

Non-profit Organizations and Tax Exemptions

A New and Clearer but More Restrictive System

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In fact, the Commission municipale du Qu ebec and the higher courts have often pointed out the difficulty of coherently interpreting legislative texts that lack clarity and open the door to contradictions.

The *Act to again amend various legislation provisions concerning municipal affairs* (S.Q. 2000, Chapter 54), known until then as Bill 150, inserted a new division in the *Act respecting municipal taxation* consisting of 25 sections and entitled "Exemption arising from recognition granted by the Commission".

About ten sections inserted at the end of the amending legislation also set force important transitional provisions concerning recognition granted before December 19, 2000, (under the "former scheme", as the legislation refers to it).

Thus, the legislator has carried out a major housecleaning, because any recognition obtained under the former scheme will all lapse no later than December 31, 2003 (and well before in some cases). This will compel the recognized organization to present a new application for recognition, in accordance with the "new scheme". Given the substantial changes in the conditions of recognition, it can be anticipated that

several currently recognized organizations will fail in their renewal application (golf clubs and marinas for example). However, it is foreseen that some organizations will become eligible for exemptions although they were not under the former scheme (we are thinking here of all the organizations involved in the prevention of suicide and family violence).

This bulletin intends to describe the key elements of the new recognition system, without claiming to identify and resolve in advance all the problems of application (if not of interpretation) that will inevitably arise.

To facilitate reading, we refer to the *Act respecting municipal taxation* as the "A.M.T".

Introduction

The end of 2000 was particularly fertile in terms of legislation concerning municipal affairs. This undoubtedly explains the lack of attention attracted by major amendments to the *Act respecting municipal taxation* (R.S.Q., Chapter F-2.1), which recodified and reorganized the mechanisms by which certain non-profit organizations can benefit from municipal or school tax exemptions.

In the past few years, several municipal stakeholders (including the Union des municipalit es du Qu ebec and F ed eration qu eb ecoise des municipalit es) intensified their criticism of the exemption system, because of its lack of precision and the resulting largesse for organizations that objectively did not deserve an exemption.



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Who Awards Recognition?

As was the case under the “former scheme”, the Commission municipale du Québec awards recognition after a quasijudicial process. It must consult the local municipality (subsection 243.23 A.M.T.) which must analyze the constituted file (subsection 243.25 A.M.T.). It may hold a hearing if it considers it necessary (subsection 243.21 A.M.T.), meaning that it is not obliged to do so.

What are the Effects of Recognition?

In principle, immovables belonging to a recognized organization are exempt from any municipal and school property tax (section 204 A.M.T.). Moreover, the eligible activities carried on by a recognized organization on any premises are exempt from the business tax (section 236 A.M.T.). However, local municipalities, on certain conditions, make collect compensation for municipal services (see page 6 of this bulletin, section “What is Compensation for Municipal Services?”).

Various mitigating measures are applied to these principles because the legislator considered it necessary to put a stop to certain abuses or exaggerations.

Who can be Recognized?

It is not specified that recognition cannot be granted to a natural person, but only to a “non-profit legal person” (section 243.6 A.M.T.). Legal person means a company, a partnership or a cooperative.

The non-profit character must be proved to the Commission municipale, notably by filing the organization’s financial statements (section 243.25 A.M.T.).

This non-profit character is inconclusive in itself because it is also necessary that the immovable and the premises be used for “eligible activities” (see page 3, section “What are the Eligible Activities?”).

A non-profit legal person may obtain recognition for the purposes of exemption from property taxes if it is the owner of the immovable where the eligible activities are carried on. It may also obtain such recognition if it is a lessee or occupant of an immovable belonging to an owner which itself is exempt from property taxes, such as the Government or a public body (section 243.3 A.M.T.).

Concerning the business tax exemption, the non-profit legal person who carries on an “eligible activity” in the immovable or on the premises may benefit from the recognition (section 243.4 A.M.T.).

To simplify the process, the owner who obtains recognition for property tax purposes shall be automatically deemed recognized for business tax purposes concerning the same “eligible activities” (section 243.4 A.M.T.).

When can Recognition be Determined?

The eligible activity must be carried on at the time when recognition is requested (sections 243.7 and 243.8 A.M.T.). Therefore, it is impossible to obtain advance recognition, for example, upon signing a mere offer to purchase accepted on condition of obtaining recognition. It is therefore necessary, at the time of the application, to already be an owner, lessee or occupant (as the case may be) and actually and concretely engage in the eligible activities.

Once recognition is obtained, it may be retroactive to January 1st of the year in which the application for recognition was received by the Commission municipale, to the extent that all the conditions were observed on the effective date (subsection 243.12 A.M.T.).

What are the Eligible Activities?

Section 243.8 A.M.T. states the three main eligible activities:

- activities in a “field of artistic endeavour”;
- activities of an informational or educational nature;
- activities in the philanthropic field.

Field of artistic endeavour:

Subsection 243.10 A.M.T. enumerates (apparently exhaustively) what the field of artistic endeavour encompasses:

- the stage;
- film and video;
- discs and other modes of sound recording;
- visual arts;
- decorative arts;
- literature.

Any activity which consists of creation, exhibition or presentation of a work in a field of artistic endeavour is eligible.

Informational and educational field:

Activities in this category must be recreational activities, and thus exclude formal education and vocational training (section 243.8, paragraph 2 A.M.T.).

The activities must be intended to improve knowledge or skills in any of the fields enumerated. They must also be educational and not purely recreational.

The fields in question are art, history, science, sport and “any other recreational field” (such as card games and philately). It is important to note that the recognition does not benefit the *practice* of the recreational activity in question (such as playing chess), but the *education* and *information* relating to the activity (learning to play chess). The distinction undoubtedly will be difficult to establish in several concrete situations.

Activities in this category must be offered to the public without preferential terms (such as a reduced admission price for the members of the organization).

Philanthropic field:

The first organizations covered are those that seek to promote or defend the rights or interests of persons on the basis of their age, language, or ethnic or national origin, or because they have a disease or a handicap (section 243.8, paragraph 2, subparagraph a, A.T.M.).

Secondly, this category covers organizations that fight any form of illegal discrimination (subparagraph b).

Thirdly, it covers organizations that assist oppressed persons or persons who are socially or economically disadvantaged or otherwise in difficulty or prevent such persons from finding themselves in difficulty (subparagraphs c and d).



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The user of the immovable must engage in an activity the main and immediate cause of which is enumerated above. However, the activity may be carried on by intermediaries acting for a non-profit purpose to establish the link between the organization and its beneficiaries (for example, relatives and friends of sick children). In other words, it is not necessary for the beneficiaries themselves to engage in the eligible activities (section 243.9 A.M.T.).

Unrecognized fields:

Contrary to the previous situation, the Act no longer permits recognition of an organization solely because it is registered as a charitable organization under the *Taxation Act*. Transitional provisions are provided in this regard (see page 6, section “What Happens to Charitable Organizations?”).

Also, section 243.7 A.M.T. excludes store services and “lodging other than temporary lodging”. In the later case, the exemption remains possible when the activity consists of providing short-term refuge to persons in difficulty.

What Happens When Several Activities are Carried on Simultaneously?

The entire logic of the recognition mechanisms depends on what constitutes the “principal activity” held in a given immovable or premises.

Under section 2 and section 243.2 A.M.T., the recognition can cover a specific part of the unit of assessment, the immovable or the premises. Any portion of section that can reasonably be delimited or distinguished (a floor, certain partitioned premises, etc.) may constitute a part of the immovable covered by the recognition.

With regard to the whole or a specific part, the legal test is to assess what constitutes the principal use. The Act does not indicate the criteria for distinguishing this use but these will generally be distinctions in space (for

example, 60% of the surface) or in time (for example, 30 weeks per year) or a combination of the two notions. It can also be asked whether the activities are distinguished from each other based on the respective proportion of the expenses they are allocated and the income they generate.

The principal activity thus identified must coincide with an “eligible activity” or a combination of several eligible activities.

A rule set forth in section 243.9 A.M.T. considers situations where an immovable is occupied simultaneously by two users. As soon as one of the two uses is for an ineligible activity or is carried on for pecuniary gain, then neither of the uses may be considered for the purposes of determining the principal use of this immovable.

According to the same logic, this rule does not govern the case where the same users engages in several uses of the same portion of the immovable. Section 243.9 A.M.T. specifies that the user may carry on the activity through a mandatary. The rules of section 243.9 A.M.T. does not apply when

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each of the uses is circumscribed in a distinct portion or section of the immovable.

A lessee or any occupant other than a true mandatary will logically be considered as a distinct user.

In our opinion, several special cases will arise where it will be necessary to establish whether there are several users or only one, and whether the uses can be physically separated or not.

Can the Organization Have Income?

Without deviating from the principle whereby the principal use is not for pecuniary gain, the Act specifies that this remains possible even if the eligible activity generates income.

However, the price level charged to a participant in the activity is then the determining factor (section 243.9 A.M.T.). This participant must not be charged a price greater than the cost of the service corresponding to the eligible activity. However, such an approach will considerably complicate the operation of organizations wishing to raise funds through a benefit activity for which they sell tickets at a price clearly above “cost”.

This having been said, it must be pointed out that the restriction posed by section 243.9 A.M.T. does not prevent the organization from receiving income that does not constitute a consideration but rather an act of generosity (think of a donation by a citizen or a government subsidy).

How Long does the Recognition Last?

Previously, the recognition was decreed by the Commission municipale for an indeterminate and unlimited period, in fact until a revocation decision, a mechanism seldom used up to now.

The legislative amendments introduce a range of mechanisms for review, lapsing and revocation of recognition (sections 243.15 to 243.22 A.M.T.).

A recognition obtained under the new legal system must be renewed after nine years (in the case of the property tax exemption) or after five years, in the case of the business tax (section 243.20 A.M.T.).

This means that the municipal assessor has an increased responsibility from now on because he must periodically verify the legal status of any unit of assessment or any premises on which the property assessment roll or the rental value roll, as the case may be, confers an exemption status.

The municipal assessor may cause the lapsing of recognition by force of law (and thus without the Commission municipale’s intervention) by altering the roll so that the connection between the elements of the recognition forming the basis of the recognition ceases to exist, either because the immovable no longer exists or is no longer entered on the roll, or because the beneficiary of the recognition has lost its status as owner, lessee or occupant.

The recognition may be revoked at the request of the local municipality or by the Commission municipale acting on its own account, when it appears that one of the essential conditions is no longer fulfilled (section 243.17 A.M.T.).

What Happens to Recognitions Already Granted?

A recognition obtained from the Commission municipale under the “former scheme” ceases to be unlimited in time.

Such a recognition will end on December 31st, 2001 if the Commission municipale had granted it by a decision rendered before December 19, 1991. It will end on December 31, 2002 if it was obtained between December 20, 1991 and December 19, 1995. It will end on December 31, 2003 if it has been obtained since December 20, 1995 (section 132 of the amending Act).

The Act provides for a notice procedure so that the beneficiary of the recognition is informed in advance by the Commission municipale that this recognition will expire (section 134 of the amending Act).

The organization must then present a new application for recognition and it is in its interest to act immediately, without waiting for the expiry date (section 133 of the amending Act).

In principle, if a new recognition is granted, the Commission municipale will ensure that this occurs to maintain continuity in relation with the recognition obtained under the “former scheme” (and thus, without a hiatus between the two).

What Happens to Charitable Organizations?

Sections 204 and 236 A.M.T. of the new legal system eliminate the exemption from which charitable organizations benefited by the mere fact of their registration under the *Taxation Act*.

However, they will have the opportunity to qualify for recognition if they are capable of fulfilling the new conditions. A transitional period is provided for this purpose.

Concerning the property assessment roll, the recognition obtained under the “former scheme” remains in force until the end of 2001, 2002 or 2003, as explained in paragraph 9 above.

For the business tax, the effect of a recognition under the “former scheme” will cease by operation of law at the end of 2001. The municipality concerned must give the subject organization a notice to the effect that the business tax exemption will expire by operation of law (section 138 of the amending Act).

The last paragraph of section 138 of the amending Act (Chapter 54) provides that the organization will not lose the benefit of the business tax exemption under the former scheme if, on January 1st, 2002, it has already presented an application for recognition under the new scheme and the Commission municipale has not yet ruled on this application. This legislative wording does not specify the term of such a stay, but it can be deduced that this situation can be extended up to the end of 2002.

What is Compensation for Municipal Services?

Sections 205 and 205.1 A.M.T. empower a local municipality to subject the owners of certain enumerated immovables to the payment of compensation for municipal services. The enumeration includes most of the immovables covered by a Commission municipale recognition (subsection 10 of section 204 A.M.T.).

Section 205.1 A.M.T. sets a ceiling according to which compensation for municipal services may not (in the present case) exceed 50% of the general property tax rate.

This means that the compensation is calculated according to the value at which an immovable is entered on the property assessment roll, even though this immovable is declared exempt from property taxes.

Therefore, the substantial amount at which the compensation for municipal services can be established may incite some owners to contest the amount of the municipal assessment, even if the immovable in question is recognized by the Commission municipale.

Conclusion

One can understand the legislator's intention to put an end to debatable situations where tax exemptions persist without justification. It remains that all non-profit organizations must have redone their homework by December 31, 2003 (and some even before the end of 2001 or 2002) so that they do not lose a recognition from which they have benefited for a number of years.

The procedure is so strict that failure to observe certain time limits and formalities can be fatal, especially since an organization whose application has been refused cannot present it again within five years of the refusal (section 243.5 A.M.T.).

The municipalities have every interest in taking inventory of all immovables and premises in their territory which benefit from a recognition granted under the former scheme and, in conjunction with the municipal assessor, in putting forward an efficient and harmonious transition to the new scheme.

Under the circumstances, we note the importance of ensuring adequate dissemination of an application for recognition which considers all the new parameters of the *Act respecting municipal taxation*.

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