether there is a requirement to obtain approval from third parties:
    - for buying and selling property; or
    - for mortgaging property



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### 4. ZONING – WHY CAN'T I DO THAT?

- Whether you are leasing or buying, one of the first investigations should be with the municipal zoning by-law which will confirm whether or not you can carry on your intended activity on the property and whether you can build to the extent planned
- Failure to comply with zoning by-laws may result in costly orders to demolish buildings or to cease activities on the property
- A minor variance or rezoning application may need to be factored into the costs



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- Minor variance and rezoning applications are costly and are not guaranteed
  - Sometimes it is a lengthy process
- Professional planners and legal counsel experienced in such applications should be retained
- When examining a zoning by-law, it is very important to review the definitions section to confirm that your organization's activities fit within the by-law
- Important to also review issues such as parking requirements and other restrictions



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### 5. GST/HST – DO WE HAVE TO PAY THAT?!

a) Real Property Purchases

- There is a general misconception that charities and NPOs are entitled to an exemption of the GST/HST on real property purchases
- There is also the misconception amongst professionals who regularly deal with for-profit corporations that the GST/HST is “a wash” for charities and NPOs
- Both misconceptions can lead to confused situations and costly last-minute searches for additional funding



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- It is safer to start with a general rule that the purchase of real property is taxable unless there is a specific exempting provision under the *Excise Tax Act*
- Common exemptions include:
  - the sale of used housing (1/2 hectare and house)
  - vacant land sold by an individual
  - the sale of a parking space in a residential condominium complex
  - the sale of real property by a public service body (unless a further exclusion applies)
- The seller must determine whether the transaction is subject to GST/HST prior to finalizing the agreement to avoid costly errors



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- The buyer must determine whether it is considered a GST/HST registrant for the purposes of claiming input tax credits (check at <http://www.cra-arc.gc.ca/esrvc-srvce/tx/bsnss/gsthstrgstry/menu-eng.html>)
- If the charity or NPO is properly registered, the HST payable on the transaction would not be paid to the Seller on closing. Instead the transaction would be reported on the buyer's return for the period in which the transaction closed
  - Many incorrectly use the phrase "the HST is a wash"
  - Many charities or NPOs do not qualify for registration as they only provide exempt supplies
  - Voluntary registration may result in unintended consequences, e.g. failure to qualify for property tax exemptions

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- It is important to confirm whether GST/HST is "in addition to" or "included in" the purchase price
  - as a Seller, it is safer to have it "in addition to" unless the application of GST/HST to the transaction is confirmed
  - as a Buyer, it is safer to have it "included in" unless the expense has been calculated into the acquisition cost
- If there is any question as to the applicability of GST/HST to the transaction, it is best to obtain an advance ruling from CRA
- Do not rely on the call by a board member to CRA's HST helpline; insufficient facts may be presented and the nuances of a charity or NPO is lost, possibly resulting in the wrong answer

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**b) Public Service Body Rebate**

- Charities and certain qualified NPOs may claim the Public Service Body Rebate on eligible purchases and expenses
- What is an eligible purchase?
  - general operating expenses, such as rent, utilities, and administration expenses, for which you cannot claim input tax credits;
  - most allowances and reimbursements you pay to employees involved in your exempt activities;
  - property and services used, consumed, or supplied in your exempt activities; and 
  - capital property
- Rebate amounts to approx. 50% of federal portion and 82% of Ontario portion

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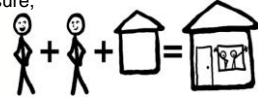
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## 6. BUYING PROPERTY WITH YOUR BEST FRIEND

- Buying real property with your best friend (aka another charity or NPO as applicable) is an increasingly popular transaction given the current economic climate
- The benefits may include the ability for smaller organizations to build equity, affording bigger and better units, having better public exposure, and enjoying greater control over the property
- For some organizations, co-ownership allows them entry into the market



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- Like every other type of relationship, organizations that decide to buy real property together need to plan for the possibility of a dispute or break-up
- Co-ownership agreements can address not only the general management of the real property, including maintenance, repair and replacement issues, but also issues such as financing and the future sale of the property
- Co-ownership of a commercial property is not easy, especially when the parties do not have equal power or resources, and can easily lead to heart break



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## 7. THIRD-PARTY FACILITY USE

- Third-party use of a charity or NPO's building is common-place, but requires careful planning in order to enjoy the financial and social benefits
- A charity or NPO may be exposing itself to a substantial risk of liability
  - personal injury claims
  - sexual abuse claims
  - human rights claims
- Directors of charities or NPOs have a fiduciary duty to protect their assets



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**a) Adopt a Facility Use Policy**

- A facility use policy articulates the charity or NPO's rules and regulations on a number of important issues, including:
  - Prioritization of use of facility
  - Restrictions on the use of the facility
  - Insurance and indemnity requirements
  - Application process
  - Setting out a Facility Use Agreement
- In adopting a Facility Use Policy, the charity or NPO must consider issues of the charity's purposes, its reputation and its exposure to liability
- Important to advise charity or NPO's insurer of third-party use

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**b) Adopt a Facility Use Agreement**

- Charities and NPOs should adopt a standard facility use agreement to outline the terms of third-party rentals
- In addition to basic business terms, should include:
  - Insurance requirements
  - Indemnities
  - Restrictions on use
- Cannot contract out of obligations under *Occupiers' Liability Act* (Ontario)
- Need to conform to human rights legislation

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**8. CRUNCHING THE NUMBERS – LTT**

- If you buy land in Ontario, you must pay Ontario's Land Transfer Tax, which is an escalating rate of 0.5% on first \$55,000, 1% up to \$250,000, 1.5% over \$250,000, and 2% over \$400,000
- In Toronto, the Municipal Land Transfer Tax virtually mirrors the provincial tax: 0.5% on first \$55,000, 1% up to \$400,000, and 2% over \$400,000 and is in addition to the provincial tax
- Gifts of land are still subject to land transfer tax, but if no consideration passes the tax will be nil

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- Assumption, though, of any liability (registered or unregistered) will be considered to be consideration for the purposes of calculating land transfer tax, e.g. the assumption of a mortgage or other contract indebtedness related to the land
- In 2010, Ontario introduced an exemption from land transfer tax for charities for certain transfers of land between qualifying corporations (or trusts) which are registered charities where there is consideration

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- To qualify for the charity exemption:
  - value of consideration must be nil, other than the assumption of any registered encumbrance
  - if a qualifying corporation, must have been the beneficial owner immediately prior to the transfer;
  - must have paid land transfer tax when it acquired the land;
  - must have held the land for a charitable purpose;
  - transferee must be a qualifying corporation and continue to hold the land for same charitable purpose for at least one year after date of transfer
- A qualifying corporation is a non-profit non-share capital corporation that is a registered charity

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- Evidence in the form of an affidavit will need to be submitted to evidence the "nil" value of consideration - will set out information about the property and about the corporations (trusts)
- In the event land transfer tax was paid and the transfer qualifies, the transferee may apply for a refund within four years of tax payment
  - This may occur where paperwork cannot be completed in time
- Transfers of land from a deceased person's estate to the "sole named beneficiary" is exempt from land transfer tax



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### 9. DONATIONS INVOLVING REAL PROPERTY

- Fundraising by charities involve numerous compliance issues under the *Income Tax Act* ("ITA") and under trust law
- In addition, there are specific issues with regard to donations involving real property, e.g.
  - If fundraising for a specific real estate project, it is important to clearly articulate an alternative use of the funds in the event the final goal is not reached and the charities wish to use the funds for other purposes

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- If a donor is donating real property in exchange for a donation tax receipt, the charity **must** first complete standard due diligence to confirm the real property is acceptable, as well as obtain one or more appraisals to confirm the value of the property for receipting purposes
- Beware of situations in which the Seller offers a donation in exchange for the purchase of the real property
- Careful attention needs to be paid to the issue of the Seller's "advantage" under the ITA and how that is to be reflected in relation to the split receipting rules



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### 10. THE DREADED HANDSHAKE AGREEMENT

- Handshake deals may have historically had their place in the business world - typically they were used in closed communities where the trust is high
- Handshake deals are dangerous today for charities and NPOs
- Oral contracts can be enforceable, but:
  - memories fade
  - interpretations may differ
  - parties change
  - relationships change
- Failure to memorialize the handshake agreement may lead to the loss of significant rights or assets



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