

# Risks for Not-For-Profit Organizations Conducting For-Profit Activities

## Overview

During 2010 the Canada Revenue Agency (“CRA”) issued two Technical Interpretations setting out its position on not-for-profit organizations (“NPO’s”) involved in for-profit activities. The CRA is of the position that an NPO involved in for-profit activities does not qualify for tax exempt status under paragraph 149(1)(l) of the Income Tax Act. Paragraph 149(1)(l) defines an NPO as an organization that is not a charity, that is organized and operated exclusively for an eligible purpose other than profit and that has no part of its income is payable to or made available for the benefit of its members unless the primary purpose and function of the organization is the promotion of amateur athletics in Canada. **According to the CRA, an NPO conducting for-profit activities risks losing its tax-exempt status even if such activities are undertaken to finance the organization’s not-for-profit objectives.**

## Examples of the CRA’s Technical Interpretations

Examples of these types of activities are wide ranging, but there are two specific items discussed in the recent Technical Interpretations. The first relates to income generated from rental operations that was not specifically incidental to the NPO’s purpose. The activities were specifically carried out to generate profits that would either reduce future membership fees or provide for future capital projects. The reduction of future membership fees is precluded by 149(1)(l) as there should be no personal benefit available to members. While funding future capital projects is in accordance with the NPO’s purpose, it was the intentional undertaking of a profit-making activity that jeopardized the organization’s tax-exempt status.

The second Technical Interpretation relates to the investment of cash donations and other assets to earn income. This too is precluded by 149(1)(l), as this activity was conducted to earn a profit, albeit to support the activities of the NPO. To meet the conditions of 149(1)(l) the cash and assets would have to be used directly in accordance with the objectives of the NPO within a reasonable time frame. Simply holding onto the assets and using the income generated from them to fund the operations of the NPO does not qualify.

## Implications and Solutions

Past court cases have seen the CRA unsuccessful in litigating tax assessments against NPO's. However, the future is uncertain as to how aggressively the CRA will challenge the current status of NPO's as are the results of potential future court cases. What is certain is that each NPO should revisit its current and long-term strategies for sustainability. This may result in either eliminating such for-profit activities through obtaining other sources of revenue, although this may not be feasible in the current economic market. Another option is to incorporate a taxable subsidiary that would carry on the for-profit activities.

## Contact Us

As described above, the position of the CRA is quite clear in dealing with for-profit activities and may result in considerable change to the NPO climate. If your NPO is involved in such for-profit activities, we encourage you to contact Manning Elliott’s NPO team to help assist you in determining the appropriate course of action, moving forward.