

SUMMARY OF RECOMMENDATIONS

The Commission sets out a general summary of the recommendations for reform contained in this report. We do not provide a detailed list of all the recommendations in this report, since most of them relate to very specific and detailed changes to the various areas of the law. In Recommendation 35, we recommend the establishment of a government agency to oversee the work of the sector. We call it the "Nonprofit Organizations Commission", "NOC" for short. We introduce that recommendation at this juncture because we refer to this agency in the earlier recommendations.

CHAPTER 1: INTRODUCTION AND BACKGROUND

1. A comprehensive rethinking, redrafting and re-organizing of the laws governing nonprofit organizations in Ontario is required. Much of the current legal framework is anachronistic, confused and contradictory. As a consequence, the government of Ontario is not currently fulfilling its traditional facilitative and protective mandate in the sector.
2. The comprehensive reform of the legal framework recommended by the Commission in this report should only be effected after extensive further consultation with the nonprofit sector.
3. The government's involvement in the sector should be motivated by the following objectives:
 - (1) to facilitate nonprofit activity and protect it from fraud and waste;
 - (2) to ensure that government support of the sector through grants and favourable tax treatment is not abused;
 - (3) to protect the sector from being used as a front for profit-motivated activities;
 - (4) to help maintain a variety of agencies capable of delivering publicly funded social and cultural programs; and
 - (5) to aid in the development of intermediate level social institutions whose existence will serve to enrich the lives of the people of Ontario.

CHAPTER 2: PREVIOUS STUDIES

4. Since governments in Canada have never attempted a systematic evaluation of the role of the nonprofit sector in Canadian society, the reforms recommended in this study should proceed only after further comprehensive consultation with the sector. Initially, the increased role of government in the sector, recommended in this report, should be careful not to be too ambitious. A more extensive reform effort should await the development of greater government expertise and greater confidence on the

part of the sector that the government's contribution to the work of the sector can be positive.

5. To the extent that the reforms recommended in this study draw on the experience of other jurisdictions, their implementation in Ontario should remain cognizant of the important and substantial differences between the situation in Ontario and the situation elsewhere, especially in the United Kingdom and the United States.

CHAPTER 3: SOURCES OF INSTITUTIONAL SUPPORT AND PROSPECTS FOR SELF-GOVERNANCE

6. The Ontario government need not involve itself in the organization of the sector since the sector has shown a strong capacity to organize itself. To the extent that the Ontario government becomes further involved in governance issues in the sector, it should do so collaboratively with the existing umbrella organizations in the sector.

7. The sector has not been effective in presenting its views to governments in Canada. The reform of the public administration in Ontario responsible for nonprofits should be aware of this historic difficulty. To that end, we propose that an Advisory Council, comprised of representatives selected from the sector, should be appointed to oversee the work of the NOC. See, further, Recommendation 10.

8. Government funds could be usefully spent on subsidising research into the issues facing the sector.

CHAPTER 4: SOURCES OF EMPIRICAL INFORMATION ON THE CHARITY

SECTOR IN CANADA: AN OPPORTUNITY FOR GOVERNMENT

9. Statistics Canada should undertake a review of its statistical operation in the third sector with a view to generating a better framework for the collection and publication of information on the sector.

10. Canadian governments should encourage the development of administrative and regulatory practices which will, to the extent that they generate information on the sector, produce that information in a useful form and accessible way. Currently, the information on the demographics of individual charitable giving, on volunteering, on business involvement in the sector, on the financing and operations of charities, on fundraising campaigns, and on government involvement in the sector is weak or non-existent.

CHAPTER 5: OVERVIEW OF THE CHARITY SECTOR IN ONTARIO

11. Government participation in the sector should not be designed on the premise that government measures can effectively influence the level or direction of altruism in Ontario society.

12. The design of the laws should reflect the fact that religious charities show a distinctive pattern of support and that they have tended historically to be the most

favoured destination of charitable donations. Recognition that most of this support is member-based, and therefore presents fewer accountability issues, should be reflected in the design of the new laws.

13. The design of the new laws should reflect the fact that Ontario has a disproportionate share (measured by assets and grants) of private foundations and that an inappropriate regulatory environment in Ontario might lead to some of these foundations changing jurisdiction to the possible detriment of charitable activity in Ontario.

14. The design of the laws should reflect the fact that governments are major supporters of the sector.

15. The design of the new laws and of the public administration should reflect the fact that the sector is moving towards greater secularization.

16. The design of the new laws should reflect the fact that, overall, charities in Canada do not seem to spend an inappropriate amount of their resources on fundraising.

CHAPTER 6: A WORKING DEFINITION OF CHARITY

17. The reform should proceed on the understanding that the central concept "charity", although covering a diverse range of activities, has a central intelligible meaning which is capable of serving as the basis of the new legal and regulatory regime. In essence, a charitable act is an act whose form, effect and motive are the provision of the means of pursuing a common goodlife, knowledge, play, religion, work, friendship, aesthetic experience, and practical reasonableness to persons who are remote in affection and to whom no moral or legal obligation is owed.

18. Public policy and the legal regulation of nonprofit activity must therefore recognize a categorical distinction between charitable and political activity and between charitable and commercial activity. This categorical distinction, however, does not entail that political or commercial activity of a charitable organization that is integrally related to the organization's purpose, or is purely incidental or ancillary to its charitable activities, jeopardizes the organization's exclusively charitable status.

19. The evaluation of the activities of a charitable organization by courts or administrators is always a context-sensitive judgment. This observation leads to two conclusions:

(1) it would be folly to attempt to define "charity" in any legislative scheme in anything but the most general of terms; and

(2) contemporary decision makers should not feel unduly bound by particular decisions of past decision makers.

CHAPTER 7: THE LEGAL DEFINITION OF CHARITY: THE CURRENT

APPROACH AND PROPOSALS FOR REFORM

20. The common-law definition of "charity" serves numerous functions in the law. The main function is to identify those entities entitled to the privileged treatment that charities receive under the law of trusts and under the taxation laws. These various uses of "charity" do not warrant various separate definitions. The law should continue to use only one definition of charity.

21. The Legislature should not enact a statutory definition of "charity". The law should continue to use the common-law definition of the term. However, to the extent that the common-law definition of charity is deficient, courts and administrators should seek to reform it incrementally, based on the suggestions set out in this report and in accordance with the historic common-law methodology.

22. The emerging general definition under the fourth limb of the *Pemsel* test that the purpose must be beneficial to the public to be charitable is essentially correct if it is understood as meaning that the purpose must advance a common good, in a practically useful way, for the benefit of strangers.

CHAPTER 8: THE LEGAL DEFINITION OF CHARITY: SPECIFIC PROBLEMS

WITH THE CURRENT DEFINITION AND PROPOSALS FOR REFORM

23. Specific problems in several areas ought to be dealt with by courts and administrators as follows:

(1) "Relief of poverty" ought to be interpreted broadly, as it presently is in some cases, to include projects that aid all categories of disadvantaged people.

(2) The law could be more direct in its evaluation of whether particular entities truly qualify as religious in purpose. To the extent that the evaluation of religious practices is required in any case, this evaluation should typically be conducted from the internal point of view. To the extent that a religious practice is called into question, it should not be evaluated on the basis of whether or not some material benefit is produced - the core religious practices of most religions would not pass that test - but on the basis, simply, of whether the good of religion is advanced.

(3) Education should be construed broadly to include the advancement of the goods of knowledge, play, practical reasonableness, friendship, and aesthetic experience, for the benefit of others.

(4) The law should accord independent recognition to the good of knowledge and recognize as charitable projects those which advance this good for the benefit of others in contexts other than strictly educational contexts.

(5) The law should accord independent recognition to the goods of friendship, aesthetic experience, and practical reasonableness, and not always require that they be advanced in educational contexts.

(6) To the extent that the advancement of knowledge is recognized as an independent good, "knowledge" should be given a meaning wide enough to encompass knowledge of all kinds, including theoretical and practical knowledge, speculative and technical knowledge, and scientific and moral knowledge.

(7) There should be no presumption that a project is charitable just because it pursues public policy.

(8) Discriminatory projects ought to be evaluated principally on the basis of whether they are properly motivated, since it ought to be permissible to construct a project which benefits a group identified on the basis of religion, sex, or cultural, but not if the point of the gift, in part, is to express an irrationally sexist, bigoted, or racist opinion.

(9) The mere fact that a project benefits persons outside the jurisdiction should not affect charitable status.

(10) The law ought to recognize a distinction between political purposes which are not charitable, on the one hand, and projects to advance international friendship or fellowship, on the other.

(11) The law should recognize sports or play as independent charitable purposes.

CHAPTER 9: POLICY PERSPECTIVES ON THE CHARITY SECTOR

24. The law should incorporate the following classifications of nonprofit organizations, and use these classifications, where appropriate, in the articulation of rules: religious, charitable, political, mutual benefit, and other. "Charitable" could be further divided into "social welfare" and "philanthropic".

CHAPTER 10: SUPERVISION OF CHARITIES BY REVENUE CANADA:

A BRIEF HISTORY

25. The recent history of the federal government's involvement in the sector has not been, from the sector's point of view, an entirely positive experience. This suggests that the sector will require some persuading that the government can play a supportive role.

CHAPTERS 11 AND 12: SUPERVISION OF CHARITIES BY REVENUE

CANADA: CURRENT LAW AND PROPOSALS FOR REFORM

26. The Commission makes a number of recommendations for the improvement of the federal supervision of charity:

(1) Although the basic premise of the federal regime is sound, there are many instances of provisions which are seriously lacking.

(2) Any reform at the federal level should take account of and attempt to integrate with the provincial regime of regulation so that the regulatory regime as a whole is as simple and coherent as possible.

(3) The best general premise of federal government regulation of the sector is to ensure that entities which avail themselves of the tax privileges are sufficiently loyal to their purpose and are sufficiently effective in its pursuit to ensure that the tax privileges are merited.

(4) The federal regulation should deploy optional quantitative rules to make compliance on the part of the sector easier, especially in the areas of fundraising expenditures, permissible political activity, and permissible commercial activity.

(5) The provisions of the *Income Tax Act* governing charity should be redrafted so that they express more directly and clearly the rules governing the sector. In the reformulation of the tax provisions, more of an effort to integrate the federal regime with the provincial regimes should be made.

(6) Revenue Canada should publish an annual report summarizing the more important registration decisions for the year as well as other important aspects of its surveillance of the sector.

(7) The *Income Tax Act* should not attempt to define "charity". It should continue to use the basic classifications "public" and "private" "foundations" and "charitable organizations". It should require every charity over a certain size to be organized as a trust or a corporation.

(8) The basic regulatory standard under the *Income Tax Act* should continue to be the "exclusively charitable" standard, but this standard should not be interpreted to exclude activity which is ancillary or incidental to charitable activity.

(9) The decision to register or deregister a charity is of general public importance and therefore should be accompanied at the initial stages by greater publicity. We recommend that the Tax Court be given initial judicial authority over the registration and deregistration decisions and that provincial authorities and third parties be given a right to participate in the decision-making process at the administrative and judicial stages.

(10) Commercial activity should be classified in the law as "related", "subordinate" ("ancillary" and "incidental"), and "unrelated". The first two types should be permitted, and the last prohibited. Where a charity carries on an unrelated business, it should be forced to divest itself of the business, or to incorporate it in a separate taxable entity. This entity should be given the right to deduct from its income, without limit, its donations to its owning charity. To make compliance with the rules governing commercial matters easier, the law should provide a list of the types of businesses which meet the related and the subordinate requirements. Program-related investments should be

expressly provided for to remove any doubt that they are not prohibited by the rules regulating commercial activities.

(11) The federal regime ought to attempt to regulate the investment activities of charities only to prevent investments which are imprudent or wasteful, or what the American law refers to as "jeopardizing" investments. This regulation of investments ought to be supported by a reporting requirement in the case of private foundations only.

(12) The federal regime should regulate the charitable fiduciary's duty of loyalty by clearly and expressly prohibiting all transactions involving fiduciaries or their associates which benefit unfairly, directly or indirectly, the fiduciary or associate to the detriment of the charitable entity. These new rules should be supported by a reporting requirement. They should extend to cover transactions involving fiduciaries or their associates and entities in which the charity has a significant investment stake.

(13) The *Income Tax Act* should be redrafted to clarify the regulation of the political and apparently political activity of charities. Partisan and other unrelated political activity should be prohibited; subordinate and apparently political activity should be permitted. The Act should also implement an optional quantitative rule to make compliance easier for most charities. Stricter regulation of political activity in the case of private foundations and laxer regulation of the political activities in the case of social welfare charities might also be implemented.

(14) The Act should not attempt to regulate the borrowing activities of charities, except where the borrowing is so imprudent that it jeopardizes the existence of the charity.

(15) The rules in the Act governing the permissible granting activity of charities are unnecessarily complex. These should be simplified. There should also be an obligation on granting charities to require their recipients to account for the expenditure of grants received.

(16) The rules governing the international activities of charities could be improved by allowing foreign entities or foreign projects of domestic charities to register for the special tax treatment in Canada.

(17) Imprudent fundraising and administrative expenditures should be prohibited. The prohibition should be supported by an annual reporting requirement which would require charities to report amounts expended on several categories of expenditures, such as legal and accounting fees, total staff salaries, and total expenditures, and on donation fundraising. In the case of donation fundraising expenditures, there should be an optional quantitative rule, compliance with which would be deemed to be compliance with the general qualitative rule.

(18) The revenue base for the disbursement quota should be the same for all charities, but the percentage amounts required to be spent should be lower for

charitable organizations than for foundations. The disbursement quota should be simplified and used only to require charities to do charity.

(19) The public administration established at the federal level to administer the *Income Tax Act* requires more financial and administrative support. The regime of available penalties for non-compliance is not adequate because it relies too much on deregistration, which usually is too severe a sanction.

CHAPTER 13: THE CHARITABLE PURPOSE TRUST: CURRENT LAW AND

PROPOSALS FOR REFORM

27. It is not necessary to reform the basic attributes of the charitable purpose trust, but there are features of the law of trusts, as it applies to the charitable purpose trust, which require reformation. These are as follows:

- (1) The *cy-près* doctrine should be reformulated in a statutory provision to permit court reformulation of charitable projects in a wider range of circumstances and in way that does not require as close conformity with the original purposes as is required at present.
- (2) The rule governing mixed purpose trusts should be reformed in a way that permits these trusts to survive.
- (3) Trustees of purpose trusts should be required to register the trust and provide information annually concerning key features of its existence.
- (4) The *Trustee Act* should be reformed in the way suggested in our 1984 *Report on the Law of Trusts*. The reform should apply to purpose trusts, with the following additional special provisions:
 - (a) The NOC should be given the same rights that beneficiaries of a private trust have. The NOC should have the power to pre-authorize or excuse breaches of the duty of loyalty.
 - (b) Specific regulation of transactions between fiduciaries of the trust and their associates and an entity controlled by the trust is required.
 - (c) A summary report of payments made by the trust to its fiduciaries and their associates should be required on an annual basis, and no remuneration to a fiduciary should be permitted without the prior authorization of the NOC
 - (d) Unanimity should not be required for decisions of trustees of a charitable trust. There should be suppletive rules in the statute dealing with trustee meetings.

(e) There should be no special regulation of the investment powers of trustees of charitable trusts except that which applies to trustees generally.

(f) Passing accounts should be abolished. Trustees should be obliged to maintain proper books of account.

(g) Rules governing the disposition of the capital of an endowment should be enacted.

CHAPTER 14: THE PURPOSE TRUST: SHOULD IT BE EXTENDED TO NON-CHARITABLE PURPOSES?

28. There is no need to extend the availability of the purpose trust to non-charitable purposes.

29. Section 16 of the *Perpetuities Act* should be redrafted to permit more readily the pursuit of non-charitable purposes, but in a way that does not necessarily entail state involvement in enforcement or continued viability.

30. The NOC should be empowered to adopt regulations establishing the viability of non-charitable purpose trusts that are, in its view, of sufficient public interest to warrant state participation in their enforcement and viability.

CHAPTER 15: THE NONPROFIT CORPORATION: CURRENT LAW AND PROPOSALS FOR REFORM

31. The general law governing nonprofit corporations requires fundamental reform. A new law should be enacted, and it should incorporate the following elements:

(1) The new law should be contained in a separate corporation statute dealing with nonprofit corporations only.

(2) The new statute should be a modernization of the basic corporate law along the lines of what occurred in the reform of business corporations law in the 1970s.

(3) The best basic model for the new law is the American Bar Association's and the American Law Institutes' *Revised Model Nonprofit Corporation Act*.

(4) None of the conceptual framework of the law of trusts should be explicitly incorporated in the formulation of the rules in the new statute, and in particular, the fiduciaries of the corporation should be conceived of as and referred to as "directors", not "trustees".

(5) Nonprofit corporations should be classified as "charitable", "religious", "mutual benefit", "political", and "others". They should be subject to clearly defined non-distribution constraint rules.

- (6) The *ultra vires* doctrine should be abolished. The constructive notice doctrine should be abolished.
- (7) The incorporation of a nonprofit corporation should be by registration of articles of incorporation, and it should be available as a matter of right.
- (8) The corporate name of a nonprofit corporation should contain an element which indicates its nonprofit status.
- (9) The rules governing pre-incorporation contracts require reform.
- (10) Nonprofit corporations should be required to file annually an updated registration statement containing basic information pertaining to its principals, assets, and activities.
- (11) The statute should contain a complete code, some of the provisions of which would be mandatory and some of which would suppletive, dealing with governance issues, including
- (a) the rights and duties and remedies of members;
 - (b) the rights and duties of the board of directors and of officers;
 - (c) the rights of creditors;
 - (d) the rights of auditors; and
 - (e) the record-keeping obligations of nonprofit corporations.
- (12) In the case of charitable corporations, the NOC should have most of the same rights as members so that it is in a position to enforce the fiduciary duties of directors.
- (13) Specific rules governing reorganizations and fundamental changes should be enacted.

CHAPTER 16: THE UNINCORPORATED ASSOCIATION

32. The basic law of the unincorporated association should be reformed and codified in a statute, similar in basic concept and form to the *Partnerships Act*.
33. The model for this reform should be section 4 of chapter 10 of the *Civil Code of Quebec*.
34. In the case of charitable associations, the NOC should have the same powers as the members of the association.

CHAPTER 17: THE SUPERVISION OF CHARITIES

35. An agency of the government of Ontario, called the Nonprofit Organizations Commission (NOC), should be established. It should have comprehensive jurisdiction to administer all laws governing nonprofit organizations in Ontario.

36. The *Charities Accounting Act* and the *Charitable Gifts Act* should be repealed.

37. The NOC should not have judicial or quasi-judicial authority. The power to make regulations affecting the nonprofit sector should be vested in the Attorney General, on the advice of the NOC.

38. The NOC should have four main areas of responsibility: registrations; fundraising; audits and investigations; and education.

39. It should have the following powers:

- (1) All the powers assigned to the NOC under the organizational laws;
- (2) The power to intervene in any proceeding involving charity under the same conditions as are currently imposed by section 5(4) of the *Charities Accounting Act*;
- (3) The power to apply to the court for
 - (a) an order on an interim or permanent basis to remove and replace a charitable fiduciary,
 - (b) an order to compel a charity, its fiduciaries, or any other person to comply with the law,
 - (c) an order dissolving a charity or placing a charity under the "stewardship" of the NOC, temporarily or indefinitely,
 - (d) an order that a meeting of the directors or members be called,
 - (e) an order requiring charitable fiduciaries or any other person to account,
 - (f) an order, on an interim or permanent basis, to preserve the property of a charity, and
 - (g) an order permitting an audit of a religious charity or an investigation.

40. There should be a Nonprofits Advisory Council to oversee the work of the NOC.

CHAPTER 18: SPECIFIC AREAS OF REGULATORY CONCERN:

FUNDRAISING, INVESTMENTS, POLITICAL ACTIVITY, AND PRIVILEGES

41. A new law regulating nonprofit fundraising should be enacted. The sole objective of the law should be to police nonprofit fundraising to prevent fraudulent schemes. The new law should require that all fundraising campaigns, subject to substantial exceptions, be registered, that all third-party fundraisers be registered, and that all third-party fundraising contracts be registered with the NOC. It would also require minimal point of solicitation disclosure.

42. Charitable gambling, as it is presently regulated, should be under the jurisdiction of the NOC.

43. Charitable gift annuities should be regulated.

44. Special restrictions on permissible investments by charity fiduciaries should be abolished. Charity fiduciaries should be subject to the same investment restrictions as trustees.

45. Investments in active businesses which are unrelated or which are not ancillary or incidental to a nonprofit purpose should be prohibited. These should be carried on by a separate, taxable, corporate entity.

46. Political activities which are unrelated to or which are not ancillary or incidental to a charity's purpose should be prohibited under the organizational laws.

CHAPTER 19: CURRENT GOVERNMENT GRANTING PRACTICES AND SYSTEMS OF ACCOUNTABILITY

47. The public accounts of the province of Ontario should be presented in a way which will render more accessible the financial information concerning the government's involvement in and support of the third sector.

48. The NOC should have the power to audit nonprofit entities in receipt of government funds. The NOC should be given the power to establish guidelines applicable to all government agencies making grants to the nonprofit sector.

49. The statutory framework governing transfer payment accountability in Ontario should be reformed.

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