

New Tax Proposals for Charities

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In the following pages we reproduce a press release from the Department of Finance announcing the intention of the Minister of Finance to introduce new rules regarding the tax treatment of charities, which will be effective for taxation years commencing after 1983.

Although the legislative and regulatory proposals are not yet available, it is evident from the press release that the Minister has responded very favourably to the many submissions placed before the Department of Finance in response to, first, the proposals contained in the November 1981 Budget, and, subsequently, to the proposals of the Discussion Paper issued in May, 1983.

In general the new rules for foundations reflect the terms of the agreement reached between the Department and the Association of Canadian Foundations in April, 1982. The rules for charitable organizations will be essentially the same as the existing rules with some favourable modifications. Both charitable foundations and charitable organizations will be gratified to learn that the legislative distinction between the two categories of foundations and charitable organizations will be maintained.

The majority of charitable organizations responding to the Discussion Paper proposals expressed concern over the complex proposals related to the concepts of "related charities" and "major donor". These proposals have been dropped as has the proposal to apply a penalty tax on deficiencies in the required disbursement quota.

A proposal in the November 1981 Budget that charities should be designated as either "private" or "public" foundations or as "charitable organizations," which was dropped from the May 1983 Discussion Paper, has been re-introduced.

The Minister of Finance is to be commended for the Department's extensive consultations with many charitable groups and for now developing a set of rules which appear to be very satisfactory to both foundations and charitable organizations.

Release

Communiqué

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PROPOSED CHANGES TO RULES FOR TAXATION OF CHARITIES ANNOUNCED

The Honourable Marc Lalonde, Minister of Finance, today announced his intention to introduce revised rules regarding the taxation of charities. This announcement culminates a process of consultation on the discussion paper "Charities and the Canadian Tax system" issued by the Department of Finance on May 17, 1983.

The revised rules are intended to accommodate the major concerns raised during extensive consultations with charitable groups and at the same time deal with the issues addressed in the discussion paper.

Mr. Lalonde expressed his thanks for the helpful advice received by the government from many charitable groups through the discussion process. "Their assistance has contributed greatly towards the proposals we are now putting forward," the Minister said.

Using the existing provisions of the Income Tax Act wherever possible, the revised rules will implement, with some modifications, the agreement reached with charitable foundations regarding minimum disbursement requirements, as announced on April 21, 1982, and will generally maintain the existing system for charitable organizations.

It is intended that the revised rules will be effective for taxation years commencing after 1983, with appropriate transitional rules. Draft legislation will be made available for public review before the final legislation is submitted to Parliament.

The proposals deal with four main issues:

1. Classification

The existing categories of charities will be maintained and new charities will be required to register as either a private foundation, a public foundation or a charitable organization. Existing charities will be designated by Revenue Canada according to the information it has on file and they will have a period of time to appeal this designation. In addition, registration requirements will be slightly modified. In the case of new and existing public foundations and charitable organizations, more than 50 per cent of the directors, officers and trustees will be required to deal with each other at arm's length. For existing charitable organizations, however, this requirement will be effective for their taxation years commencing after 1984.

For new public foundations and charitable organizations, an additional requirement will be imposed that not more than 50 per cent of the capital contributed can be so contributed by any one person or by a non-arm's length group of persons (except governments and their agencies, municipalities and charities which are not private foundations). Those charities that do not meet these requirements will be classified as private foundations.

2. Disbursement Quota

The disbursement quota for charitable organizations will be 80 per cent of the previous year's receipted donations (other than endowments and testamentary gifts). The disbursement quota for charitable foundations will be 80 per cent of the previous year's receipted donations (other than endowments and testamentary gifts), 80 per cent of the previous year's gifts from other charities (other than gifts out of capital), and 4.5 per cent of the value of investment assets. Where a charity fails to meet its disbursement quota, the existing sanction of possible de-registration will apply rather than the special tax as proposed in the discussion paper. However, charities will be able to carry over excess disbursements in one year against any disbursement deficiencies in other years and will also be permitted to apply to the Minister of National Revenue for a reduction of their disbursement quota where the circumstances warrant.

3. Non-qualified Investments

Private foundations will be required to earn a minimum rate of return on certain non-qualified investments, as set out in the agreement of April 21, 1982. Where the minimum return is not met, a penalty will be imposed to the extent of the deficiency. Among the exclusions from these rules will be shares which are listed on a prescribed stock exchange and certain qualifying equity shares of Canadian private corporations.

4. Anti-avoidance Rules

Anti-avoidance measures will be included to prevent the shifting of property among charities for the purpose of minimizing or delaying their disbursement requirements. This will be accomplished by a rule which scrutinizes a pattern of gift-making as between charities and another rule which prevents capital transfers in excess of 50 per cent of a charity's capital without the approval of the Minister of National Revenue. Further, private foundations will not be able to fulfill their disbursement quota by making gifts to other private foundations.

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