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CBA CHARITY LAW Online Symposium

Bill S-216: End of the 'Own Activities' Requirement?

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Introduction

- Current Regime – Own Activities Test & Direction and Control
- Bill S-216, *Effective And Accountable Charities Act*
- Bill C-19, *Budget Implementation Act, 2022, No. 1*

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1. Current Regime – Own Activities Test & Direction and Control

ITA allows charities to use their resources in 2 ways	(1) Make gifts to qualified donees ("QDs")
	(2) Conduct "own activities" in 2 ways: (a) Charities' own staff and volunteers (b) Through 3rd party intermediaries (non-QDs)
ITA "Own Activities" test	Activities must be that of the charity that are directly under the charity's direction, control and supervision, and for which it can account for any funds expended
CRA "Direction and Control" policy	When working through an intermediary, a charity must direct and control the use of its resources

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Active involvement	Charities must be actively involved in programs to achieve its charitable purposes
	Can only make gifts to QDs
	Cannot carry out charitable purposes by simply giving monies, or "resources" to non-QDs
Ongoing involvement	How the activity will be carried on
	The overall goals of the activity
	The area or region where the activity will be carried on
	Who will benefit from the activity
	What goods and services the charity's money will buy
	When the activity will begin and end
Guidances regulate	How to conduct activities through intermediaries
	What to include in the written agreements with intermediaries
	How to maintain direction and control over intermediaries
	What books and records to obtain from intermediaries

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See CRA guidances

- Updated Guidance CG-002 *Canadian Registered Charities Carrying Out Activities Outside of Canada*

https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/guidance-002-canadian-registered-charities-carrying-activities-outside-canada.html

- Updated Guidance CG-004 *Using An Intermediary to Carry Out a Charity's Activities Within Canada*

https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/using-intermediary-carry-a-charitys-activities-within-canada.html

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Key concerns of current regime

- Creates legal fiction – must structure everything that a charity does through a third party intermediary as activity of the charity itself
- Internationally outdated - top-down approach to dictate how charitable activities are carried out does not reflect int'l development philosophy
- Impractical and unrealistic - micro-management required of charities distracts charities from focusing on programs and ignores the benefit of a potential partner organization's local expertise in an international context
- High administrative costs – high cost to complying with the CRA's onerous requirements, even where the charity is working with a trusted partner
- Obstructs indigenous communities - paternalistic and patronizing relationship between charitable organizations and Indigenous communities that are not registered charities or other types of QDs

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2. Bill S-216, *Effective And Accountable Charities Act*

- Bill S-216 was introduced in the Senate on November 24, 2021 – after its predecessor Bill S-222 died on the Order Paper when Parliament was dissolved on August 15, 2021
- Bill S-216 has passed through the Senate and completed its first reading in the House of Commons on February 3, 2022, and is expected to receive second reading in May 2022
- Bill S-216 proposes to remove the own activities test, and allow charities to provide resources to and work with non-QDs while ensuring "resource accountability" to achieve charitable purposes

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- Bill S-216 has received broad-based support from the sector and charity lawyers, including
  - Open letter signed by 37 charity lawyers on February 19, 2021 in support of the then Bill S-222 as "precisely the type of reform that is" needed by the sector
  - Second open letter signed by 42 charity lawyers on March 31, 2022, indicated that Bill S-216 "has been carefully drafted and effectively addresses all of the issues that we had raised in [the] February 19, 2021 open letter", and advocating for legislative and regulatory reform through the adoption of Bill S-216 in the House of Commons without amendment, encouraging Finance Canada to support its passage as well
  - Canadian Bar Association letter April 26, 2022, to Finance in support of Bill S-216

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Proposed changes in Bill S-216

- Deletes "own activities" test from the *Income Tax Act* (Canada)
- New "Resource Accountability" – Allows charities to make resources available to non-QDs, provided that the charity takes "reasonable steps" to ensure that those resources are used exclusively for a charitable purpose
  - Adds new subsection 149.1(27) on what constitutes "reasonable steps" means

    (a) before providing resources to a non-QD, the charity collects the information necessary to satisfy a reasonable person that the resources will be used for a charitable purpose by the non-QD, including information on the identity, experience and activities of the non-QD

    (b) when providing resources to a non-QD, the charity establishes measures, imposes restrictions or conditions, or otherwise takes actions necessary to satisfy a reasonable person that the resources are being used exclusively for a charitable purpose by the non-QD

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Benefits of Bill S-216

- Addressed all concerns under the current regime (see slide above)
- Principled approach, not prescriptive
- Simple and easy to implement
- "Reasonableness standard" that can be adjusted to fit different situations

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3. Bill C-19, *Budget Implementation Act, 2022, No. 1*

- April 7, 2022 – Federal Budget 2022
- April 26, 2022 - Notice of Ways and Means Motion introduced
- April 28, 2022 – Bill C-19, *Budget Implementation Act, 2022, No 1*, received First Reading in the House of Commons
- Budget 2022 indicates that these changes are "intended to implement the spirit" of Bill S-216

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Proposed changes in Bill C-19

- New definition "grantee organization" [ITA ss. 149.1(1)] - "includes a person, club, society, association or organization or prescribed entity" but not a QD
- New definition of "qualifying disbursement" [ITA ss. 149.1(1)] - a disbursement by a charity, by way of a gift or by otherwise making resources available,
  (a) to a QD – subject to new ITA ss. 149.1(6.001)
  (b) to a grantee organization - if all 3 requirements below are met
    (i) the disbursement is in furtherance of a charitable purpose of the charity
    (ii) the charity ensures that the disbursement is exclusively applied to charitable activities in furtherance of a charitable purpose of the charity
    (iii) the disbursement meets prescribed conditions (in the Regulations)
- New ITA ss. 149.1(6.001) - disbursements of income of a charitable organization by way of gifts to a QD (other than to an associated charity) in excess of 50% of the charitable organization's income are not qualifying disbursements

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- Prescribed conditions for qualifying disbursement to grantee organizations [new Regulation 3703] - These qualifying disbursements must meet detailed prescribed conditions:
  - Must have a written agreement containing the terms and conditions of the disbursement and other prescribed information (see next slides for details)
  - Must conduct pre-disbursement due diligence of prescribed matters in Regulation to obtain "reasonable assurance" of future compliance
  - Must conduct ongoing monitoring of the grantee organization – include obtaining periodic reports and verifying disbursements
  - Must receive, review and approve the final report
  - Must take "adequate remedial action "if the agreement is not complied with

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- Written agreement must contain all of the following:

  (i) terms and conditions of the disbursement, including all resources must be used exclusively for charitable activities in furtherance of a charitable purpose of the charity

  (ii) description of the charitable activities that the grantee organization will undertake

  (iii) Require any resources not used exclusively for the purposes for which they were disbursed must be returned to the charity

  (iv) Require periodic reports must be made by grantee organization, at least annually – must include details on the use of the disbursed resources, compliance with the terms of the agreement, and progress made

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(v) Require a written final report must be made in timely manner – must include a summary of the results achieved with the charity's re sources, details on how the resources were used and documentary evidence to demonstrate that resources were used exclusively for the purposes for which they were disbursed

(vi) Require books and records relating to the use of the disbursement (containing information in such form as will enable CRA to determine whether the disbursement is a qualifying disbursement) be kept at least 6 years following the end of the last taxation year of the charity to which the books and records of account relate

(vii) Require books and records relating to the use of the disbursement be made available in a timely manner to the charity (upon request by the charity) to inspect, audit, examine or copy

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- T3010 reporting - A charity that makes over $5,000 in qualifying disbursements to a grantee organization in a year must include report on those disbursements in its T3010 [new Regulation 3704]
- Directed gifts - Expands the power of the CRA to revoke the registration of a registered charity if a gift was made "expressly or implicitly conditional" on the charity making a gift to another person, club, society, association or organization other than a QD (a power that is currently limited to registered Canadian amateur athletic associations and registered journalism organizations) [ITA s. 168(1)(f) amended]
- Bill S-216 - If Bill S-216 received royal assent before or on the same day as Bill C-19, then Bill S-216 would be deemed never to have come into force and would be repealed on the day Bill C-19 came into force

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Questions and concerns of the proposed regime in Bill C-19

- "Own activities test" legal fiction is not deleted
- Complicated system by adding a third new regime
- Introduces new definitions to allow charities to make "qualifying disbursements" to "grantee organizations", thereby introduces new concept of grant – potentially confusing terminology for "gifts" (to QDs) and grants (to non-QDs, also called "grantee organizations")
- Creates 3 "buckets" (see next slide)
  - Conduct own activities with direction and control (current regime)
  - Gifts to QDs (current regime) – which will become gifts to QDs as qualifying disbursements in the new regime
  - "Qualifying disbursements" to grantee organizations (new regime)

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Current regime	Bill C-19 regime
Conduct "own activities" in 2 ways: **(a) Charities' own staff and volunteers** **(b) Through 3rd party intermediaries (non-QDs)** **Under CRA's "direction and control" policy**	**[same as current regime]**
Make gifts to QDs	**Make qualifying disbursements – "by way of a gift or by otherwise making resources available"** **(a) to QDs** **(b) to grantee organizations – must comply with the following requirements:** **(i) the disbursement is in furtherance of a charitable purpose of the charity** **(ii) the charity ensures that the disbursement is exclusively applied to charitable activities in furtherance of a charitable purpose of the charity** **(iii) the disbursement meets prescribed conditions (Regulations 3703 and 3704)**

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- The intent and application of new ITA ss. 149.1(6.001) is not clear –
  - Charitable organizations currently cannot disburse more than 50% of their income as gifts to QDs
  - New ss. 149.1(6.001) provides that disbursements by a charitable organization by way of gift to qualified donees over 50% of its income are not qualifying disbursements – then what are they?
  - This seems to treat qualifying disbursements to grantee organizations the same as charitable disbursements by a charity on its "own activities"- but this is at odds with defining "qualifying disbursements" to include gifts to QDs
- The choice of the term "qualifying disbursement" will result in the acronym "QD" for both "qualifying disbursement" and "qualified donee", resulting in the odd situation that a QD will be required in order to fund a non-QD
- Potentially confusing to charities when to choose bucket #2 vs bucket #3 – this may lead to problems on audits with CRA saying the charity should be in bucket #2 instead of the what the charity intended for bucket # 3

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- Highly prescriptive conditions in Regulations for qualifying disbursements to non-QDs
  - Similar to the US based "expenditure responsibility" regime
  - Very similar to CRA's current onerous direction and control policy , although admittedly devoid of the fictitious "own activities" test
  - CRA's current direction and control regime is in CRA policy, not law, and therefore flexible and can be changed if necessary – but the prescribed conditions in the Regulations are law and cannot be easily changed
  - Same requirements for all situations (such as small grants of $1000 to huge grants of $50 million), with no minimum threshold for small gifts
- For charities whose current purposes are to make gifts to QDs, not sure if purposes would need to be revised to permit qualifying disbursements
- Unclear rationale for onerous mandatory reporting in T3010 qualifying disbursements of $5,000 or more to each non-QD

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Ending Comments

- There is a clear intent by Finance to pre-empt Bill S-216 from ever becoming law, likely because Finance does not want a private members' bill amending the ITA
- However, Bill S-216 has broad support from the sector (see above slides) – a Bill that 42 charity lawyers agreed that it "has been carefully drafted and effectively addresses all of the issues" with the current regime
- In response, Finance has introduced Bill C-19 in record time after Budget 2022 and claims that Bill-C-19 embodies "the spirit" of Bill S-216, all without public consultation or input from the sector or charity lawyers
- However, the reality is that Bill C-19 fails to eliminate the fictitious "own activity test", and is more reflective of a prescriptive US style "expenditure responsibility" regime than a principled "resource accountability" regime as proposed by Bill S-216

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QUESTIONS

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