

NCNCANADA 

## Shared Spaces Learning Series

### **KNOWLEDGE IN ACTION 1: CORPORATE STRUCTURES AND REGULATORY CONTEXT**

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NCN Canada: A Program of Tides Canada

 **Tides Canada**

# NCN Canada and the Shared Spaces Learning Series

Mission-driven shared spaces have long operated across Canada in service of a variety of social and hybrid missions. More recently, the phenomenon of shared spaces has been experiencing a surge in growth and strategic interest across the public, private and non-profit sectors. In 2015, The Nonprofit Centers Network (NCN) and the Social Purpose Real Estate Collaborative (SPRE) hosted a series of conversations and research project about the unique needs of Canadian organizations involved in non-profit and mission-based shared space projects. In 2016 Tides Canada, with support from NCN, initiated a new program, **NCN Canada**, to begin to address these needs.

This paper is part of NCN Canada's *Shared Spaces Learning Series* initiative, designed to contribute to the emerging national conversation about the roles, capacities and limitations of shared spaces, understood in various contexts as Community Hubs, Social Purpose Real Estate and Non-profit Centres. The *Shared Spaces Learning Series* features "Knowledge in Action" research briefs, which gather and summarize relevant data and information, and "Stories from the Centres" case studies, highlighting emerging practices and perspectives in Canadian shared spaces.

## HOW CAN THIS GUIDE BE USED?

Operators of Canadian non-profit centres should find this information relevant to informing strategic decision-making about structural options available to their organizations, the advantages and limitations of each, and the implications of Canadian Revenue Agency (CRA) policies on permissible activities for registered charities.

Each organization's context is unique and no general guide can replace the utility of specific research, consultation, and legal counsel. The aim of this paper is to organize information in a complex field, to help facilitate useful preliminary and evaluative conversations, and to help operators clarify the questions relevant to their specific context.

The information in this paper should not be construed as legal counsel.

## WHAT IS INSIDE?

This paper, *Knowledge in Action 1: Corporate Structures and Regulatory Context*, is organized in three sections: *Preliminary Considerations*, *Corporate Structure Options*, and *Considerations for Registered Charities*. Sources and additional resources can be found in the final section.

The information in the forthcoming *Knowledge in Action 2: Business Models and Revenue Streams* is complementary to the information here.

## Introduction

Non-profit shared space centres operate in a context of complexity in regards to the legal and regulatory frameworks that shape organizations. Shared spaces often behave as social enterprises, blending non-profit missions with private sector style revenue generating activities. Social enterprise activities in Canada are governed by a combination of Federal and Provincial corporate registration legislation, the Commercial Tenancies Act, the Income Tax Act, and Canada Revenue Agency policies and interpretations.<sup>1</sup> As a result, a significant variety of structural options are available to organizations and collaboratives founding a shared space facility.<sup>2</sup> Frequently arising governance questions – *Should we run the centre as a program at one of the founding member organizations or register a new organization? Should it be a corporation, a society or a co-operative? Who will hold title to the property and make decisions about use of assets?* – all need to be examined through the multiple lenses of these varying pieces of legislation and regulation.

Additional complexities often arise in the operating stages, as non-profit centres can take on a variety of roles in relation to their constituent organizations – often acting as some combination of landlords, space managers, community conveners, backbone organizations, service providers, and/or shared platforms. As your centre grows and develops, the assessment of new activities will sometimes also require a renewed assessment of your chosen structure: *Can our non-profit society register as a charity? What are the implications to our charitable status of owning revenue-producing property? Should our charity operate its social enterprise coffee shop as an internal program, an arms-length subsidiary or a fully independent new organization? Can we open a second location without jeopardizing our status? Should our capacity-building program be limited to our members or open to the public?* These questions, too, should be understood through the legal and regulatory context.

The process and considerations outlined here help to evaluate new opportunities at both foundational and operational stages: whether opening a new centre, planning new activities at an existing centre, or planning a change in status or scope of an existing organization. Use the questions in the “Preliminary Considerations” section to make decisions about the scope and purpose of the opportunity. Then, use these decisions to evaluate the options described in “Legal Structure Options.” Finally, use the “Considerations for Registered Charities” section to understand the particular restrictions placed on the activities of registered charitable organizations by the CRA.

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<sup>1</sup> Pauline O'Connor, “The New Regulatory Regime for Social Enterprises in Canada: Potential Impacts on Nonprofit Growth and Sustainability,” Centre for Voluntary Sector Studies: Working Paper Series (Toronto, ON: Ryerson University, 2014).

<sup>2</sup> Susan Manwaring and Andrew Valentine, “Social Enterprise in Canada: Structural Options” (SiG@MaRS, December 2011), <http://diversecityonboard.ca/wp-content/uploads/2015/11/MaRSReport-Social-Enterprise.pdf>.

# Preliminary Considerations

In order to make an informed decision about the right structure, begin by getting to clarity about some foundational questions.

1. What is the **primary purpose** of the activity or enterprise?
2. What roles does the centre [plan to] play in **relation to its members**?
3. What roles does the centre [plan to] play in **relation to the public**?
4. Do we [plan to] **lease or own** property?
5. What types of **financing** will the initiative need to access now and in the future?

## 1. PRIMARY PURPOSE

It is critical to understand and commit to the primary purpose of your initiative, typically understood as one of the following<sup>3</sup>:

- Responding to a market need,
- Contributing to organizational sustainability,
- Advancing a social mission.

Although most centres' missions will be a hybrid of two or all three of the above, it is important to be explicit about your priority, so that you can later know where you can be flexible and where you must be firm. Activities driven by market or organizational needs, rather than the advancement of a social mission, are heavily restricted by the CRA for registered charities.

## 2. RELATIONSHIP TO MEMBERS

Getting clear about the full scope of the activities you are planning will not only help you to understand which legal structure is the best fit, but also help to frame (or reframe) your non-profit's or charity's *objects* in alignment with regulations. Consider the combination of various possible roles and activities taken on (or planned for) your centre<sup>4</sup>:

- Landlord,
- Building Operations,
- Shared Platform / Service Provider,
- Community Development,
- Collaborative/Sector Leadership.

<sup>3</sup>Anna Bubel, "Choosing a Legal Form for Your Social Enterprise," Social Enterprise Guides (Alberta: Western Economic Diversification Canada, 2006), <http://socialenterprisefund.ca/wp-content/uploads/2010/01/legal-structure.pdf>.

<sup>4</sup>Definitions and examples of different approaches are presented in Knowledge in Action 2: Business Models.

### 3. RELATIONSHIP TO THE PUBLIC

In addition to supporting your tenants, members and other specific stakeholders, does [will] the centre have a public facing mission of its own? If yes, what types of activities will you endeavour in support of that? Understanding this will help you to locate your initiative on the public-private interest spectrum, further informing your structural decision. While non-profits can be formed to provide benefits only to their membership, charitable status is only conferred on organizations whose scope is public.

### 4. LEASING VS. OWNING PROPERTY

For new shared space initiatives, deciding whether your organization will need to lease or own its Centre will have profound implications on the types of financing you will require, and therefore the kinds of corporate structures that are available. Overlaps between the Commercial Tenancies Act and the Income Tax Act will need to be explored in order to surface the governance structure that can best support your particular needs. Many centres delegate the functions of ownership and management to separate, related, arms-length organizations. For example, the owner of the property might be a Corporation limited by share or a charitable Foundation created solely for the purpose of owning the property, while ongoing operations are governed by a non-profit society.

### 5. TYPES OF FINANCING

Different organizational structures enable different sources of financing. Consider the different stages and financial requirements of your operation and what *types* of finance you will need to access:

- Private equity (investment),
- Debt,
- Government grants,
- Charitable donations (from private sector and other charities).

Only private companies (corporations limited by share) can access private equity; only charitable organizations can receive charitable donations. Government grants are sometimes restricted. There are no structure-based limits on access to debt financing.

## Corporate Structure – Options

Three key corporate structures are available to Canadian initiatives in the private/civic sector:

- Corporation Limited by Share (for-profit private sector company)
- Corporation Limited by Guarantee or Not-For-Profit Society (non-profit organization)
- Registered Charity (a non-profit with additional special CRA status)

Each of the key structures has sub-variations that provide some additional flexibility. For example, British Columbia’s “C3” or “Community Contribution Company”<sup>5</sup> and Nova Scotia’s “CIC” or “Community Interest Company”<sup>6</sup> are subtypes of private sector companies. As well, any of the three can also be registered as a co-operative if more democratic governance is desired.

Table 1 presents a brief summary of each option vis-à-vis four of the foundational questions.

	For-Profit Organization	Non-Profit Organization	Registered Charity
Available Variations	<ul style="list-style-type: none"> <li>• Private equity corporation</li> <li>• Private equity cooperative</li> <li>• C3 (British Columbia)</li> <li>• CIC (Nova Scotia)</li> <li>• Registered B Corp</li> <li>• Private subsidiary of non-profit or registered charity</li> </ul>	<ul style="list-style-type: none"> <li>• Provincial scope (typically under a <i>Societies Act</i>)</li> <li>• National Scope (under the <i>Canada Not-For-Profit Corporations Act</i>)</li> <li>• Nonprofit Cooperative</li> </ul>	<ul style="list-style-type: none"> <li>• Nonprofit Society, Corporation or Cooperative with special registration status with the Canada Revenue Agency</li> <li>• Private or public foundation with special registration status with the Canada Revenue Agency</li> </ul>
Business Driver	Most appropriate when <i>primary driver</i> is based on <i>market needs</i> or <i>organizational sustainability</i>	Most appropriate when <i>primary driver</i> is based on a <i>social mission</i> .	
Relationship to Tenants	<ul style="list-style-type: none"> <li>• Suitable for transactional activities such as landlord/tenant and service provider/client</li> <li>• Reputational risk for community-based activities, due to perceived or real conflicts with profit motive</li> </ul>	<ul style="list-style-type: none"> <li>• Suitable for all transactional and community-based activities</li> <li>• Multi-role engagement possible, e.g. members as volunteers or governance stakeholders</li> </ul>	<ul style="list-style-type: none"> <li>• Suitable for all community-based activities (Community Development, Collaborative/Sector Leadership)</li> <li>• Legal risk for transactional activities (lease holding, service provision) if determined to be “carrying on an unrelated business”</li> <li>• Broad capacity for shared platform activities if appropriately structured</li> </ul>
Relationship to Public	<ul style="list-style-type: none"> <li>• Transactional: public represented by shareholders</li> <li>• Corporate Social Responsibility / Blended Value Creation</li> </ul>	<ul style="list-style-type: none"> <li>• Public represented by membership</li> <li>• Mission can benefit members exclusively or public at large</li> </ul>	<ul style="list-style-type: none"> <li>• Mission must benefit public to be “charitable in the sense understood by the law”</li> <li>• Public benefit can be indirect if organized as an “umbrella organization”</li> </ul>
Financing Options	<ul style="list-style-type: none"> <li>• Only structural option that is eligible for private equity</li> <li>• Ineligible for philanthropic/charitable donation</li> <li>• Highly limited grant eligibility</li> </ul>	<ul style="list-style-type: none"> <li>• Cannot access private equity</li> <li>• Cannot receive tax-exempt donation</li> <li>• Limited grant eligibility</li> </ul>	<ul style="list-style-type: none"> <li>• Cannot access private equity</li> <li>• Only structural option that can receive tax-exempt donation from private sector and other charities</li> <li>• Full grant eligibility</li> </ul>

Table 1 – Legal Structures, Advantages and Limitations

<sup>5</sup>“Community Contribution Companies - Commonly Asked Questions,” accessed July 27, 2016, <http://www.fin.gov.bc.ca/prs/ccc/caq.htm>.

<sup>6</sup>“Community Interest Companies Now Available in Nova Scotia | The Canadian CED Network,” accessed July 27, 2016, <https://ccednet-rcdec.ca/en/new-in-ced/2016/06/17/community-interest-companies-now-available-nova>.

## Considerations for Registered Charities

The structure that combines maximum operational flexibility with maximum formal adherence to a social mission is the nonprofit organization. Many shared spaces choose the nonprofit structure. Non-profit organizations incorporated under any Provincial or Federal legislation may apply to the CRA to register as a charitable organization. This can be undertaken at any point during its existence. Charitable registration enables the organization to receive charitable donations, which is to say to issue tax receipts to individual donors and gain eligibility for grants from charitable foundations. As a trade-off, charitable status comes with specific limitations on the activities that the organization can carry on – being limited to those in explicit support of the registered charitable purposes or “objects”.

### CHARITABLE ORGANIZATION – LEGAL OBJECTS

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*Canadian law requires that an organization's purposes be exclusively charitable and define the scope of activities that can be engaged in by the organization. Subject to limited exceptions, all of a registered charity's resources must be devoted to these activities ... An organization's governing document must contain a clear statement of each of its purposes.<sup>7</sup>*

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The formulation of your organization's registered purposes, also known as “charitable objects,” is critical since they will determine the permissible activities the organization can undertake. CRA defines “charitable” purposes as being public in scope and belonging to one or more of four categories:

- Relief of poverty,
- Advancement of education,
- Advancement of religion,
- Other purposes beneficial to the community in a way the law regards as charitable.<sup>8</sup>

In addition to the categories, the CRA will assess each of the proposed objects to determine the beneficiaries of your activities, looking for a demonstration of direct public benefit. An organization may work towards the advancement of multiple purposes (and therefore have multiple objects). All of them must be regarded as charitable in order to obtain and maintain charitable status.

While it is possible to change an organization's objects after registration, the process is both labour intensive and risk laden, consisting of a formal consultation with the CRA's Charities Directorate, a duly carried out amendment to the bylaws or constitution, the filing of the amendment with the registering body (Provincial or Federal), and a final application to register the new objects as charitable with the CRA.

Shared spaces that are in a pre-incorporation phase would be well advised, therefore, to define a set of charitable objects that do not accidentally limit the scope of activities, both immediate and future. Each object must be specific, and consist of three parts as required by regulation,<sup>9</sup> while the combined set of objects should provide the breadth necessary for operations.

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<sup>7</sup> Canada Revenue Agency Government of Canada, “Guidance CG-019, How to Draft Purposes for Charitable Registration,” December 11, 2012, <http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cgd/drftprpss-eng.html>.

<sup>8</sup> Ibid.

<sup>9</sup> Ibid.

## UMBRELLA ORGANIZATIONS

If your shared space organization does not have directly public-facing charitable objects of its own, existing instead to help your constituent organizations (members, tenants, etc.) achieve their missions, you may still be eligible for charitable status:

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*[A]n organization that devotes its resources to improving the efficiency and/or effectiveness of the activities of other registered charities is itself charitable.<sup>10</sup>*

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If at least 90% of your member organizations are themselves registered charities, the typical activities undertaken by Nonprofit Centres are an explicit fit for this classification. However, if you work with a mix of registered charities and other organizations, you face limitations in the benefits you can confer onto non-charitable organizations. Such benefits must only further those activities at the non-charitable organizations which would themselves meet the charitable test, i.e. they must advance a charitable goal and be public in nature. The policy statement warns that “increasing the *general organizational capacity* of a *non-charitable* entity would not necessarily result in [...] the advancement of [any] charitable purpose. It would also be contrary to the requirements of the Act.”<sup>11</sup>

The CRA also recognizes the need of a charity to sometimes establish a separate entity to hold title to property on its behalf. Such a “title-holding company” is explicitly distinct from “a landlord organization that owns a facility, which it leases, rents, or allows the use of by other, generally unrelated registered charities.”<sup>12</sup> Instead, these entities hold title to property on behalf of its parent organization, which must itself be a charity.



<sup>10</sup> Canada Revenue Agency Government of Canada, “Policy Statement CPS-026, Guidelines for the Registration of Umbrella Organizations and Title Holding Organizations,” May 1, 2008, <http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cps/cps-026-eng.html>.

<sup>11</sup> *Ibid*, *emphasis added*.

<sup>12</sup> *Ibid*.



## A CHARITY'S BUSINESS ACTIVITIES – RELATED AND UNRELATED

Charities face limitations not just in how they *spend* but also in how they *earn* revenues. It is not sufficient that your organization's revenues are used to further your objects. All of the *activities* of a registered charity must be in support of those objects, including the revenue-generating activities. You cannot run a Tim Hortons franchise from within a charitable organization – even if all of the proceeds were to be directed to your charitable purposes – because “selling coffee and doughnuts” is not a itself a valid charitable activity.

Some revenue-generating activities – such as leasing of space or fee-for-service work such as event organization or capacity-building workshops – are broadly permissible if they are a part of your charitable objects. Other social enterprise activities in your centre – such as operating a shop in the common area or selling your publications online – may be permissible only if they are constitute a “related” business. Related businesses are either (a) run entirely by volunteers or (b) found to be both “linked” and “subordinate” to your charitable objects.<sup>13</sup>

“Linked” activities satisfy *any one* of the following four criteria:

- A usual and necessary concomitant of a charitable program; or
- An off-shoot of a charitable program; or
- A use of excess capacity; or
- The sale of items which promote the charity.

“Subordinate” activities satisfy *all four* of the following criteria:

- Business activity receives a minor portion of the charity's attention and resources; and
- The business is integrated into the operations, rather than acting as a unit; and
- Charitable goals dominate organization's decision-making; and
- No element of private benefit enters into operations.

An ongoing business activity which is not run primarily by volunteers and is not found to be both linked and subordinate is classified as an “unrelated” business. According to the Income Tax Act, charities are prohibited from conducting unrelated business activities. However, charities are allowed to found and wholly own subsidiary share capital companies, which can carry out business activities, pay income tax, and return proceeds back to the parent charity both in the form of donation and dividend.

## Conclusion

Non-profit Centre operators must choose a legal structure with trade-offs between operational flexibility and access to charitable financing resources. Understanding the core purpose of the enterprise will help to reconcile these competing priorities; understanding the legal options and requirements will help to navigate the process effectively and in a way that maximizes both to the extend possible. Be sure to seek broad input into your planning processes to effectively position your unique organizational context in the set of multiple regulations that will significantly impact your centre's capacity to achieve its mission.

<sup>13</sup> Government of Canada, “Policy Statement CPS-019, What Is a Related Business?”

## Further Reading

- Bubel, Anna. "Choosing a Legal Form for Your Social Enterprise." Social Enterprise Guides. Alberta: Western Economic Diversification Canada, 2006. <http://socialenterprisefund.ca/wp-content/uploads/2010/01/legal-structure.pdf>.
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- Government of Canada, Canada Revenue Agency. "Guidance CG-019, How to Draft Purposes for Charitable Registration," December 11, 2012. <http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cgd/drftprps-eng.html>.
- "Policy Statement CPS-019, What Is a Related Business?," November 1, 1999. <http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cps/cps-019-eng.html#N102BB>.
- "Policy Statement CPS-024, Guidelines for Registering a Charity: Meeting the Public Benefit Test," March 10, 2006. <http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cps/cps-024-eng.html>.
- "Policy Statement CPS-026, Guidelines for the Registration of Umbrella Organizations and Title Holding Organizations," May 1, 2008. <http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cps/cps-026-eng.html>.
- Manwaring, Susan, and Andrew Valentine. "Social Enterprise in Canada: Structural Options." SiG@MaRS, December 2011. <http://diverseconomyonboard.ca/wp-content/uploads/2015/11/MaRSReport-Social-Enterprise.pdf>.
- O'Connor, Pauline. "The New Regulatory Regime for Social Enterprises in Canada: Potential Impacts on Nonprofit Growth and Sustainability." Centre for Voluntary Sector Studies: Working Paper Series. Toronto, ON: Ryerson University, 2014.





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