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Good Government Act: Good News for Ontario Charities seeking to generate Ancillary Revenue

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That sound of joy you heard on December 15, 2009? It was not just that of retailers revelling in the success of seasonal promotions. No, for charities in Ontario, the sound evidenced their collective relief at the passage of Ontario's Bill 212, *An act to promote good government by amending or repealing certain Acts and by enacting two new Acts*, or the *Good Government Act*, in short. *The Good Government Act* jettisoned one statute long the bane of Ontario charities seeking to generate ancillary revenue through investments in subsidiary corporations. It also amended other statutes relevant to the "business" activities of Ontario charities.

Across Canada, the activities of charities are regulated by the Charities Division of the Canada Revenue Agency ("CRA"). The Division has dozens of policies and guidelines to assist charities in complying with the provisions of the *Income Tax Act* (Canada), the statute that provides for their tax free status and their ability to issue charitable receipts. In Ontario, charities are also regulated by the Public Guardian and Trustee (the "PGT") who administers provincial statutes that apply to charities operating in the province including the *Charities Accounting Act*, the *Charitable Gifts Act* and the *Accumulations Act*. These statutes impose constraints on Ontario

charities operating in Ontario not applicable to charities operating in other provinces.

Charitable Gifts Act

CRA has long recognized the ability of charities to raise funds other than through charitable donations, either through investments or by carrying on related businesses. Canadian charities operating outside of Ontario were free to incorporate subsidiaries to carry on such activities. Most charities operating in Ontario could not easily do so. The *Charitable Gifts Act* provided that a charity was required to dispose of any interest of greater than 10% that it acquired in a business that was carried on for gain or profit, within seven years of its acquisition. It went on to define an interest in a business to include most types of indirect interests.

The constraints of the *Charitable Gifts Act* were particularly significant for charities which could have carried on a related business directly in compliance with the *Income Tax Act* and the *Charitable Gifts Act* but could not generally carry on the business indirectly through a subsidiary without running afoul of the provincial statute (unless their interest in the subsidiary was less than 10% or unless the subsidiary corporation was prepared to

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dispose of that interest within seven years of its acquisition). This was the case despite the fact that the use of a subsidiary corporation to carry on the ancillary business was based upon sound risk management or business efficacy principles. For Examples include, where the activity undertaken would have exposed the charitable assets to undue risk or where the charity was seeking to carry on the business with a third party investor. Elaborate arrangements based on highly technical interpretations of the *Charitable Gifts Act*, were resorted to in order to provide charities with a legitimate means to meet their objectives. No longer will such arrangements be required.

The *Charitable Gifts Act* has now been repealed by Section 10 of the *Good Government Act*. For any charity that may have been in contravention of its provisions prior to its repeal, the *Good Government Act* provides relief to them as well. Section 14 of the *Good Government Act* provides that the repeal of the *Charitable Gifts Act* extinguishes all obligations under that Act to dispose of an interest in a business that was in existence at the time of repeal.

Charities Accounting Act

The *Charities Accounting Act* contained provisions which were relevant for charities seeking to hold investments in subsidiaries. While the Act did not place limitations on the ownership of investments, it did require corporations controlled by trustees and executors to report to the PGT, as requested, on the operations, assets, profits, losses and finances of such corporations.¹ The provisions were relevant to charities because the *Charities Accounting Act* provided that any corporation incorporated for a religious, educational, charitable or public purpose was deemed to be a trustee with the meaning that Act.² Unfortunately, that section of the *Charities Accounting Act* was not repealed by the *Good Government Act*. Accordingly, the ownership interest of charities in

corporations continues to be subject to the reporting obligations of that Act.

The expression “what the Lord giveth, the Lord taketh away”, holds true in this regime with the government, of course, being the giver and taker. For while the repeal of the *Charitable Gifts Act* now allows charities to hold investments in corporations, the *Charities Accounting Act* now requires charities to report, when requested by the PGT, on all such investments—and not just investments in for-profit corporations but also “investments” in non-share capital corporations, partnerships, trusts and “other entities”. Furthermore, the investment level that triggers the reporting obligation has been reduced from one of control to generally a 20% interest, determined based on direct or indirect interests, whether held alone or through one or more persons, entities or both.³

In addition, the *Charities Accounting Act* placed constraints on the ability of Ontario charities to earn revenue through the use of excess land. Section 8 of that Act formerly provided that land held by a charity that was not used for the actual use and occupation for the charitable purpose of the charity for a period in excess of three years and was not then required or would not be required for such purposes, could be seized by the PGT.⁴ Among the difficulties with the provision was the uncertainty that arose as to whether it was necessary for the charity itself to use its real property for its charitable purposes or whether the act was complied with if a charity leased the land to a third party to use it for a purpose that was consistent with the charitable purposes of the charity that owned the land. The consensus among practitioners (although the conclusion was not tested by the courts) was that the property could be leased to a third party to use it for the charitable purposes of the landlord charity but it could not be leased to simply generate ancillary income which would allow the charity landlord to meet its charitable purposes.

¹ Section 2(2)

² Section 1(2)

³ Section 11(3) New Section 4.1(4) of the *Charities Accounting Act*

⁴ Section 8(2)

Section 8 of the *Charities Accounting Act* has been repealed by the Good Government Act. However, the positive obligation of the charity to use its land for its charitable purposes has for all intents and purposes been maintained and has been expanded to apply to personal property as well as real property. The new Section 8 reads as follows:

A person who holds an interest in real or personal property for a charitable purpose shall use the property for the charitable purpose.

On its face the language is no clearer as to whether it allows the property to be leased to a third party simply to generate ancillary revenue. Notwithstanding this, however, during the public review of the draft statute, the PGT indicated that in its view the use of the property to generate ancillary income to be used to carry out the charity's objects was acceptable even if the lease payments were generated through a use of the land unrelated to the charity's objects. Whether such an interpretation will be observed by subsequent PGTs or the courts has yet to be seen.

Accumulations Act

A final change effected by the *Good Government Act* was the amendment of the *Accumulations Act* to provide that it will no longer apply to charitable trusts. Where a charitable trust provided for the accumulation of income for a period greater than 21 years from its establishment, the statute provided that thereafter income must be distributed to the person entitled to it. Most practitioners took the position that charitable trusts, being to benefit a purpose not a person, were

outside the scope of this statute. Schedule 2 of the *Good Government Act* provides that:

The rules of law and statutory enactments relating to accumulations do not apply and shall be deemed never to have applied to trusts created for a charitable purpose, as defined in section 7 of the *Charities Accounting Act*.

This change provides welcome certainty to many charities choosing to carry on their ancillary business activities through charitable trusts or to charities that are established as a trust.

All in all, the *Good Government Act* is a good Act for Ontario charities as it has removed two impediments to structuring arrangements for the carrying on of ancillary businesses. Such arrangements continue to be challenging though and charities are urged to involve their legal and financial advisors as they plan to engage in such activities.

For more information on the subject of this bulletin, please contact the authors.

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