RELEASE DATED APRIL 21, 1982 FROM THE OFFICE OF THE HONOURABLE ALLAN J. MacEACHEN

The Honourable Allan J. MacEachen, Deputy Prime Minister and Minister of Finance, today announced revised rules relating to minimum disbursements for charitable purposes by public and private foundations, and to financial transactions between foundations and related persons.

These rules are being proposed as a result of extensive consultations held between the Minister of Finance and members of various charitable foundations, who have given the revisions their full support. Mr. MacEachen stated that the consultations had proved "very worthwhile".

"The revisions now being proposed address the main concerns expressed by foundations about the impact of the November 12 budget while at the same time fulfilling the objectives of the original proposals," he said.

Disbursement Requirements

Foundations have been basically required to disburse 90 per cent of their income for charitable purposes. The budget proposed that the full amount of capital gains and losses be included in computing the income subject to this disbursement requirement.

The foundations submitted that this would lead to attrition of the capital base supporting their charitable purposes. In response to these representations, the Minister now proposes that foundations be required to make annual disbursements of at least 4.5 per cent of the fair market value of all their investment assets.

This minimum disbursement requirement will replace the present test of 90 per cent of income. Thus disbursements will no longer depend upon either the form or the amount of investment income realized.

In order to minimize the adverse impact of fluctuations in asset values, disbursement in a single year will be based upon the average value of a foundation's assets in the previous two fiscal years. If a foundation fails to disburse the required amount in a given year, a tax of 15 per cent of the deficiency will be imposed. If, after receiving a notice of deficiency, a foundation fails to make the required distribution within a reasonable, specified period of time, additional tax equal to 100 per cent of the deficiency will be imposed.

The new disbursement requirement will become effective for fiscal years beginning in 1983. The pre-budget rules will continue until that time. Those foundations that claimed a reserve in their last fiscal year under the pre-budget rules will be permitted to disburse this reserve over the next 10 years provided they disburse at least one-tenth of the reserve each year. Assets used by the foundation in charitable activity or in the administration of the foundation, and funds being accumulated for a specified purpose with the permission of the Minister of National Revenue, will not be included in the base for calculating the disbursement requirements.

Non-Qualified Investments

Prior to the budget, the Income Tax Act required that private foundations disburse an amount equal to the greater of 90 per cent of income or five per cent of the fair market value of non-qualified investments, which included loans to persons related to private foundations or equity investments in private corporations. This rule was difficult to enforce and could be used to confer benefits on persons related to the foundation.

Under the new rules announced by the Minister, the 4.5 per cent disbursement requirement will apply to all investment assets, qualified as well as non-qualified. There will, however, be special rules for non-qualified investments which will be defined as investments in which there is a potential for self-dealing between the foundation and related persons. Loans to related persons will be required to earn interest each year at a rate equal to, or greater than, the prescribed interest rate on the cost amount of the debt. The prescribed interest rate is the rate charged by Revenue Canada on tax arrears and paid on tax overpayments. Investments in share capital of related corporations will be required to earn dividends of at least two-thirds of the prescribed interest rate on the cost amount of the shares. These rules will be effective for any transactions after April 21, 1982.

If a foundation has non-qualified investments that do not meet these requirements, a special penalty will be imposed.

Transitional relief will be available for existing non-qualified investments which continue to be non-qualified under these new rules. Commencing with fiscal years beginning in 1983, this special penalty will not be imposed if interest payable on outstanding non-qualified debt is increased by two percentage points each year until it equals the prescribed interest rate for the year. For the special penalty not to be imposed on non-qualified share investments, foundations will be required to earn dividends of at least four per cent of the higher cost or fair market value commencing with fiscal years beginning in 1983, and increase the earnings on such shares by one percentage point every five years until the rate equals two-thirds of the prescribed rate.

The Minister stated that further details of these provisions will be included in the budget legislation.

The Minister said the new rules meet the objectives of the proposals in the budget while addressing the concerns identified by the foundations. The government recognizes the importance of charitable foundations in the voluntary sector in Canada and will continue to provide them encouragement to fulfill this role.