

**Registered Charities:  
Community Economic Development Programs**

## As of November 1, 1999, Revenue Canada became the Canada Customs and Revenue Agency.

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- 954-0410 for local Ottawa calls (English)
- 954-6215 for local Ottawa calls (bilingual)
- 1-800-267-2384 for toll-free, long-distance calls (English)
- 1-888-892-5667 for toll-free, long-distance calls (bilingual)
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The Division's fax numbers are (613) 952-6020 and (613) 946-2423.

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## Community economic development

This guide explains which programs pursued by community economic development organizations are charitable. It originated in a conference organized by the Muttart Foundation in October 1997. At the conference, representatives from the Charities Division of the Canada Customs and Revenue Agency (CCRA), and from organizations interested in community economic development (CED) discussed the charitable status of CED programs.

CED involves a combination of economic and social goals. These goals are often inter-related; for example, economic development and commercial activities are undertaken to achieve social goals such as the relief of poverty or the empowerment of the community, while social goals, such as the advancement of education, are undertaken to develop the local economy.

CED is an evolving field and one in which each community has to find its own solutions. Because of this, organizations that call themselves community development corporations may be pursuing different programs. As a result, we review each case individually.

Many projects carried on in the name of CED are charitable, some are not, and some fall into a grey area. When we evaluate the charitable status of CED projects, we ask two key questions:

1. Who benefits?
2. What is the nature of the benefit provided?

Many issues that CED proponents consider to be important are irrelevant to the framework presented by these two questions. Generally, when we determine charitable status, it does not matter whether an organization:

- is democratically controlled;
- is broadly representative of community interests;
- is located in the community or outside it;
- hires and buys locally;
- derives its income from within the community; or
- has assets that are controlled by the community.

The courts have classified charitable purposes into four categories known as the **four heads of charity**. The first head is the relief of poverty; the second, the advancement of education; the third, the advancement of religion; and the fourth, various purposes that are beneficial to the community which the courts have determined to be charitable. Requirements for recognition as a charity vary somewhat among the four heads.

The expression “beneficial to the community” refers primarily to services or facilities that are open to the public at large. The fourth head does not confer a privileged status on the concept of “community” as a good in itself, and programs intended to sustain a community are not necessarily charitable.

In this guide, community refers to “the people living in a specific locality,” not to “a body of people having a religion, a profession, etc. in common.” (*Concise Oxford Dictionary*) However, one exception occurs in the section called “Relief of people with disabilities” on page 7, which concerns persons with physical, mental, or developmental disabilities.

## Unemployment and employment

### General

Relieving and preventing unemployment is a charitable purpose under the first head and the fourth.<sup>1</sup> However, providing employment is not a charitable purpose in its own right, though on occasion it can be a way to achieve a charitable purpose.<sup>2</sup>

### Who is the organization helping?

Helping people who are unemployed is usually a charitable activity. Where it may not be charitable is when the clients have enough resources and skills of their own that they do not need the help of others.

At the other extreme there is a sub-group among the unemployed that is particularly hard to employ. These people are very much in need of help. We usually recognize people to be among the hard-to-employ if they:

- have been out of the labour force for over a year;
- have completed high school or post-secondary education and not found employment within a year;
- have not completed high school;
- are over age 45;
- have a previous criminal conviction;
- are on social assistance;
- are affected by a physical, mental, or developmental disability (see the section called “Relief of people with disabilities” on page 7);
- are located in an economically challenged community (ECC) (see the section called “Relieving suffering in economically challenged communities” on page 8); or
- are refugees.

<sup>1</sup> IRC v *Oldham Training and Enterprise Council* ([1996] BTC 539).

<sup>2</sup> Cf. Charity Commissioners, *Report* (1980: 27); (1983: 9). The Charity Commissioners are the body that supervises charities in England and Wales. Their decisions are relevant because the English law of charity is similar to that used in Canada to determine eligibility for registration as a charity under the *Income Tax Act*.

We consider an activity to be charitable under the first-head if it addresses:

- the needs of the hard-to-employ; or
- the employment needs of any other group, as long as the applicant can show that substantially all of the members of the group are living below the poverty line.

#### Note

The low income cut-off figures available from Statistics Canada are often used as a poverty line. However, other measures that are widely used and accepted as valid indicators are acceptable alternatives.

Charitable activities that address the needs of other unemployed people are considered charitable under the fourth-head.

First-head charities can restrict the people to whom they offer help based on arbitrary criteria like sex and religion.

Fourth-head charities generally have to offer their services to all in the community who may need them. Any restriction they place on whom they make their services available to must flow naturally from the type of services they are set up to provide. As a result, an organization that helps only young, unemployed persons may be justified if it needs to tailor its programs to meet the needs of its clientele. Similarly, the type of services required by certain immigrants may be different from those needed by the general population. However, we will usually not accept a restriction based on a criterion such as occupation. The issue is not whether unemployed doctors or unemployed plumbers deserve charitable assistance, but rather whether any occupational group needs programs that are so specialized as to justify denying help to others who are unemployed.

## Preventing unemployment

This purpose can be charitable. However, if an organization's focus is helping businesses to start up or to stay in operation, the presence of private benefit for the businesses in question would seem to contradict the possibility of a charitable purpose (see the section called "Existence of a private benefit" on page 10). For this reason, we require applicants seeking to prevent unemployment to demonstrate that any private benefit is a minor by-product of its programs. In addition, the prospect of unemployment must be an immediate problem, not some vague future possibility. Greater latitude in this area applies in ECCs (see the section called "Relieving suffering in economically challenged communities" on page 8).

## Types of programs

We recognize the following programs for the relief of unemployment as charitable activities.

### Job search assistance

Among the various services a charity may offer its clientele are:

- career counselling;

- referrals of persons with special needs to other agencies for assistance;
- encouragement to pursue a job search, including the formation of peer groups for mutual support;
- help preparing résumés or preparing for job interviews;
- establishing lists of those seeking work;
- establishing lists of available jobs after canvassing local employers;
- matching its clientele to an appropriate employer; and
- where needed, providing funds to allow a client to attend interviews or to relocate.

## Assistance claiming benefits

We recognize helping unemployed persons obtain Employment Insurance or other benefits to which they are legally entitled as a charitable activity.

## Vocational, employability, and entrepreneurial training

In general, any training that offers a formal course of instruction is charitable under the second head (advancement of education).

Employability training refers to developing the skills necessary to prepare a person for employment. It includes teaching English or French as a second language, as well as life skills such as time management and interpersonal relations.

Entrepreneurial training includes instruction on preparing a business plan, obtaining financing, bookkeeping, preparing financial statements, marketing, and government regulations.

Providing training to meet a particular employer's needs is not as a rule charitable because of the substantial private benefit that results for the employer. If a training program set up by a company for its employees is not charitable,<sup>3</sup> neither is such training if it is provided by an external agency. However, this rule can be relaxed somewhat in the case of first-head charities in the following circumstances:

- It may only be possible to find employment for hard-to-employ persons if a particular company and an independent charity agree ahead of time that the latter will provide training that both see as necessary to meet the company's hiring standards.
- For hard-to-employ persons, making the transition to the labour force can be a slow, uncertain process. Therefore, it may be necessary to provide a client with additional post-employment training so that he or she can remain employed.
- In ECCs, it is acceptable to prevent further unemployment by providing training for the employees of any company within the community if:
  - without this training, a company would be forced to close or dismiss workers; **and**

<sup>3</sup> *Re Leverhulme* [1943] 2 Ch. 143.

- the training can be generally applied in the marketplace (such as literacy or computer skills), as opposed to training that is of use only to a specific employer.

### Training “businesses”

The purpose of these “businesses” is to give on-the-job training in vocational skills or more general training in work skills that enhances a person’s employability. To be charitable, the dominant purpose cannot be simply to provide people with employment, or the charity with resources. Training businesses typically share the following characteristics:

- classroom training occurs before or accompanies the on-the-job training;
- the participants are employed in the business for a limited period of time;
- the charity offers a job placement service to help graduates of the program find work in the labour force;
- the proportion of workers from the target population in relation to the total number of employees is no lower than 70%, but alternative ratios may be justifiable if considerable supervision is required; and
- revenues derived from the business do not substantially or consistently surpass the break-even point.

#### Note

“Break-even point” would include provision for a charity to build up an adequate reserve, although it would not extend to generating ongoing surpluses. In the latter case, the identity of the program as a charitable activity (as opposed to a related business) is open to question.

Although referred to as training businesses, organizations that meet the above criteria may be conducting a charitable activity. In contrast, if an organization does not satisfy the second and fourth criteria above, it is questionable whether the organization’s purpose is indeed training (charitable) as opposed to providing jobs (non-charitable). If the last criterion is not satisfied, the organization may have moved from a charitable activity into running a business. To determine whether the business activities of the organization are acceptable, the tests for related businesses would have to be considered (see the section called “Related business” on page 12).

### Individual development accounts

Individual development accounts are restricted savings accounts for low-income individuals, families, or groups. In contrast to loans, which must be repaid, charities involved in these accounts provide matching grants at a ratio determined by the charity (e.g., 2:1) to help these people develop savings over a one- to three-year period. To be charitable, these funds must be restricted in use to purposes that help to relieve the poverty of the recipients (e.g., funding post-secondary education).

### Micro-enterprises and community loan funds (first-head charities only)

We recognize the setting up in business of hard-to-employ persons as a charitable activity. Such businesses may be sole-proprietorships or collective enterprises such as worker co-operatives. These programs usually include entrepreneurial training, plus support services and start-up loans.

Ongoing support services are justifiable until the business is viable. Such services can include consulting services providing, office space, and secretarial services.

Before registration, an applicant micro-lending organization has to provide us with its policy for determining when a business is viable and therefore no longer in need of its support services or further loans. These guidelines will vary depending on the clients, the community they are operating in, and the type of business. One example of such a guideline might be found in the criteria used by the charity to determine when a business should have the capacity to obtain financing from conventional sources.

Start-up loans (or loan guarantees) can be offered to those who cannot effectively finance even the smallest business venture. This happens when regular financial institutions refuse either to handle the small amount involved or to lend in the absence of collateral. Amounts loaned by the charity are typically under \$10,000. Loans that exceed \$25,000, or that are consistently larger than \$10,000, suggest the crossing of the threshold between the relief of poverty and the non-charitable support of small business.

Community loan funds, themselves operating a micro-enterprise program or lending money to charities operating such a program, are charitable.

#### Note

Community loan funds also lend money for other purposes. One example is a bridge-loan to an organization to tide it over before it receives a government grant. If the community loan fund lends only to registered charities, it will not have to concern itself with benefiting non-qualified donees or with using its resources for non-charitable purposes. However, if the borrowing organizations are not registered, the fund could be breaching the *Income Tax Act* unless it can show either that the loans qualify as straight investments or that the borrowing organization is under contract with the lender to conduct one of the latter’s charitable programs. See the section called “Funding non-qualified donees” on page 12.

Under any program providing loans to the poor, charging beneficiaries an interest rate that yields a surplus to the lending organization calls into question whether the purpose of the organization is to relieve poverty.

#### Note

A rate would produce a surplus if it exceeded what was necessary to cover the lender’s own borrowing rate, its administrative costs, and a loan-loss provision that is supported by the organization’s actual loan-loss experience. New organizations can rely on the loan-loss experience of charities that operate similar programs.

## Loans and expenditures

The *Income Tax Act* requires a charity to spend a minimum amount each year (its disbursement quota) on its charitable programs. Legally, a loan does not constitute an expenditure, unless it is written off as uncollectable.

However, lending the necessary funds rather than giving them to clients is central to the concept of micro-lending programs. The argument is that a handout will not break the cycle of poverty, whereas a loan can. A loan ensures the charity's continuing interest in the recipients' progress, enhances their self-respect, is salutary in imposing certain obligations on them, and helps them to establish a credit rating.

Our policy is that micro-lending organizations can satisfy their disbursement quotas by expenditures on training, business support services, loans written off as uncollectable, and an amount equal to the opportunity cost, if any, of making the loans, calculated as follows:

- total of outstanding micro-enterprise loans **multiplied by** the difference between the interest rate the charity could earn if it invested the amount in T-bills or GICs, and the interest rate the charity is charging its beneficiaries.

### Note

We are not prepared to extend the exceptional treatment of loans described in this paragraph to other loan programs (e.g., loans to students or loans for families to attend the sick), unless an applicant can establish an equally convincing argument that lending rather than giving is necessary to effectively achieve its charitable purpose.

We will use subsection 149.1(5) of the *Income Tax Act* to treat the opportunity cost of making the loan as if it were an expenditure on charitable activities. The amount should be reported on line 832 of the charity's annual return ("Deemed expenditure: special relief amount"). In the case of micro-lending organizations, we will also consider an amount placed on line 832 as fulfilling the requirement of subsection 149.1(5) for "an application made to the Minister on prescribed form," as long as "micro-enterprise loans" is written beside the entry on line 832.

## Relieving poverty through the operation of stores

### Providing low-cost necessities

We recognize the operation of thrift stores and similar outlets as a charitable activity if the stores are located in sections of a community inhabited largely by the poor, if they sell donated goods at a low price, and if they operate on a break-even basis. Such stores cannot be separately registered if they are operated as a fund-raising vehicle, although they may qualify as a related business of an

organization that otherwise qualifies as a charity. The decision in *Alberta Institute on Mental Retardation v. R.* ([1987] DTC 5306) will be applied only to similar fact situations (notably, when an organization is involved in converting donated goods to cash, and none of the charity's assets are at risk).<sup>4</sup>

## Selling goods produced by the poor

Our policy is not to register such stores separately, but to recognize them as ancillary and incidental to a charitable program and to allow this mechanism only for charities working with the extreme poverty found in certain third-world countries. We recognize that the sale of items made by poor artisans in third-world countries and the development of a marketing network for their products provides these workers with an income and can relieve their poverty. However, we are not prepared to extend this concept to Canadian artisans, with the exception noted in the following section. The reason for this distinction is that Canadian residents are not known to experience the same incapacity to bring their products to market as do some of the overseas poor.

## Relief of people with disabilities

### Social "businesses"

Social "businesses" address the needs of the disabled and are recent equivalents of sheltered workshops. They seek to provide employment on a permanent basis, unlike training businesses that provide employment for a limited period.

Social businesses that can be registered typically share the following characteristics:

- the work is specifically structured to take into account the special needs of the workers;
- the workforce is comprised entirely of people who are physically, mentally, or developmentally challenged, with the exception of a few persons with specialized skills required for operating the business;
- the workers are involved in decision-making for the organization and sit on its board to foster their sense of competence and control over their lives;
- income derived from the business may pay the workers' wages, but the organization is subsidized, usually by government grants; and
- the organization provides training that is not only immediately job-related, but which enhances the general skills of its workers.

A social business usually provides services, but it can also manufacture articles. In the latter case, it can be structured as a workshop used either by employees of the business or by individuals working for themselves, with the organization providing technical assistance, tools, materials, and marketing.

<sup>4</sup> Cf. Charity Commissioners, *Report* (1991: 42): "Although trading can be permitted in direct furtherance of a charity's objects (for instance, charities for the disabled selling goods made by beneficiaries) or if ancillary and incidental to a main charitable purpose (for instance, theatres providing refreshments at performances and selling their own publications), a charity cannot properly undertake unrestricted trading activity to raise funds."

The purpose of these workshops is to provide persons working in them with the sense of self-esteem, competence, and usefulness that comes from earning an income. The products must accordingly be sold. The organization may itself operate a retail outlet or send the products to a store in a larger centre. This store, to the extent that it only accepts products produced in the programs of a number of registered charities assisting the disabled, can itself be registered as promoting the efficiency and effectiveness of these charities.

## Relieving suffering in economically challenged communities

### General

An economically challenged community (ECC) is a geographically defined community where the unemployment rate has been 50% or more above the national average for two or more consecutive years. A community is no longer an ECC when its unemployment rate has fallen below this level for four years in a row. When this happens, an organization would be given a further two years to wind up any of its programs that are charitable solely because they have been located in an ECC.

#### Notes

1. Where appropriate, labour force participation may be used as an alternative to the unemployment rate.
2. An ECC may be either larger or smaller than a municipality. Yet as a “community,” its population cannot be so large that the residents lose their sense of belonging together in a common space. A suggested maximum size for an ECC is a population of 20,000, but this can only be a suggestion since people’s sense of sharing a neighbourhood will depend on the area’s history and the diversity of its population, natural boundaries such as rivers, and long-established political boundaries, such as city wards. In one region, however, there could be a number of contiguous ECCs. If the community is too small to appear separately in statistical reports, data from the surrounding region may be acceptable.

ECCs frequently display a number of the following symptoms of social stress:

- a declining population, as the working-age population is forced out of the community in search of employment elsewhere;
- high rates (i.e., above the national average) of family breakdown and family violence;
- high rates of crime generally;
- high rates of health problems, including mental health problems and suicides;
- high rates of drug and alcohol addiction; and
- high rates of children taken into care and school drop-outs.

Typically, the community’s social infrastructure is underdeveloped or declining. Affordable housing may be in short supply, medical services unavailable locally, places for religious congregation abandoned, community centres or recreational facilities lacking, and libraries, theatres, and other venues for educational and artistic development absent. The community may also be facing a degraded physical environment in such forms as industrial pollution from former industries, failure of external property owners to maintain their land and buildings, and vandalism. As well, demoralization and a sense of helplessness may have reached the point where voluntary action—the creation, joining, and support of local groups established for social and philanthropic purposes—all but ceases.

### Types of programs

Many well-recognized charitable purposes address the needs outlined in the previous paragraph, and are usually charitable whether or not they are conducted in an ECC. For example:

- providing affordable housing to the poor, or specially adapted housing for the aged and the disabled;
- providing community facilities, such as a hall, park, or a multi-sport recreational centre;
- providing cultural facilities, the opportunity to see artistic works, or training in the arts and crafts;
- preserving heritage properties owned by the organization or a qualified donee such as a municipality;

#### Note

“Qualified donees” are those organizations (other than political parties) that can issue official donation receipts to their donors. For practical purposes, qualified donees are primarily other registered charities, although other categories exist, such as municipalities.

- beautifying and preserving natural sites; and
- training volunteers.

However, people working to improve socio-economic conditions in an ECC may also focus on problems particular to such communities. In considering whether their activities are charitable, the usual considerations apply. For example:

- Agencies created by a community-based organization to address a social need (sometimes referred to as community businesses) cannot be assumed to be charitable. In many service sectors, charities and for-profit entities operate side-by-side. A nursing home, for instance, can be run on either a for-profit basis or a charitable one.
- Building or retaining a community’s infrastructure of professional and commercial services, such as a general store, bank, post office, doctor or dentist, may be important for the continued viability of the community. However, when determining charitable status, the issue is whether the absence of these services is creating suffering among the people of the community. It would be necessary to demonstrate more than inconvenience.



- It may be possible, for instance, to establish a connection between a lack of health professionals and documented distress in a community. Being able to provide needed medical services in an ECC is often a question of attracting health professionals to an area that they regard as undesirable for reasons of remoteness, lower economic returns, and burden of work. We recognize that the public benefit can sometimes greatly outweigh any private benefit conferred on the health professionals in these situations, such as providing them with a low-rent clinic out of which to operate.
- Whenever potential private benefit is at issue, each case has to be examined on its own merits: Is there (or would there be) actual suffering if the service was not locally available? How necessary is it to offer an inducement in order to obtain the service? Is the inducement no more than is necessary?
- Community mobilization is considered essential to a successful CED strategy. This is based on the assumption that a community can only hope to overcome its problems through the combined efforts and resources of the entire population.
- Fostering social interaction in a geographic community as a by-product of other, charitable programs, is certainly acceptable. However, as a dominant purpose, it would extend beyond the limits of charity. A social club is not charitable, nor is the pursuit of a political purpose. We also reject barter systems for exchanging goods and services of commercial value, unless an organization has an appropriate mechanism in place to ensure compliance with the relevant tax laws.

It may be that in areas of cultural breakdown and despair, some measures—such as the communication of information—can stand on their own as charitable even though this would not be the case in less distressed communities.<sup>5</sup>

However, many programs that can pull a community together are clearly within the bounds of charity. To cite one imaginative example from the Charity Commissioners (*Report, 1978: 29-30*):

The area was a deprived one with economic depression, unemployment, low incomes, social stress, vandalism, high crime rates, unbalanced population structure and a high proportion of immigrants. The facilities to be provided included a community garden, a farmyard, a nature reserve, a riding school and an area for outdoor drama and sports, a community workshop, and a pre-school play centre. . . .

The workshop would have a comprehensive range of equipment suitable for metal work and crafts. It would be open to all comers, who would learn from the more experienced and would have the opportunity to use equipment which, if it were not provided on this communal basis, they were unlikely to have the opportunity to handle. . . . An “auto repair” area would be provided for the servicing of cars, vans, boats, and play centre and farming equipment. Organised courses of instruction would be provided, and small charges made to those wishing to use the facilities to repair their own property, with or without guidance. . . .

The Commissioners also noted that the usual bar to self-help or members’-benefit organizations does not apply to a first-head charity such as this one.

#### Note

The purpose of a charity must be to help others, not its members. This rule is relaxed only for first-head charities.

## Promoting industry and trade

Promoting industry and trade for the benefit of the community (i.e., the public at large) is an acknowledged charitable purpose. However, organizations often have difficulty finding a way of accomplishing this purpose without conferring a more-than-minor private benefit on individuals or corporations engaged in industry and trade. The case law offers limited examples, only one of which is directly relevant to community-based organizations.<sup>6</sup>

The courts have specifically sanctioned the promotion of agriculture and craftsmanship in this context. However, apart from these two examples, we do not accept the promotion of any other industry as charitable. It appears impossible to advance a particular industry, such as car manufacturing or tourism, without at the same time conferring an advantage on those who make their living from making cars and serving tourists.

Nevertheless, the presence of a board that represents the various sectors of a community (as opposed to a board dominated by representatives of only one sector) may indicate that the organization is established for the benefit of the public at large. A number of CED organizations have boards that are explicitly structured to enable the organization to co-ordinate various local interests. Groups represented could be employers, labour, non-profit organizations, government, and educational authorities.

<sup>5</sup> In *Native Communications Society of B.C. v. MNR* ([1986] DTC 6353 at 6358, emphasis added), Stone J. commented: “it is apparent that the newspaper is used more than as a mere vehicle for conveying news. An examination of its pages shows that through them its Indian readers are made aware of activities of a cultural nature going on elsewhere in the wider Indian community and of attempts being made to foster language and culture as, for example, through greater use of native languages and the revival of ancient crafts, music and story telling. All of this may well instill a degree of pride of ancestry in the readers of ‘Kahtou’, deepen an appreciation of Indian culture and **thereby promote a measure of cohesion** among the Indian people of British Columbia that might otherwise be missing.” [Emphasis added]

Two years later, MacGuigan J. in *NDG Neighbourhood Association v. RCT* ([1988] DTC 6279 at 6281) considered “there may well be an argument that an organization similarly dedicated to the interests of the urban disadvantaged as the British Columbia society was to the interests of the native people should qualify as a charity. But, on the facts, this is not such a case.” The Association’s focus was not limited to the urban disadvantaged.

<sup>6</sup> See the discussion of *IRC v. Oldham Training and Enterprise Council* ([1996] BTC 539) in “Existence of a private benefit” on page 10.

Whether or not these community-based organizations can be registered will depend on the type of programs delivered and whether the organization is itself delivering the programs or is simply an umbrella group co-ordinating the work of others.

#### Note

Apart from funding bodies, the Act permits us to register only organizations that carry on charitable activities themselves. Umbrella or facilitator organizations are generally not eligible, unless they are co-ordinating the work of a group of charities.

From the case law, the following are charitable programs:

- Research conducted to establish the socio-economic profile of a community, to assess its socio-economic strengths and weaknesses, and to identify potential economic opportunities can be charitable under the second head (advancement of education). It would, however, be necessary for the research to be made public and be conducted in the form of an open-minded enquiry, rather than as a marshalling of evidence that supports a cause or a particular business interest.
- Holding exhibitions, open to the public, of a community's products and services, with prizes awarded to promote excellence, and demonstrations held both to enable spectators to learn about the community's industries and to showcase new advances in technology.
- Other methods that encourage excellence in products and services, such as a competition open to all businesses in the community, the creation of standards, and the creation of new scientific and technological knowledge and its dissemination.

## Factors negating charitable registration

### Existence of a private benefit

Subsidies are sometimes provided to established businesses to encourage them to locate in ECCs, or local businesses are provided with free or low-cost services, grants, or loans (or investment funding) to keep them in an ECC. We consider these activities to be non-charitable because the private benefit to the businesses concerned outweighs the public benefit. This position is based on *Hadaway v. Hadaway* ([1954] 1 W.L.R. 16), which held that a fund for making loans to needy agriculturalists was non-charitable because of the private benefit conferred, and on *IRC v. Oldham Training and Enterprise Council* ([1996] BTC 539). Since the latter case is the closest the courts have come to considering CED, it may be useful to look at it more closely.

It was conceded that much of what Oldham TEC did was charitable; only one aspect of its program was in dispute. In citing the organization's purposes and activities below, we have used bold characters to identify the disputed area.

Oldham TEC was established:

... to promote and provide vocational education and retraining of the public, to improve the skills of the

workforce and to **promote the development of industry, commerce and enterprise of all forms for the benefit of the community in and around Oldham** and in furtherance of these objects . . . to:

- (1) examine the local labour market and assess key skill needs, prospects for increasing local employment and the adequacy of existing training opportunities;
- (2) devise, implement and monitor local training, education and work experience programmes for young people, unemployed people and adults requiring new knowledge, skills and technical training;
- (3) **develop, secure and provide training, advisory, consultative and other support services and advice to and for local businesses;**
- (4) **promote the development of existing businesses and the establishment of new businesses.**

Oldham TEC's activities were summarized as follows:

- (1) **Enterprise services, which include information and advice to businesses, diagnostic services (assessment of a business's strengths and weaknesses and opportunities for development) and business skills training (planning, financial management, identification of new markets, etc.).**
- (2) Business start-up services, which include a free enterprise training scheme for anyone thinking of setting up a new business (in such subjects as marketing and bookkeeping) and a cash allowance of up to £60 per week for people setting up new businesses. To qualify for such an allowance (which is in lieu of any unemployment or social security benefits) the recipient must:
  - have been unemployed for at least six weeks,
  - be starting a business judged by Oldham TEC to have potential for the employment of more persons,
  - have attended a business training scheme and be able to produce an acceptable business plan, and
  - have access to sufficient capital.
- (3) Training, which includes training young people for work and re-training unemployed people.

The court found the purposes and activities in bold to be non-charitable:

[The third main object, read in the light of the third and fourth subsidiary objects] on any fair reading must extend to enabling Oldham TEC to promote the interests of individuals engaged in trade, commerce or enterprise and provide benefits and services to them. [The organization's description of its activities under "Enterprise services" shows it does provide such benefits.] . . . Such efforts on the part of Oldham TEC may be intended to make the recipients more profitable and thereby, or otherwise, to improve employment prospects in Oldham. But the existence of these objects, in so far as they confer freedom to provide such private benefits, regardless of the motive or the likely beneficial consequences for employment, must disqualify Oldham

TEC from having charitable status. The benefits to the community conferred by such activities are too remote.

The ban on private benefit would also disallow another program mentioned in CED literature—**flexible manufacturing networks**. These are intended to strengthen the competitiveness of small-to-medium sized enterprises by linking them collaboratively to share resources, solve common problems, and jointly market their products.

A further concept found in the literature is the **business incubator**. These provide space, shared facilities, support services, and business advice to new businesses to improve the survival rate of business start-ups. Again, because of the private benefit to the businesses concerned, we would generally not recognize business incubator programs as charitable. However, as an adjunct to a micro-enterprise program run by a first-head charity, we accept that such a supporting framework can be necessary to the success of the program.

## Political purpose

To some, community development is clearly a political movement, resting on an analysis of global trends which indicate that people can no longer rely on the state or the multinational economy to serve their needs. It is argued that people must organize locally to acquire the political and economic power to preserve the autonomy and continuing viability of their communities.

The word “empowerment” appears in two contexts: one refers to the empowerment of individuals, the other to the empowerment of communities.

Individual empowerment usually means addressing helplessness, social isolation, and lack of self-esteem by involving people in the day-to-day decisions that affect their lives. As such, it can be charitable as relieving the needs of poor, unemployed, or disabled individuals.

Community empowerment is a process of organizing and mobilizing the community so that it can gain control of its destiny. However, there is a distinction between countering community demoralization (which can be addressed in part by many well-established charitable programs) and organizing the population specifically to enhance its influence in the economic and political realms. The latter appears clearly to be what the law would regard as a political and, therefore, non-charitable purpose.

Yet, leaving aside the political reasoning and examining what an organization is actually doing may lead to the conclusion that it is delivering a charitable program. As such we may be able to register it even if the initial motivation behind its creation was political. However, if registered, it will have to operate as essentially a non-political entity, although common law and the *Income Tax Act* do allow otherwise charitable entities to engage in a limited amount of political activity.

## Objects not fully charitable

CED is a relatively new concept, the meaning and scope of which practitioners are still exploring. We must expect that it will evolve in unforeseen ways or directions. The organizations that embrace CED often adapt their programs

as sources of government funding change. These are also typically organizations struggling with intractable problems, such as the challenges faced in an ECC, and who use their inventiveness to try one imaginative solution after another.

In reviewing the formal objects of CED applicants, we have to seek a balance between, on the one hand, not stifling what could be valuable experimentation and, on the other hand, obtaining a reasonable degree of certainty that the organization is not empowered to stray into non-charitable fields.

Formal objects are the statements of purpose contained in an organization’s governing documents. They sometimes also specify the type of activities it will undertake to achieve its purposes. When we review applications, we see purposes that are:

- charitable;
- stated broadly or imprecisely, with the result that they do not prevent an organization from straying into the non-charitable realm; and
- non-charitable.

### Note

Examples of broadly-stated purposes are:

- to improve the conditions in life of the local citizens;
- to enhance the social, economic, and environmental health of the community; and
- to promote the well-being of native people.

Ideally, formal objects should start with a clear statement of charitable purpose, followed by a limitation describing how the organization intends to achieve that purpose. For example:

- to relieve need amongst the unemployed in the region of A by providing training, job searches, and micro-lending programs;
- to undertake research on the socio-economic structure of A, including needs assessment surveys; or
- to enhance the environment of A by cleaning up toxic wastes in the vicinity.

### Note

Sometimes a further purpose, often stated in broad terms, is tacked on to the end of objects formulated in this way: “to relieve the needs of persons with developmental disabilities by providing them with employment to the end of upholding their dignity as human beings.” Technically, this is a better formulated object than the converse which starts with the broadly stated purpose: “to uphold the dignity of persons with developmental disabilities by operating an employment program that will provide for their social and economic needs.”

Formal objects are often in the form of: “To achieve [some very broadly stated purpose] by doing X, Y, and Z.” If the evidence submitted on the organization’s activities substantiates that X, Y, and Z are indeed charitable programs, we will judge whether to accept the organization as is or whether to require a clarification of the object.

However, we will likely reject such an applicant if the directors are also given a wide discretion to select the organization's course of action, such as if the directors are empowered "to do such further things as will achieve the organization's goals."

Formal objects may simply be broadly stated, with no attempt to restrict their application to defined areas of activity. For example, the following objects are too broad for us to accept:

- to unite the unemployed and jobless to the end of promoting their social and economic interests;
- to study, promote, protect, and develop in any way the social and economic interests of its members; and
- to offer the population of region A assistance and consultations on any questions or procedures relating to the rights of workers, with or without employment.

The second and third do not confine the organization to providing services to those in need; the second raises the issue of members' benefit; and all three do not preclude the organization from straying into political waters. An acceptable main object for a group helping the unemployed obtain the Employment Insurance benefits to which they are entitled would be:

- to offer the unemployed of region A assistance and consultations on any questions or procedures relating to their rights in regard to Employment Insurance.

We reject applicants with formal objects that are clearly non-charitable. These would include objects along the lines of:

- to promote the economic development of region A;
- to promote tourism in region A;
- to create employment and diversify the economy of region A;
- to attract new businesses to region A and assist existing businesses to expand; and
- to assist the development of co-operatives and other forms of community-owned enterprises.

#### Note

Entities structured as co-operatives are generally not themselves eligible for consideration as charities because they confer a benefit on their members.

## Funding non-qualified donees

The *Income Tax Act* requires registered charities to use their resources either on their own charitable programs or to make gifts to other qualified donees. Thus, a registered charity cannot transfer its assets to a non-qualified donee.

However, a charity can enter into a contract with a non-charity to have the latter perform services on the

charity's behalf. Our policy is strict in this area—there should be a written agreement in place that clearly sets out what the non-charity is expected to do in return for the payment or other advantage it will be receiving from the charity. The non-charity has to report back to the charity in enough detail that the charity can show it is controlling the use of its funds and can account for them.

## Other issues

### Related business

Charities are not businesses. The key distinction is not so much one of corporate structure as the purpose of the entity concerned: a charity exists to confer a benefit or gift on the community, while the purpose of a business is to make a profit. Charities can and do charge fees for their charitable programs, but when their fees are high enough that they exclude those in need of the service or provide a return above the break-even point,<sup>7</sup> it raises the question of whether their purpose is indeed charitable. A key to identifying whether a training business or social business is a charitable program in its own right (as opposed to a potentially "related" business) is to determine whether its focus is on helping the clientele or on making a profit.

The question of related business (as opposed to charitable programs for which a fee is charged) arises in the context of allowable business activities for an organization seeking to raise funds for its charitable programs. The *Income Tax Act* allows all charities except private foundations to carry on related businesses; by implication, it bars unrelated businesses.

Distinguishing between related and unrelated businesses is often difficult. The following summarizes our current position.

- Any business "substantially all" the staff of which are volunteers is deemed by the Act to be a related business. As a rule of thumb, we interpret "substantially all" as meaning 90%.
- A charity can seek to profit from the temporarily idle capacity of specific equipment, property, or expertise used in delivering the charity's core programs. Classic examples are churches renting out their parking lots during the week and universities renting accommodation in their student residences during the summer.
- A charity can seek to profit from the sale of by-products of its charitable program, for example, a symphony orchestra selling recordings of its performances.
- Certain business operations have gained community acceptance as a useful ancillary service to a charitable program, such as a church operating a religious bookstore, a museum opening a gift store, or a hospital running a cafeteria or "medical arts" building.

<sup>7</sup> A charity can, however, subsidize a particular charitable service by charging some of the clientele for this service a fee set at a profit-returning level. *CIR v. Peebleshire Nursing Association* (1927) 11 T.C. 335. Cf. *Everywoman's Health Centre v. MNR* ([1992] DTC 6001 at 60): "Any surplus [from the fees charged] or charitable donations are to be used to reduce charges to patients. [The Centre] does not charge women a fee if they cannot afford to pay."

## Program related investments

Program related investments are integral to the concept of community economic development as developed and practised in the United States. A program related investment (PRI) is:

- an investment rather than a grant, most often in the form of an interest-bearing loan but also by purchase of shares in an enterprise;
- made to an organization, usually but not necessarily a charity, since U.S. law accepts the concept of expenditure responsibility under which non-charities (including for-profit businesses) can receive charitable funds if steps are taken to ensure that the recipient applies the funds for charitable purposes only;
- funded with money from a foundation's endowment funds; and
- for the primary purpose, not of income-generation, but of furthering the foundation's charitable purposes.

In Canada, trust law would require that a charity be authorized by its objects to confer a benefit such as a PRI on another entity. Provincial law on the investments open to charitable trustees must also be considered.

Canadian tax law would require limiting the recipients of PRIs to qualified donees. Canada does not employ the expenditure responsibility concept, relying instead on specifying **qualified donees** to identify the organizations that can benefit from the use of charitable assets. Thus, a PRI made to a qualified donee would be acceptable, while a PRI made to a non-qualified donee, such as a for-profit organization, would not.

Another tax law limitation is that registered charities designated as public or private foundations cannot hold a controlling<sup>8</sup> interest in a company. Ontario's *Charitable Gifts Act* also restricts charities to holding no more than a 10% "interest in a business that is carried on for gain and profit."

How could a PRI be accounted for in the Canadian disbursement quota? As noted previously, the Canadian disbursement quota requires a charity to make certain expenditures (see the section called "Loans and expenditures" on page 7). Yet, in making payments such as bridge loans or loans to community loan funds, the lending charity is carrying on a charitable activity of its own in promoting the efficiency and effectiveness of the recipient charity. As property "used directly in charitable

activities," a foundation can thus deduct the amount of the loan from its investment assets, and accordingly reduce the part of its quota based on investment assets. At the same time, we will treat the opportunity cost to the charity in making the loan<sup>9</sup> as an expenditure that it can apply towards meeting its quota.

## Community land trusts

Community land trusts are a relatively new tool in the CED arsenal. A community land trust (CLT) is set up to take land out of private hands and ensure that it will continue to be available for community purposes. CLTs operate by purchasing and developing properties and leasing them to local homeowners and businesses.

CLTs may or may not be charitable. We have declined to register a CLT holding title to an industrial park, but we may be able to register a CLT that provides housing for the needy. However, until we learn more about how such CLTs typically operate, each application will have to be judged on its own merits.

A CLT that held what the Act defines as "ecological" land would probably be considered charitable.

### Note

That is, land that the federal Minister of the Environment certifies to be important to conserve and protect in the interest of preserving the country's environmental heritage. See the definition of "ecological gifts" in subsections 110.1(1) and 118.1(1) of the Act.

## Corporate structure for non-charitable programs

Non-charitable programs can be "housed" in a legal entity that is separate from the charitable body. However, it is essential that there be a financial firewall between the two bodies, so that the charity's assets can in no way be used to benefit the non-charitable entity. The separate interests of the two entities should also be reinforced by such other boundaries as:

- separate boards, or at least a situation in which the charity's board is not controlled by members from the board of the non-charitable entity;
- distinctive names to avoid public confusion;
- separate membership or shareholders; and
- separate equipment, personnel, and space.

<sup>8</sup> Paragraph 149.1(12)(a) of the Act defines "control" in this context as follows: "[A] corporation is controlled by a charitable foundation if more than 50% of the corporation's issued share capital, having full voting rights under all circumstances, belongs to the foundation, or the foundation and persons with whom the foundation does not deal at arm's length." However, foundations may acquire control of a corporation if they receive the shares as a gift and they have not previously "purchased or otherwise acquired for consideration more than 5% of the issued shares of any class of the capital stock of that corporation."

<sup>9</sup> That is, the amount of the loan **multiplied by** the difference between the following two interest rates: the interest rate the charity could earn if it invested the amount in T-bills or GICs, and the interest rate the charity is receiving on the amount.

We will use subsection 149.1(5) to treat the opportunity cost of making a PRI loan as if it were an expenditure on charitable activities. The amount should be reported on line 832 of the charity's annual return ("Deemed expenditure: special relief amount"). In the case of PRI loans, we will also consider an amount placed on line 832 as fulfilling the requirement in subsection 149.1(5) for "an application made to the Minister on prescribed form," as long as "PRI loans" is written beside the entry at line 832.

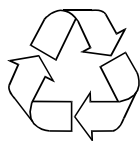
**Note**

The charity could still control the non-charitable entity. For example, if the non-charitable entity had a three-member board, two of those members might also sit on the board of the charity and thus ensure the business was operating for the benefit of the charity. The desirable control, in this example, would be for the charity's board to number at least five persons, so that the two members sitting on both boards could not outvote those with a concern only for the charity's interests.

We understand that the non-charitable entity can be set up as a share-capital corporation, controlled by the charity, in all provinces except Ontario.



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