



CRA releases new 2012 guidance on CED in relation to charitable status

On July 26th, the Canada Revenue Agency released new guidance called *Community Economic Development Activities and Charitable Registration* (CG-014). It replaces the 1999 guidance entitled *Registered Charities: Community Economic Development Programs* (RC4143).

The new guidance seems to be more logically constructed than the older version, and clearer in its meaning. It also seems to establish more enabling parameters, specifically with respect to two common forms of social enterprise, in addition to program related investing.

The guidance states that Community Economic Development (CED) activities tend to fall into these five areas:

- ✓ Activities that relieve employment;
- ✓ Grants and loans;
- ✓ Program-related investments (PRI's);
- ✓ Social businesses for individuals with disabilities; and
- ✓ Community land trusts.

It's important to note that as before, CED activities in themselves are not charitable. The onus is on the nature of the beneficiaries of the CED activities, for example those who are unemployed, living in poverty or with a disability, or residing in a depressed neighbourhood. In these cases, CED activities can further charitable purposes, and would therefore be considered as charitable.

Where PRI's and community land trusts seemed somewhat of a postscript in the earlier guidance, we now see expanded information in these two areas, particularly PRI's, which now absorb roughly one-quarter of the entire new document. With respect to individual development accounts, specific examples and recommended support criteria are now given. Economically Challenged Communities (ECC's) have been renamed as 'deprived areas', with some relaxation given to its definition.

This is also the first piece of CRA guidance that explicitly uses the terms 'social enterprise' and 'social finance'.

Social enterprise

Social businesses and training businesses continue to appear in this guidance, though a more appropriate place might be within the guidance on social enterprise, entitled *What is a Related Business?* Revisions are expected to be made to this 1993 document soon, and we hope to see social and training businesses reflected in that document as well.

'Social businesses' are somewhat misnamed, because rather than considering these as a 'business', CRA views them as a charitable activity. Social businesses can either employ people with disabilities indefinitely, or can support self-employed folks with disabilities.

In order to be considered charitable (i.e. able to be operated as projects of a charity and therefore tax-free), the social business MUST have a workforce 'composed entirely of individuals with disabilities, with the exception of employees who provide necessary training and supervision' with work that is 'specifically chosen and structured to take into account the special needs of individuals with disabilities and to relieve conditions associated with those disabilities.'

'Not required but generally expected' are related training programming, and worker involvement in management and decision-making. The latter point represents a relaxation of the earlier guidance, which stated that workers were expected to serve on the Board. In the field, Board membership was proving an insurmountable goal in many cases.

Absent in the updated version is any mention of 'sheltered workshops'.

Fortunately, the language with respect to profit generation has been relaxed. The old guidance specified that social businesses were expected to be perpetually subsidized (i.e. either by the parent charity itself or additional grants), which placed a chill on social enterprises that could have broken even or generated a small profit. The new guidance instead states that 'a social business must focus on helping eligible beneficiaries and not on making a profit': the phrasing in no way explicitly prohibits profits as the earlier guidance seemed to, but does leave the onus on the charity to demonstrate that although it may be generating profits, the main focus is on benefitting the disabled worker.

As another form of social enterprise, what was previously termed a 'training business' is now called 'on-the-job training', perhaps a more appropriate term because rather than a business, CRA considers this to be a charitable activity.

The stated characteristics of this activity are much the same as before (i.e. instruction is provided, employment is temporary, job placement services are offered, the proportion of target workers is no less than 70% of the total employees), with the exception of a loosening of language around profit generation (as in the social business scenario described earlier).

Where these types of businesses were previously only permitted to consistently break even at best, the new guidance asserts that 'the focus of the activity must be to further a charitable purpose, not to generate revenue'. Groups that we have worked with have for some time needlessly racked up expenses in order to meet the breakeven requirement, or have hived the enterprise off into a taxable corporation. The new guidance should see more charities feeling safer about building enterprise success within their charitable structure.

The new guidance no longer contains sections on unrelated business and what a corporate structure would look like in order to house unrelated businesses, but we expect to see this information in the upcoming revision of the *What is a Related Business?* guidance.

Social finance

In Canada, one burgeoning area of social finance is program-related investing (PRI). A success story south of the border, PRI's are repayable investments made by charitable foundations out of their grant funds (as opposed to their traditional investment portfolio). PRI's 'count' towards the disbursement quota, unlike investments from the main endowment.

The new guidance will likely please foundations, due to the enabling language, level of detail, and clarity provided on the topic. We should no longer be hearing foundations saying 'CRA does not allow PRI's'. Although permission was given in the 1999 guidance, it appeared at the back of the book, in no more than a half page. Now, we find over four pages, providing definitions; examples; requirements; details on PRI's as loans, loan guarantees, and share purchases; specialized PRI intermediaries; and accounting for loans and PRI's. Interestingly, leases of land or buildings are also mentioned as a form of PRI.

The new guidance states clearly that PRI's can be directed to non-qualified donees in addition to qualified donees. Direction and control must be maintained by the charity flowing PRI's to non-qualified donees (such as simple non-profits and for-profit businesses), with the guidance giving clear examples on what this oversight would look like in deals related to housing, employment training, and education.

The guidance also allows the foundation to factor in PRI opportunity costs if it is otherwise unable to meet its disbursement quota.

In short, this section is a must-read for foundations currently undertaking, or considering the dive into program-related investing.

Kudos to the Charities Directorate (the division of CRA responsible for charities) for releasing this clearer and more enabling guidance on CED. We hope for the same forward movement from the updated *What is a Related Business* guidance.