



2012 Canadian Federal Budget - How will it affect the Canadian charitable sector?

By Mark Blumberg¹ (March 29, 2012)

There are about 10 pages of material in the 2012 Federal budget dealing with Canadian charities and other qualified donees, which are groups that can issue tax receipts. Here are different parts of the budget and I will be placing further information on www.globalphilanthropy.ca

Federal Budget 2012

<http://www.budget.gc.ca/2012/plan/toc-tdm-eng.html>

Highlights (p.189)

The Government is introducing measures to ensure that charities devote their resources primarily to charitable, rather than political, activities, and to enhance public transparency and accountability in this area.

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Enhancing Transparency and Accountability for Charities (p.204-205)

Economic Action Plan 2012 proposes measures to ensure that charities devote their resources primarily to charitable, rather than political, activities, and to enhance public transparency and accountability in this area.

The Government of Canada provides registered charities with generous assistance under the tax system in recognition of the valuable work that they perform. Registered charities are exempt from tax on their income and may issue official donation receipts for gifts received. In turn, donors can use those receipts to reduce their taxes by claiming the Charitable Donations Tax Credit (for individuals) or Charitable Donations Tax Deduction (for corporations). In 2011, federal tax assistance for the charitable sector was approximately \$2.9 billion. At the request of the Government, the House of Commons Standing Committee on Finance is studying current and proposed incentives for charitable giving to ensure that the tax incentives are as effective as possible. Canadians have shown that they are willing to donate generously to support charities, but want to be assured that charities are using their resources appropriately. In this regard, charities are required by law to operate exclusively for charitable purposes and to devote their resources exclusively to charitable activities. Given their unique perspectives and expertise, it is broadly recognized that charities make a valuable contribution to the development of public policy in Canada. Accordingly, under the Income Tax Act charities may devote a limited amount of their resources to non-partisan political activities that are related to their charitable purposes. Recently, concerns have been raised that some charities may not be respecting the rules regarding political activities. There have also been calls for greater public transparency related to the political activities of charities, including the extent to which they may be funded by foreign sources.

The Canada Revenue Agency (CRA), as administrator of the tax system, is responsible for ensuring that charities follow the rules. Accordingly, to enhance charities' compliance with the rules with respect to political activities, Economic Action Plan 2012 proposes that the CRA:

- Enhance its education and compliance activities with respect to political activities by charities.
- Improve transparency by requiring charities to provide more information on their political activities, including the extent to which these are funded by foreign sources.

These administrative changes will cost \$5 million in 2012–13 and \$3 million in 2013–14.

It is also proposed that the Income Tax Act be amended to restrict the extent to which charities may fund the political activities of other qualified donees, and to introduce new sanctions for charities that exceed the limits on political activities, or that fail to provide complete and accurate information in relation to any aspect of their annual return.

Refocusing Government and Programs (p. 217)

The Government is committed to reducing unnecessary spending by focusing on providing programs that are consistent with federal roles and responsibilities, ensuring programs are delivered by those best positioned to do so, and refocusing program funding based on achievable objectives and the needs of Canadians. In particular, the Government's review of departmental spending has identified opportunities to better align program funding with citizen and business demand.

- The Government will introduce legislation to modernize Canada's currency set by eliminating the penny from Canada's coinage system. The Government will no longer distribute pennies as of Fall 2012. However, the penny will retain its value indefinitely and can continue to be used in payments. The penny has weak purchasing power and costs the Government 1.6 cents to produce. Other countries, such as New Zealand, Australia, the Netherlands, Norway, Finland and Sweden, have made smooth transitions to a penny-free economy. The Government expects that businesses will apply rounding for cash transactions in a fair and transparent manner. Canadians will be able to redeem pennies for full value. The Government will work in collaboration with institutions and charitable organizations that may wish to organize fundraising activities around the elimination of the penny.

GST Rebate for Books to be Given Away for Free by Prescribed Literacy Organizations (p. 431)

To promote literacy, a rebate of the GST (and the federal portion of the HST) is provided for printed books (including audio recordings of printed books and printed versions of religious scriptures) acquired by public libraries, educational institutions, as well as charities and qualifying non-profit organizations prescribed by regulation and whose primary purpose is the promotion of literacy. Currently, the rebate does not apply to tax paid on printed books purchased to be sold or given away.

Budget 2012 proposes to allow charity and qualifying non-profit literacy organizations prescribed by regulation to claim a rebate of the GST (and the federal portion of the HST) they pay to acquire printed books to be given away. This change will allow literacy organizations, if prescribed by regulation, to claim a rebate of tax paid on printed books that are, for example, purchased to be given to children from low income households who might not otherwise be able to afford them. Information on the process for charity and qualifying non-profit literacy organizations to apply to be prescribed by regulation for this purpose is available from the Canada Revenue Agency. This measure will apply to acquisitions and importations of printed books in respect of which tax becomes payable after Budget Day.

OTHER TAX MEASURES

Gifts to Foreign Charitable Organizations (p. 435)

In general, donations made by Canadians to foreign charities are not eligible for the Charitable Donations Tax Credit or Deduction. However, a foreign charitable organization that receives a gift from the Government of Canada may register as a qualified donee under the Income Tax Act. As a qualified donee, a foreign charitable organization may issue an official donation receipt for a gift received from a Canadian donor, entitling the donor to a credit or deduction in computing Canadian income or tax. A Canadian registered charity may also make a gift to a foreign charitable organization that is a qualified donee.

Budget 2012 proposes to modify the rules for registering certain foreign charitable organizations as qualified donees. Foreign charitable organizations that receive a gift from the Government may apply for qualified donee status if they pursue activities:

- related to disaster relief or urgent humanitarian aid; or
- in the national interest of Canada.

After consultation with the Minister of Finance, the Minister of National Revenue will have the discretionary power to grant qualified donee status to a foreign charitable organization that meets these criteria. Qualified donee status will be made public, and will be granted for a 24-month period that begins on the date chosen by the Minister of National Revenue, which normally would be no later than the date of the gift from the Government. Granting qualified donee status in these situations will ensure that Canadians receive tax relief for donations made to approved foreign charitable organizations that carry out activities of significance to, and in the interest of, the Canadian public. The Canada Revenue Agency will develop guidance regarding the administration of this measure. Foreign charitable organizations that have received qualified donee status under the existing rules will continue to be qualified donees until the expiration of the period of their current status. This measure will apply to applications made by foreign charitable organizations on or after the later of January 1, 2013 and Royal Assent to the enacting legislation.

Charities – Enhancing Transparency and Accountability (p. 436-439)

Under the *Income Tax Act*, registered charities are required to operate exclusively for charitable purposes and to devote their resources exclusively to charitable activities. Charitable purposes include the relief of poverty, the advancement of education or religion and certain other purposes as recognized by the courts.

A charity is, however, allowed to engage in political activity as long as the activities represent a limited portion of its resources, are non-partisan and are ancillary and incidental to its charitable purposes and activities. Concerns have been raised that some charities may be exceeding these limitations and that there is currently no requirement for a charity to disclose the extent to which it receives funding from foreign sources for political activities. To support the administrative measures proposed in this Budget to enhance compliance and increase disclosure by charities regarding political activities, Budget 2012 also proposes to provide additional enforcement tools to the Canada Revenue Agency (CRA). These measures will also apply to registered Canadian amateur athletic associations. These measures will apply on Royal Assent to the enacting legislation.

Intermediate Sanctions

Where a charity does not comply with its obligations under the *Income Tax Act*, the CRA generally takes a graduated approach to addressing non-compliance. First, the CRA works with the charity and provides it with an opportunity to comply voluntarily. If compliance issues become more serious, the CRA may apply intermediate sanctions, such as monetary penalties or a one-year suspension of the charity's tax-receipting privileges. The CRA may also revoke the registration of a charity. Intermediate sanctions are not, however, currently available in the context of political activities.

Budget 2012 proposes to grant to the CRA the authority to suspend for one year the tax receipting privileges of a charity that exceeds the limitations on political activities. Further, to ensure that charities are accurately reporting in respect of all the activities in which they engage, the CRA will be granted the authority to suspend the tax-receipting privileges of a charity that provides inaccurate or incomplete information in its annual information return until the charity provides the required information.

Funding of Political Activities

Where a charity makes a gift to another qualified donee, the *Income Tax Act* currently treats the amount of the gift to have been devoted to its charitable purposes and activities, even if the gift is earmarked for political activities. This treatment allows a charity to indirectly pursue political activities beyond what would be permitted if it engaged in those activities directly. Budget 2012 proposes that, where a gift is made by a charity and it can reasonably be considered that a purpose of the gift is to support the political activities of a qualified donee, the gift will be considered to be an expenditure made by the charity on political activities.

Tax Shelter Administrative Changes

The registration of tax shelters and the reporting requirements imposed on tax shelter promoters are important tools that assist the Canada Revenue Agency (CRA) in identifying, investigating

and challenging abusive tax planning arrangements. Budget 2012 proposes to encourage tax shelter registration and reporting by:

- modifying the calculation of the penalty applicable to a promoter when a person participates in an unregistered charitable donation tax shelter;
- introducing a new penalty for a promoter who fails to meet their reporting obligations with respect to annual information returns; and
- limiting the period for which a tax shelter identification number is valid to one calendar year.

Charitable Donation Tax Shelters

The *Income Tax Act* imposes a penalty on any person (normally the tax shelter promoter) who sells an interest in, or accepts consideration in respect of, a tax shelter that is not registered with the CRA, or who files false information in an application to register a tax shelter. Where this penalty applies, a participant in the tax shelter cannot make any related claim or deduction until the tax shelter is registered and the penalty is paid.

Currently, the penalty is the greater of \$500 and 25 per cent of the consideration received or receivable in respect of the tax shelter. For example, if a participant were to pay \$12,000 to acquire from a promoter a property that is an unregistered tax shelter, the penalty to the promoter would equal \$3,000. This penalty is intended to encourage compliance by making a promoter liable for a significant proportion of the tax savings that the promoter asserts are available to participants in the tax shelter. In the context of some charitable donation tax shelters, the cost to participants of the property acquired is relatively small in relation to the tax savings that the promoter asserts are available to participants. In these cases, the penalty may be less effective in encouraging compliance by the promoter. Budget 2012 therefore proposes that, in the case of a charitable donation tax shelter, this penalty be the greater of the amount determined under the existing rules and 25 per cent of the amount asserted by the promoter to be the value of property that participants in the tax shelter can transfer to a donee. This measure will generally apply on Royal Assent to the enacting legislation.

Unreported Tax Shelter Sales

A promoter who accepts consideration, or acts as a principal or agent, in respect of a tax shelter is required to file an annual information return, which must include the amount paid by each participant who has acquired an interest in the tax shelter. The penalty for not filing this return on time is the greater of \$100 and \$25 multiplied by the number of days that the return is outstanding, to a maximum of \$2,500. Since one of the primary purposes of the tax shelter registration system is to provide timely and accurate information regarding tax shelters to the CRA, there is a need for a stronger incentive for promoters to provide the required information.

Budget 2012 proposes that an additional penalty be imposed if a promoter fails to either:

- file an annual information return in response to a demand by the CRA to file the return; or
- report in the return an amount paid by a participant in respect of the tax shelter.

The new penalty will equal 25 per cent of the consideration received or receivable by a promoter in respect of all interests in the tax shelter that should have been, but were not, reported in an annual information return, or, in the case of a charitable donation tax shelter for which amounts paid by the participants are not reported, the greater of 25 per cent of the consideration received or receivable by the promoter and the amount asserted by the promoter to be the value of the property that those participants can transfer to a donee.

This measure will apply:

- in the case of the failure to file an annual information return, to demands to file made by the CRA after Royal Assent to the enacting legislation; and
- in the case of the failure to report in an annual information return an amount paid by a participant, to returns filed after Royal Assent to the enacting legislation.

Tax Shelter Identification Numbers

A tax shelter identification number does not have an expiration date, meaning that a promoter may market for an indefinite period a tax shelter for which an identification number has been issued. As a result, when an annual information return in respect of a tax shelter has not been filed, the CRA may need to allocate resources to determine whether the return has not been filed because the promoter is not complying with their filing obligations, or because no interests in the tax shelter were sold in the year. Budget 2012 proposes that a tax shelter identification number be valid only for the calendar year identified in the application for the number filed with the CRA. This measure will apply to applications made on or after Budget Day. Tax shelter identification numbers issued as a result of applications made before Budget Day will be valid until the end of 2013.

NOTICE OF WAYS AND MEANS MOTION TO AMEND THE INCOME TAX ACT –

Annex 4

Gifts to Foreign Charitable Organizations (p. 475)

(42) That, for applications made by a foreign organization on or after the later of January 1, 2013 and the date of Royal Assent to the enacting legislation,

(a) subparagraph (a)(v) of the definition “qualified donee” in subsection 149.1(1) of the Act be replaced with the following:

(v) a foreign organization designated under subsection 149.1(26),
and

(b) section 149.1 of the Act be amended by adding the following after subsection 149.1(25):

Designated foreign charitable organizations

(26) For the purposes of the definition “qualified donee” in subsection (1),

(a) the Minister may designate, in consultation with the Minister of Finance, a foreign organization for a 24-month period that includes the time at which Her Majesty in right of Canada has made a gift to the foreign organization, if

- (i) the foreign organization is a charitable organization that is not resident in Canada,
- (ii) the Minister is satisfied that the foreign organization is
 - (A) carrying on relief activities in response to a disaster,
 - (B) providing urgent humanitarian aid, or
 - (C) carrying on activities in the national interest of Canada, and
- (iii) the foreign organization has applied to the Minister for designation under this subsection; and

(b) a foreign organization designated under paragraph (a) is deemed to have been registered by the Minister at the beginning of the 24-month period.

Charities – Enhancing Transparency and Accountability (P. 476-479)

(43) That, effective on Royal Assent to the enacting legislation,

(a) the definition “charitable purposes” in subsection 149.1(1) of the Act be replaced with the following:

“charitable purposes” includes the disbursement of funds to a qualified donee, other than a gift the making of which is a political activity;

(b) subsection 149.1(1) of the Act be amended by adding the following definition in alphabetical order:

“political activity” includes the making of a gift to a qualified donee if it can reasonably be considered that a purpose of the gift is to support the political activities of the qualified donee;

(c) paragraphs 149.1(6)(b) and (c) of the Act be replaced with the following:

(b) it disburses income to qualified donees, other than income disbursed by way of a gift the making of which is a political activity, if the total amount of income of the charitable organization that is disbursed to qualified donees in a taxation year does not exceed 50% of its income for the year; or

(c) it disburses income to a registered charity that the Minister has designated in writing as a charity associated with it, other than income disbursed by way of a gift the making of which is a political activity.

(d) subsection 149.1(10) of the Act be replaced with the following:

Deemed charitable activity

(10) An amount paid by a charitable organization to a qualified donee that is not paid out of the income of the charitable organization is deemed to be a devotion of a resource of the charitable organization to a charitable activity carried on by it, unless the amount paid is a gift the making of which is a political activity.

(e) subsection 188.2(2) of the Act be amended by deleting “or” at the end of paragraph (c) and by adding the following after paragraph (d):

(e) in the case of a registered charity that is a charitable foundation, if the foundation devotes resources to political activities that are not considered under subsection 149.1(6.1) to be devoted to charitable purposes;

(f) in the case of a registered charity that is a charitable organization, if the organization devotes resources to political activities that are not considered under subsection 149.1(6.2) to be devoted to charitable activities; or

(g) in the case of a registered Canadian amateur athletic association, if the association devotes resources to political activities that are not considered under subsection 149.1(6.201) to be devoted to its exclusive purpose and exclusive function.

(f) section 188.2 of the Act be amended by adding the following after subsection (2):

Suspension – failure to report

(2.1) If a registered charity or a registered Canadian amateur athletic association fails to report information that is required to be included in a return filed under subsection 149.1(14), the Minister may give notice by registered mail to the charity or association that its authority to issue an official receipt referred to in Part XXXV of the *Income Tax Regulations* is suspended from the day that is seven days after the day on which the notice is mailed until such time as the Minister notifies the charity or association, as the case may be, that the Minister has received the required information in prescribed form.

(g) the portion of subsection 188.2(3) of the Act before paragraph (a) be replaced with the following:

Effect of suspension

(3) If the Minister has issued a notice to a qualified donee under subsection (1), (2) or (2.1), subject to subsection (4),
and

(h) subsection 188.2(4) of the Act be replaced with the following:

Application for postponement

(4) If a notice of objection to a suspension under subsection (1), (2) or (2.1) has been filed by a qualified donee, the qualified donee may file an application to the Tax Court of Canada for a postponement of that portion of the period of suspension that has not elapsed until the time determined by the Court.

Tax Shelter Administrative Changes

(44) That, effective on Royal Assent to the enacting legislation, paragraph 227(10)(b) of the Act be replaced with the following:

(b) subsection 237.1(7.4) or (7.5) by a person or partnership,

(45) That, for applications for identification numbers made

(a) before Budget Day, subsection 237.1(4) of the Act be replaced with the following:

Sales prohibited

(4) A person may, at any time, whether as a principal or an agent, sell or issue, or accept consideration in respect of, a tax shelter only if

- (a) the Minister has issued before that time an identification number for the tax shelter; and
- (b) the time is before 2014.

and

(b) on or after Budget Day, paragraph 237.1(4)(b) of the Act, as enacted in accordance with paragraph (a), be replaced with the following:

(b) the time is during the calendar year designated by the Minister as being applicable to the number.

(46) That, in respect of applications for identification numbers made, sales or issuances of tax shelters made and consideration in respect of tax shelters accepted, after Royal Assent to the enacting legislation, paragraph 237.1(7.4)(b) of the Act be replaced with the following:

(b) 25% of the greater of

(i) the total of all amounts each of which is the consideration received or receivable from a person in respect of the tax shelter before the correct information is filed with the Minister or the identification number is issued, as the case may be, and

(ii) the total of all amounts each of which is an amount stated or represented to be the value of property that a particular person who acquires or otherwise invests in the tax shelter could donate to a qualified donee, if the tax shelter is a gifting arrangement and consideration has been received or is receivable from the particular person in respect of the tax shelter before the correct information is filed with the Minister or the identification number is issued, as the case may be.

(47) That, in respect of demands to file an information return that are made and in respect of failures to report an amount in an information return filed, after Royal Assent to the enacting legislation, section 237.1 of the Act be amended by adding the following after subsection (7.4):

Penalty

(7.5) Every person who is required under subsection (7) to file an information return and who fails to comply with a demand under section 233 to file the return or to report in the return information required under paragraph (7)(a) or (b), is liable to a penalty equal to 25% of the greater of

(a) the total of all amounts each of which is the consideration received or receivable by the person in respect of the tax shelter from a particular person in respect of whom information required under paragraph (7)(a) or (b) had not been reported at or before the time the demand was issued or the return was filed, as the case may be; and

(b) if the tax shelter is a gifting arrangement, the total of all amounts each of which is an amount stated or represented to be the value of property that the particular person could donate to a qualified donee.

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