



THE CANADIAN
BAR ASSOCIATION

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Pre-Budget Consultation 2015

**NATIONAL CHARITIES AND NOT-FOR-PROFIT LAW SECTION
CANADIAN BAR ASSOCIATION**

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PREFACE

The Canadian Bar Association is a national association representing 37,500 jurists, including lawyers, notaries, law teachers and students across Canada. The Association's primary objectives include improvement in the law and in the administration of justice.

This submission was prepared by the National Charities and Not-for-Profit Law Section of the Canadian Bar Association, with assistance from the Legislation and Law Reform Directorate at the National Office. The submission has been reviewed by the Legislation and Law Reform Committee and approved as a public statement of the National Charities and Not-for-Profit Law Section of the Canadian Bar Association.

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I. INTRODUCTION

The Charities and Not-for-Profit Law Section of the Canadian Bar Association (CBA Section) is pleased to make this pre-Budget 2015 submission to the House of Commons Standing Committee on Finance. The CBA Section represents lawyers from across Canada who advise or serve on the boards of charitable and other not-for-profit organizations.

This submission builds on the CBA Section's past representations on fiscal and regulatory measures affecting registered charities and other voluntary sector organizations. This year we focus on four issues:

1. broadening current *Income Tax Act* provisions to allow limited qualified donee status to be conferred on selected foreign charities and facilitate gifting by Canadian charities to them;
2. removing the related business restriction on private foundations and the prohibition on their use of limited partnerships for investment purposes that stems from it;
3. providing for regulatory discretion with respect to contemplated changes to tax treatment of gifts by will, to ensure that its intent is not thwarted by litigation proceedings or other delays in estate administration; and
4. providing more systematic and thorough guidance on non-tax compliance issues.

All these proposals fall under the Pre-Budget Consultation theme of "Improving Canada's taxation and regulatory regimes". The current framework in which Canadian registered charities are required to do their work outside the country is unnecessarily complex and unduly costly. Existing prohibitions on private foundations carrying on related business are redundant given the substantive and reporting obligations now in place for these foundations and may curtail the investment options available to them in the contemporary marketplace.. Absent appropriate regulatory discretion, the anticipated legislative amendments with respect to tax treatment of gifts, while welcome, will be less efficient in channeling funds into the charitable sector than they could be. Last, more attention is needed to the non-tax regulatory

regime governing charities and other voluntary sector organizations, particularly through more systematic and thorough guidance on compliance issues unrelated to taxation.

II. LIMITED QUALIFIED DONEE STATUS AND PERMISSIBLE GIFTING TO SELECTED FOREIGN CHARITIES

The current rules in the *Income Tax Act* related to foreign activities by registered charities create significant inefficiencies in operations, particularly for charities that operate as part of a large international network of affiliated charities. The “own activities” requirement that must be met by Canadian charities seeking to conduct activities through international intermediaries is cumbersome and prevents Canadian charities from taking advantage of the structural efficiencies present in sophisticated international networks.

We recommend amending the *Income Tax Act* to allow the Minister of Revenue to confer a limited registration status on foreign charitable organizations so that grants received from Canadian charities are deemed to be gifts to qualified donees. The foreign donee would be required to use the resources exclusively for charitable activities. Existing record-keeping requirements for charities carrying out activities outside Canada would apply. These foreign organizations would not be eligible to issue official donation receipts that would allow donors to claim charitable tax credits or deductions. The Minister might restrict this registration to charities in countries with a regulatory regime comparable to that in Canada.

This proposal would facilitate grants by Canadian charities to international intermediaries, benefiting Canadian charities engaged in international work, their beneficiaries worldwide and individual Canadian donors by reducing administrative costs and enabling more donations to be used in charitable activities. Canadians generously support the charitable sector, including charities that benefit the developing world.

This proposed change would: enhance the impact of the charitable support on the intended beneficiaries, without compromising the public policy goals of transparency and accountability; increase the confidence of the Canadian public in the charitable sector; better harmonize Canadian charity law with that of other developed nations; and enable Canadian charities to work more efficiently within international charitable networks to deliver charitable programs worldwide. Our recommendation is designed to eliminate the unnecessary administrative requirements imposed by the “own activities” requirement, while maintaining full accountability and transparency from international recipients of Canadian charitable funds.

RECOMMENDATION:

- 1. Broaden current *Income Tax Act* provisions to allow limited qualified donee status to be conferred on selected foreign charities and facilitate gifting by Canadian charities to them.**

III. PRIVATE FOUNDATION RELATED BUSINESS AND INVESTMENT RULES

We recommend removing the restriction in the *Income Tax Act* on private foundations pursuing related business activity and clarifying rules around investment in limited partnerships (including whether that investment constitutes related business activity). Other types of charities (charitable organizations and public foundations) may pursue revenue-generating activity related to their purposes. Private foundations should be permitted to do the same at a time when investment in social purposes is being encouraged by governments across the country and throughout the world.

Recent enactment of anti-avoidance measures related to private foundations has eliminated the need for the current restrictions to protect the assets of charities. The T3010 annual reporting form already requires reporting of such activities by other charities and could impose the same requirement on private foundations, providing the necessary oversight mechanism. Additionally, we recommend that section 149.1 of the *Income Tax Act* be added to the existing section 253 to reinforce for all charities that investment in a limited partnership does not constitute carrying on a business.

Allowing private foundations to pursue related business activity will unleash capital assets for investment in social issues, creating an additional source of desperately needed capital and enabling private foundations to support and invest more effectively in Canadian communities. Our proposal will also benefit other registered charities, funded by private foundations, and the communities in which they operate.

RECOMMENDATIONS:

- 2. Remove the related business restriction on private foundations and the prohibition on their use of limited partnerships for investment purposes that stems from it.**

IV. ADMINISTRATIVE DISCRETION RELATED TO NEW MEASURES DEALING WITH GIFTS BY WILL

The 2014 Budget proposals will limit the availability of the donation tax credit for gifts by will to those gifts actually distributed to the charity by the trustee within 36 months of the death of the testator.

If the distribution cannot be made within the 36 month period, the credit can only be used for taxation years subsequent to the deceased's death. The most significant tax liability in an estate, and the taxation event which is generally the focus of most estate planning, is typically the deemed disposition upon death. The ability to use the donation tax credit for the terminal T1 for the year of death is critical. If the credit is not available for use in the terminal T1 return, the amount of the estate available for distribution to the beneficiaries could be dramatically and substantially different and could, in itself, create uncertainty in the administration of an estate.

There are many estate situations where the actual distribution to a registered charity might be delayed beyond 36 months. Assets, particularly real property and private businesses, might be illiquid. With real property in particular, an environmental contamination may mean a delay in sale is protracted because of the need to remediate the site. With businesses, there may be no market for sale or the business may need to be reorganized before a sale is possible.

Tax issues frequently arise in estates that can take a number of years to resolve. It is also, unfortunately, the case that many estates become litigious because of problems in the drafting or clarity of the will, inter-family issues leading to will variation claims, disputes about parentage and therefore the inheritance rights of individuals, care for disabled individuals, undue influence in the preparation of the will or the contested transfer of assets prior to death. When these issues arise, the trustee is not in a position to make a distribution to a registered charity within 36 months nor in many cases is the trustee able to determine the quantum of the gift to be made to the registered charity. The inability to use the donation tax credit in the terminal T1 return will compound the difficulties for the trustee and the beneficiaries of the estate.

The Canada Revenue Agency (CRA) has administrative policies that deal with delayed payments for gifts by will in the absence of any specific requirement in the *Income Tax Act*. The current discretion CRA exercises may not be available if such provision is not included in the new legislation. We recommend that the new legislation contain a provision, similar to

subsection 70(6) of the *Income Tax Act*, permitting the personal representative to apply in writing to the Minister to extend the time for the application of the donation tax credit in the year of death in the event that there are circumstances preventing the distribution of the amount to a registered charity within the 36 month period.

RECOMMENDATION:

- 3. Provide for regulatory discretion with respect to contemplated changes to tax treatment of gifts by will, to ensure that charities fully benefit from the measure rather than having its intent thwarted by litigation proceedings or other delays in estate administration.**

V. GUIDANCE ON NON-TAX COMPLIANCE ISSUES

Recent years have seen numerous changes to the tax rules governing registered charities and their donors. Leaving aside the merits of these measures, the extensive guidance available from CRA plays a crucial role in fostering compliance and educating advisers, charities and the public about regulatory obligations. CRA's work, however, pertains mainly to tax matters.

We recommend a similar approach be developed for guidance dealing with statutes or regulations on other issues. One ambiguity that often arises is that legislation or regulations unrelated to taxation are not framed with reference to *Income Tax Act* categories or other established regulatory criteria, so the extent to which exemptions or exceptions apply to registered charities and the not-for-profit sector is unclear. For example, this is the case with the application of certain Canada's Anti-Spam measures. Uncertainty about the applicability of provisions and lack of awareness stemming from limited outreach efforts can result both in an unnecessary administrative burden on organizations – diverting resources from core programming – and in compliance actions that are costly both for the regulator and for organizations.

RECOMMENDATION:

- 4. Develop a more thorough and systematic approach to providing guidance on legislative or regulatory initiatives that are not tax-related.**

VI. CONCLUSION

The CBA Section trusts these recommendations will assist the Standing Committee in its consultation on the 2015 Budget. We would be pleased to respond to questions and provide further information regarding any of the issues raised in this submission.

VII. SUMMARY OF RECOMMENDATIONS

The CBA Section recommends four important measures that will improve the taxation and regulatory regime for registered charities:

- 1. Broaden current *Income Tax Act* provisions to allow limited qualified donee status to be conferred on selected foreign charities and facilitate gifting by Canadian charities to them;**
- 2. Remove the related business restriction on private foundations and the prohibition on their use of limited partnerships for investment purposes that stems from it;**
- 3. Provide for regulatory discretion with respect to contemplated changes to tax treatment of gifts by will, to ensure that charities fully benefit from the measure rather than having its intent thwarted by litigation proceedings or other delays in estate administration; and**
- 4. Develop a more thorough and systematic approach to providing guidance on legislative or regulatory initiatives that are not tax-related.**