

NO.: **IT-496R**

DATE: August 2, 2001

SUBJECT: INCOME TAX ACT
Non-Profit Organizations

REFERENCE: Paragraph 149(1)(l) (also sections 149.1 and 168; subsections 149(2), (5) and (12), 181.1(3), and 227(14) and the definitions of “registered charity” and “registered Canadian amateur athletic association” in subsection 248(1); and subsection 216(1) of the *Income Tax Regulations*)

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Application

This bulletin cancels and replaces Interpretation Bulletin IT-496 dated February 18, 1983 and its Special Release dated June 16, 1989.

Summary

This bulletin discusses non-profit organizations. It sets out the conditions that a club, society or association must meet to qualify as a tax-exempt non-profit organization (NPO) and comments on some of the factors that are considered when determining whether it is tax-exempt in a particular year. The bulletin explains when an NPO must file an income tax return and when it is required to file an NPO information return. It also briefly describes the circumstances under which an otherwise tax-exempt NPO may be subject to tax on its property income.

In addition, the current versions of the following Canada Customs and Revenue Agency (CCRA) publications also deal with NPOs:

- IT-83, *Non-profit Organizations – Taxation of Income from Property*
- IT-409, *Winding-Up of a Non-Profit Organization*
- *Income Tax Guide to the Non-Profit Organization (NPO) Information Return (T4117)*

Discussion and Interpretation

General

Unless otherwise noted, all statutory references throughout the bulletin are to the *Income Tax Act*. In this bulletin, the phrases “club, society or association” and “proprietor, member or shareholder”, as they appear in paragraph 149(1)(l), are referred to by the words **association** and **member**, respectively. The phrase “club, society or association” is also considered general enough to include a corporation.

- ¶ 1. In general terms, paragraph 149(1)(l) provides that the taxable income of an association is exempt from tax under Part I of the Act for a period throughout which the association complies with all of the following conditions:
- it is not a charity (see ¶ 4);
 - it is organized exclusively for social welfare, civic improvement, pleasure, recreation or any other purpose except profit (see ¶s 5 to 10);
 - it is in fact operated exclusively for the same purpose for which it was organized or for any of the other purposes mentioned in (b); and
 - it does not distribute or otherwise make available for the personal benefit of a member any of its income unless the member is an association which has as its primary purpose and function the promotion of amateur athletics in Canada (see ¶s 11 and 12).

Whether a particular association meets all of the above conditions and qualifies under paragraph 149(1)(l) as a tax-exempt NPO is a question of fact that can only be determined after we review the purposes and activities of the association. The comments that follow are taken into consideration when making such a determination. Also, even though an association qualifies under paragraph 149(1)(l), it may, as discussed in ¶ 14, be subject to tax on certain income under subsection 149(5).

¶ 2. Where a corporation qualifies as an NPO under paragraph 149(1)(l), subsection 227(14) provides that throughout the period during which the corporation is exempt from Part I tax, it is also exempt from tax under Parts IV, IV.1, VI, and VI.1 of the Act. Furthermore, if such a corporation is exempt from Part I tax throughout the taxation year on all of its taxable income, subsection 181.1(3) provides that no tax is payable for the year under Part I.3.

¶ 3. The fact that one or more of the members of an association is a tax-exempt NPO or a “registered charity”, as defined in subsection 248(1), will not relieve the association of the necessity of complying with the conditions in ¶ 1(a) to (d). In addition, the conditions to be complied with are neither waived nor altered by the fact that most or all of the assets and facilities of the association are leased to one or more tax-exempt organizations or registered charities. Where the association maintains that certain of its activities are carried on in trust, or as agents, for another association, and

the evidence supports this position, these activities may affect the status of that other association as an NPO.

Charities

¶ 4. If, during a period in a particular year, the Minister of National Revenue considers an association to be a “charity” (i.e., a charitable organization or charitable foundation) as defined in subsection 149.1(1), then it cannot qualify in that period as a tax-exempt NPO. For these purposes, an association may be considered to be a charity even if it is not a registered charity or if its designation as a registered charity has been revoked under section 168.

Although an organization that is a charitable organization or charitable foundation will not be exempted from tax by paragraph 149(1)(l), an exemption from tax will be available under paragraph 149(1)(f) if it is a registered charity. For information concerning the registration of a charity, see the CCRA’s guide *Registering a Charity for Income Tax Purposes* (T4063).

Organized and Operated Exclusively for Non-Profit Purposes

¶ 5. To qualify under paragraph 149(1)(l), an association must be both organized and operated exclusively for social welfare, civic improvement, pleasure or recreation or for any other purpose except profit. An association may also be organized and operated exclusively for any combination of these purposes. When determining the purpose for which an association was organized, the instruments creating the association will normally be reviewed. These instruments may include letters patent, articles of incorporation, memoranda of agreement, by-laws, and so on. The terms “social welfare”, “civic improvement”, and “pleasure or recreation” are not defined in the Act. In general terms, **social welfare** means that which provides assistance for disadvantaged groups or for the common good and general welfare of the people of the community. **Civic improvement** includes the enhancement in value or quality of community or civic life. An example would be an association that works for the advancement of a community by encouraging the establishment of new industries, parks, museums, etc. Under the categories of social welfare and civic improvement, care must be taken to ensure that the purposes of the association are not those of a charity. **Pleasure or recreation** means that which provides a state of gratification or a means of refreshment or diversion. Examples include social clubs, golf clubs, curling clubs, badminton clubs and so on that are organized and operated to provide recreational facilities for the enjoyment of members and their families. The phrase **any other purpose except profit** is interpreted as a catch-all for other associations that are organized and operated for other than commercial or financial reasons.

¶ 6. An association may be considered to be organized and operated for any other purpose except profit if its aims and activities are directed toward the general improvement of conditions within one or more areas of business. An example

of this would be where an association was organized to advance the educational standards within a particular industry or profession, to publicize, improve and promote the association's objectives in a general way and to encourage the exchange of relevant technical information. If the activities of such an organization were consistent with these aims, then it would qualify for exemption provided all other conditions of paragraph 149(1)(I) were complied with in the year. However, the association will probably not qualify as a tax-exempt NPO if it is primarily involved, for example, in an activity that is directly connected with the sales of members' goods or services and for such services receives a fee or commission computed in relation to sales promoted. Such an association is normally considered to be an extension of the members' sales organizations and will be considered to be carrying on a normal commercial operation. If the fees and commissions charged are well beyond the needs of the association and these earnings are accumulated and invested as described in ¶ 8 by the association, this would be another reason why the association would not qualify as a tax-exempt NPO.

A **residential condominium corporation** is another example of an association that may be organized and operated for any other purpose except profit. Since a residential condominium corporation is organized as a requirement of the applicable provincial legislation and is normally not operated as a business, it will usually be considered to be organized and operated for other than commercial or financial reasons. Therefore, if the other conditions of paragraph 149(1)(I) are complied with in the year, a residential condominium corporation will generally qualify as a tax-exempt NPO. For more information concerning condominiums, see the current version of IT-304, *Condominiums*.

¶ 7. It will be a question of fact to be determined with regard to the particular circumstances as to whether an association is carrying on a trade or business and if so, whether it will result in a finding that an association is not operated exclusively for non-profit purposes. Some characteristics that might indicate that an activity is a trade or business are as follows:

- (a) it is a trade or business in the ordinary meaning, that is, it is operated in a normal commercial manner;
- (b) its goods or services are not restricted to members and their guests;
- (c) it is operated on a profit basis rather than a cost recovery basis; or
- (d) it is operated in competition with taxable entities carrying on the same trade or business.

Generally, the carrying on of a trade or business directly attributable to, or connected with, pursuing the non-profit goals and activities of an association will not cause it to be considered to be operated for profit purposes.

¶ 8. An association may earn income in excess of its expenditures provided the requirements of the Act are met. The excess may result from the activity for which it was organized or from some other activity. However, if a material part of the excess is accumulated each year and the balance of accumulated excess at any time is greater than the association's reasonable needs to carry on its non-profit activities (see ¶ 9), profit will be considered to be one of the purposes for which the association was operated. This will be particularly so where assets representing the accumulated excess are used for purposes unrelated to its objects such as the following:

- (a) long-term investments to produce property income;
- (b) enlarging or expanding facilities used for normal commercial operations; or
- (c) loans to members, shareholders or non-exempt persons.

This may also be the case where the accumulated excess is invested in a term deposit or guaranteed investment certificate that is regularly renewed within a year and from year to year, whether or not the principal is adjusted from time to time.

¶ 9. The amount of accumulated excess income considered reasonable in relation to the needs of an association to carry on its non-profit activities and goals is a question of fact to be determined with regard to the association's particular circumstances, including such things as future anticipated expenditures and the amount and pattern of receipts from various sources (e.g., fund raising, membership fees, training course fees). For example, it is conceivable that there would be situations where an accumulation equal to one year's reasonably anticipated expenditures on its non-profit activities may not be considered excessive, while in another situation, an accumulation equal to the reasonably anticipated expenditures for a much shorter period would be considered more than adequate. Where the present balance of accumulated excess is considered excessive or an annual excess is regularly accumulated that is greater than an association's needs to carry on its non-profit activities (see ¶ 8), it may indicate that the association's aims are two-fold: to earn profits and to carry out its non-profit purposes. In such a case, the **operated exclusively** requirement in paragraph 149(1)(I) would not be met.

As discussed above, accumulating surplus funds in excess of its current needs may affect the association's status as a tax-exempt NPO. However, in certain cases, when an association requires a time period in excess of the current and prior year to accumulate the funds needed to acquire a capital property that will be used to achieve its declared exempt activities, the association's tax-exempt status may not be affected. For example, this could be the case if an association annually sets aside funds to provide for a special project such as the construction of a new building to replace an existing building when it deteriorates or no longer meets the association's needs. In such cases, any funds accumulated for this purpose should be clearly identified and all transactions

concerning a special project should be clearly set out in the association's accounting records. Provided the funds accumulated for a special project are used for that project, an association's tax-exempt status should not be affected.

¶ 10. To qualify for exemption, an association must not only be organized exclusively for non-profit purposes but it must in fact be operated in accordance with these purposes in each year for which it seeks exemption under paragraph 149(1)(l). A determination of whether an association was operated exclusively for and in accordance with its non-profit purposes in a particular taxation year must be based on the facts of each case, which can be obtained only by reviewing all of its activities for that year. Such a determination cannot be made in advance of or during a particular year but only after the end of the year. An association that qualifies for exemption in a particular year may cease to qualify in a subsequent year by failing to operate in accordance with one of the purposes for which it was organized or by revising its objectives so that it is no longer organized in accordance with a purpose specified in paragraph 149(1)(l).

Personal Benefit to Members

¶ 11. To qualify for exemption under paragraph 149(1)(l), no part of the income of an association, whether current or accumulated, can be payable to, or otherwise made available for the personal benefit of, any member of the association that is not a member described in ¶ 13. An association may fail to comply with this requirement in a variety of ways. For example, subject to the comments in ¶ 12, an association would not qualify as tax-exempt if

- (a) it distributed income during the year, either directly or indirectly, to, or for the personal benefit of, any member; or
- (b) it has the power at any time to declare and pay dividends out of income.

An association that has been tax-exempt may fail to comply with this requirement on a winding-up, dissolution, or amalgamation. For example, on winding-up, such an association will lose its tax-exempt status at the time when a determination is made that an amount of income will become payable to, or otherwise available for the benefit of, a member other than a member described in ¶ 13. Possible difficulties in this regard may be avoided if the association's enabling documents provide that upon a winding-up, amalgamation or dissolution all of its assets and accumulated income are to be transferred to an organization with similar objects that qualifies for exemption under paragraph 149(1)(f) or (l).

Also, for the purposes of paragraph 149(1)(l), in determining any income that was payable to, or otherwise available for the personal benefit of, a member, subsection 149(2) provides that such income is deemed to be the amount of income determined on the assumption that the amount of any taxable capital gain or allowable capital loss is nil. This subsection operates, for example, to allow an association that is a tax-exempt NPO to distribute its net taxable capital gains

(taxable capital gains less allowable capital losses) to a member without prejudicing its tax-exempt status.

¶ 12. Certain types of payments made directly to members, or indirectly for their benefit, will not, in and by themselves, disqualify an association from being tax-exempt under paragraph 149(1)(l). Such payments include **salaries, wages, fees or honorariums** for services rendered to the association, provided the amounts paid are reasonable and no more than those paid in arm's length situations for similar services. Also included are payments made to employees or members of the association to assist them in covering their expenses to attend various conventions and meetings as delegates on behalf of the association, provided attendance at such conventions and meetings is to further the aims and objectives of the association. In addition, campaign expenditures of a political party (other than payments to a candidate that are not reimbursements of reasonable expenses), which often result in an indirect benefit for a candidate, are not the type of personal benefit contemplated by paragraph 149(1)(l) that would cause the party to be denied exemption under that paragraph.

¶ 13. An association that is a tax-exempt NPO described in paragraph 149(1)(l), whose main purpose and function is the promotion of amateur athletics in Canada on a nationwide basis, can qualify as a "registered Canadian amateur athletic association" as defined in subsection 248(1) if it is resident and created under a law in Canada. To apply for registration, such an association must complete and file Form T1189, *Application to Register a Canadian Amateur Athletic Association Under the Income Tax Act*.

Registered Canadian amateur athletic associations may receive gifts from

- (a) corporations that are thereby entitled to a deduction in computing taxable income under paragraph 110.1(1)(a); or
- (b) individuals who, as a result, are entitled to a deduction in computing tax payable determined by the formula in subsection 118.1(3).

Without disqualifying itself under paragraph 149(1)(l), such an association may distribute income to, or for the benefit of, any member that is an association the main purpose and function of which is the promotion of amateur athletics in Canada. Consequently, a registered Canadian amateur athletic association is able to distribute the proceeds of the gifts it receives to qualifying members without jeopardizing its status as a tax-exempt NPO or as a registered Canadian amateur athletic association.

Subsection 149(5)

¶ 14. Although a particular association may otherwise qualify to be exempt from Part I tax under paragraph 149(1)(l), it could be subject to tax on its property income if subsection 149(5) applies. That is, when the main purpose of an association is to provide dining, recreational or sporting facilities for its members, the special rules in

subsection 149(5) will apply and override the exemption in paragraph 149(1)(l). These rules deem an *inter vivos* trust to be created and provide that the association's income from property, as well as certain taxable capital gains, is income of the deemed trust. For more detailed information on the application of subsection 149(5), see the current version of IT-83, *Non-profit Organizations – Taxation of Income from Property*.

Filing Requirements

¶ 15. An association that qualifies under paragraph 149(1)(l) is required to file an income tax return if

- (a) it is a corporation;
- (b) it is deemed *inter vivos* trust under subsection 149(5) (see ¶ 14) which has
 - (i) tax payable, or
 - (ii) disposed, or realized a taxable capital gain on the disposition, of any capital property that is **not** used directly in the course of providing dining, recreational or sporting facilities to its members; or
- (c) the Minister has demanded that it file a return.

A *T2 Corporation Income Tax Return* or a *T2 Short* return must be filed within 6 months from the end of the corporation's taxation year. A *T3 Trust Income Tax and Information Return* must be filed within 90 days from the end of the trust's taxation year.

¶ 16. In addition, for fiscal periods ending after 1992, subsection 149(12) requires a tax-exempt association to file Form T1044, *Non-Profit Organization (NPO) Information Return*, if

- (a) the total of all amounts received or receivable by the association in the fiscal period for taxable dividends, interest, rentals, or royalties is more than \$10,000;

- (b) the total assets of the association (determined in accordance with generally accepted accounting principles) at the end of its immediately preceding fiscal period exceeded \$200,000; or
- (c) the association had to file an NPO information return for a preceding fiscal period.

An NPO information return must be filed within 6 months after the end of the association's fiscal period. For more information, see the *Income Tax Guide to the Non-Profit Organization (NPO) Information Return* (T4117).

However, an association which is tax-exempt under paragraph 149(1)(l) and is also a registered Canadian amateur athletic association does not have to file an NPO information return. Subsection 216(1) of the *Income Tax Regulations* requires such an association to file Form T2052, *Registered Canadian Amateur Athletic Association Return of Information*. Form T2052 must be filed within 6 months of the end of the association's fiscal period.

¶ 17. Whether or not an association that qualifies under paragraph 149(1)(l) files an annual income tax return or the appropriate information return, it must still comply with the other requirements of the Act. For example, where amounts such as salaries and wages are paid, the association must comply with the withholding and remittance requirements as well as the requirements concerning the preparation of T4 and other forms.

Explanation of Changes

Introduction

The purpose of the *Explanation of Changes* is to give the reasons for the revisions to an interpretation bulletin. It outlines revisions that we have made as a result of changes to the law, as well as changes reflecting new or revised interpretations.

Reasons for Revision

Interpretation Bulletin IT-496R deals with non-profit organizations described in paragraph 149(1)(l). The bulletin sets out the conditions that a club, society or association must meet to qualify as a tax-exempt NPO. It also discusses some of the factors that are considered when determining whether such an organization is tax-exempt in a particular year. We have revised this bulletin to reflect the provisions of new subsection 149(12) which requires certain NPOs to file an information return. This subsection was added by S.C. 1994, c.7, Schedule VIII (formerly Bill C-92).

Legislative and Other Changes

Under the heading **General**, the use of the words “association” and “member” in the bulletin is explained. Also, comments indicating that a corporation can qualify as a tax-exempt NPO were included in this area.

New ¶ 1 describes, in general terms, the conditions that must be met for a club, society or association to qualify as a tax-exempt NPO. It brings forward information previously contained in former ¶s 1 and 2.

New ¶ 2 was added to indicate that, throughout the period during which a corporation qualifies as a tax-exempt NPO, it may also be exempt from tax under Parts I.3, IV, IV.1, VI, and VI.1.

¶ 4 was revised to eliminate the reference to a provision of the Act which is no longer relevant and to refer to a more appropriate publication concerning the registration of a charity for income tax purposes.

¶ 6 was expanded to indicate that most residential condominium corporations will generally qualify as NPOs because they are normally organized and operated for any other purpose except profit. This position was previously announced in issue No. 4 of the *Income Tax Technical News*, dated February 20, 1995.

¶ 7 was revised to state that it is a question of fact whether the carrying on of a trade or business by an association will result in it not being operated exclusively for non-profit purposes.

¶ 9 was modified to indicate that the amount of accumulated excess income considered reasonable is a question of fact. It was also expanded to discuss accumulating funds required for the purchase or construction of a capital property.

¶ 11 was revised to comment on when an NPO would lose its tax-exempt status on winding-up. These comments are consistent with our position as set out in the current version of IT-409 and with the findings in *L.I.U.N.A. Local 527 Members' Training Fund v. The Queen* reported at [1992] 2 CTC 2410; 92 DTC 2365.

¶ 13 was revised to eliminate references to taxation years and provisions which are no longer relevant. Also, a reference to Form T1189 was added.

New ¶ 14 was added to expand on the information in former ¶ 1 concerning subsection 149(5).

¶ 15 (former ¶ 14) was expanded to include information on the type of income tax return an NPO may have to file.

New ¶ 16 was added to describe the provisions of subsection 149(12) which require certain tax-exempt NPOs to file an NPO information return (Form T1044) for each fiscal period ending after 1992. It also explains that a registered Canadian amateur athletic association does not have to file an NPO information return but must file Form T2052, *Registered Canadian Amateur Athletic Association Return of Information*.

New ¶ 17 brings forward the remainder of the information previously contained in former ¶ 14.

Throughout the bulletin, we have made minor changes for clarification or readability purposes and deleted comments which are no longer timely.

We consulted with the Canadian Society of Association Executives in the course of revising this bulletin.

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