

# Nonprofit Law in Canada

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This section describes the legal framework governing charities and nonprofit organizations (also known as non-governmental organizations or NGOs) in Canada, and includes translations of legislative provisions relevant for a foundation or advisor undertaking an equivalency determination of a foreign grantee under IRS Revenue Procedure 92-94.

These reports have been prepared by the [International Center for Not-for-Profit Law](#) (ICNL). Please direct corrections and comments to [Lily Liu](#).

We include hyperlinks to the following information, to the extent available:

- Longer country reports analyzing various aspects of local legislation; and
- Texts of local laws that affect the decision whether or not to qualify a grantee (generally in translation, although ICNL and the Council cannot warrant the accuracy of any translation; in addition, legislative excerpts were selected by in-country contacts, and ICNL and the Council cannot warrant that all relevant provisions have been translated).

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## **I. Summary**

### **A. Types of Organizations**

Canada is a federal jurisdiction with ten provinces and three territories. There are no statutory requirements under either federal or provincial law mandating the legal form in which a not-for-profit organization (NPO) must be organized. The most common legal forms are:

1. "Non-share" (membership) corporations, incorporated under either federal or provincial law;
2. Trusts, which are recognized in common law provinces (Quebec, which is a civil law jurisdiction, also recognizes forms similar to trusts); and
3. Unincorporated organizations or associations.

With the exception of federal incorporation, the creation of any organization is a function of the applicable provincial law. These vary somewhat from province to province.

## **B. Tax Laws**

### **1. General Classification**

The federal tax legislation in Canada makes distinctions among not-for-profit organizations that may be relevant for U.S. donors. Canadian federal income tax law distinguishes between "non-profit organizations" (hereinafter "NPOs") and "registered charities" (hereinafter "charities"). Although most potential grantees in Canada will be "charities," it is possible that NPOs may also seek funds from U.S. donors.

To qualify as an NPO, an entity must meet three tests. First, it cannot be a charity or an organization that could be registered as a charity. Second, it must be organized and operated exclusively for a purpose other than profit. Third, no part of its income may be paid or made available for the personal benefit of any proprietor, member, or shareholder (with an exception for amateur athletic organizations).

The category of "charities" is divided into charitable organizations and charitable foundations (consisting of private foundations and public foundations). A charitable organization, whether incorporated or not, must devote its resources to charitable activities carried out directly by the organization. A charitable foundation must provide funding to other charitable organizations, although it can also directly engage in charitable activities. All charities, like NPOs, are subject to the non-distribution constraint.

### **2. Income Tax Exemption and Tax Treatment of Donations**

Neither NPOs nor registered charities are subject to income tax. Additionally, Canada recognizes a list of foreign universities, domestic municipalities, and certain other preferred organizations which are not technically "charities," but which are treated as such for the purpose of giving tax relief for donations. Together with charities, these listed

organizations are collectively known as "qualified donees." NPOs and qualified donees are exempt from most types of income taxation including the taxation of most common sorts of income. They may be subject to property taxes and may have to register for Goods and Services Tax/Harmonized Sales Tax (GST/HST) purposes, however.

All qualified donees are publicly listed by the Canada Revenue Agency (CRA). The listing may be found on the [CRA website](#).

Individuals are entitled to a tax credit (as opposed to a deduction) for contributions to qualified donees. Corporations, by contrast, receive a tax deduction for their donations to qualified donees.

### **3. Other Tax and Fiscal Provisions**

Canada has a 5 percent federal tax known as the Goods and Services Tax (GST), however the GST does not apply to foreign grants. Moreover, while charities and NPOs are subject to the GST regime, there are many potentially applicable exemptions. With regard to customs duties, there are no particular exemptions for charities or NPOs. Real property taxes, which are part of provincial and/or municipal jurisdiction, are applied based on provincial law and so vary depending upon the jurisdiction.

## **II. Applicable Laws<sup>[1]</sup>**

Because Canada is a confederation with ten provinces and three territories, there are potentially fourteen different jurisdictions with laws applicable to NPOs and charities. However, federal law, because of the impact of the donation tax credit, is the most important of these regimes. Key federal legislation consists of:

- [The Income Tax Act](#); and
- [The Canada Not-for-Profit Corporations Act](#).

While the provinces have jurisdiction over charities, there is little legislation in this area; instead, most provinces rely primarily on the common law powers of the Attorney General to act when there has been a breach of fiduciary duty. However, Ontario and Alberta have enacted legislation which is of some consequence for charities, namely:

- The Charities Accounting Act (Ontario);
- The Religious Organizations' Lands Act (Ontario) [\[2\]](#); and
- The Charitable Fund-Raising Act (Alberta).

The Trustee Acts of all provinces are relevant. Finally, for membership corporations, each province also has legislation that deals with the incorporation of corporations without share capital.

### **III. Relevant Legal Forms**

Neither federal nor provincial law sets forth requirements for the organizational form of an NPO or charity. The most common forms are "non-share" corporations, trusts, and unincorporated organizations or associations. The Federal Income Tax Act does, however, distinguish between NPOs and charities—a distinction that may prove useful in making equivalency determinations. [\[3\]](#)

#### **1. Not-for-profit Organizations (NPOs)**

The Income Tax Act provides the primary definition of a non-profit organization (NPO), as follows:

"[A] club, society or association that, in the opinion of the Minister, was not a charity within the meaning assigned by subsection 149.1(1) and that was organized and operated exclusively for social welfare, civic improvement, pleasure or recreation or for any other purpose except profit, no part of the income of which was payable to, or was otherwise available for the personal benefit of, any proprietor, member or shareholder thereof..." (Income Tax Act, Paragraph 149(1)(l)).

The term "club, society, or association" includes corporations and trusts. The key criterion is that the pursuit of profit cannot be a purpose of the entity. This does not mean that activities which incidentally generate a profit are forbidden, however, so long as the *motive* for the activity is not the generation of profit. Also, because the Income Tax Act does not require registration of NPOs, they essentially self-assess their status.

## **2. Charities**

The Income Tax Act distinguishes between "charitable organizations," "public foundations," and "private foundations" based on the entity's structure, source of funding, and mode of operation. As a practical matter, charitable organizations are operational charities, while foundations are almost always grantmakers.

### *Charitable Organizations*

A registered charity is designated as a "charitable organization" if:

1. It is constituted and operated exclusively for charitable purposes;
2. All the resources that are devoted to charitable activities are carried out by the organization itself or are allotted to qualifying disbursements.
3. No part of its income is payable to or otherwise available for the personal benefit of any proprietor, member, shareholder, trustee, or settlor thereof;
4. More than 50% of the directors, trustees, officers, or others in similar positions deal at arm's length with each other;
5. It is not controlled directly or indirectly by a person who has contributed to the organization amounts that total more than 50% of the organization's capital, a person who is not at arm's length with someone who has contributed to more than 50% of the organization's capital.

### *Public Foundations*

A registered charity is a "public foundation" if:

- a. More than 50% of its directors, trustees, officers, or other like officials deal at arms length with each other, including individual members of groups that serve these positions; and
- b. It is not controlled directly or indirectly by a person who has contributed to the organization amounts that total more than 50% of the organization's capital, a person who is not at arm's length with someone who has contributed to more than 50% of the organization's capital.

### *Private Foundations*

A registered charity is a "private foundation" if it does not qualify as a public foundation.

A private foundation is one in which more than 50 percent of the board is **not** at arm's length with each other or more than 50% of the board contributes to more than 50% of the private foundation's revenue.

Grants to private foundations may raise "out of corpus" and other issues for U.S. donors. For a detailed discussion of issues arising with grants to private foundations (as defined under U.S. law).

## **IV. Public Benefit Status**

NPOs are not required to serve the public benefit. For example, some organizations are organized purely for the benefit of their members, such as the Canadian Bar Association, sporting and social clubs, labor unions, and political parties (Income Tax Act subsection 188.1(1)). However, some NPOs may be organized for public benefit or social welfare purposes.

In contrast, charities must satisfy the common law test of "charity." There is no federal or provincial statutory definition of this term, and the

concept of what constitutes charitable activities draws heavily on traditional English common law dating back several centuries. Over the years, the courts have generally based their interpretation of "charity" on four categories described in English common law:

- The relief of poverty;
- The advancement of education;
- The advancement of religion; and
- Certain other purposes for the benefit of the community.

The CRA also issued guideline [CPS-024](#) in 2006, which explains how the CRA determines whether a charity serves the public benefit. The guideline echoes the four categories of charity listed above, and outlines a general "test for public benefit" that CRA examiners use when registering charities.

Finally, it should be noted that in the case of other organizations that comprise the category of "qualified donees" (apart from registered charities), a public benefit purpose is not a requirement.

## **V. Specific Questions Regarding Local Law**

### **A. Inurement**

The Income Tax Act contains the following provision which applies to both NPOs and charities:

"No part of the income of which is payable to, or is otherwise available for, the personal benefit of any proprietor, member, shareholder, trustee, or settlor thereof" ([Income Tax Act, Paragraph 149 \(1\)\(l\)](#)).

This is interpreted to mean that no dividend or similar payment or a liquidating distribution (out of income in the case of an NPO) can be made for the personal benefit of individual proprietors, members, etc. in an organization. It does not preclude, however, members or others



being paid for services actually rendered. There are other statutory and common law provisions which create further restrictions on charities from making such payments. However, only Ontario has a statutory mechanism to approve payments for services rendered by directors (but not qua director which is still prohibited) These requirements, specified in law and practice, are generally consistent with U.S. prohibitions on private inurement.

## **B. Proprietary Interest**

In the case of an NPO, members may have a proprietary interest and may, for example, be entitled to a return of contributed capital upon retirement as a member or upon the dissolution of the organization.

In the case of a charity, no proprietary interest is possible, and the legislative framework precludes a member from receiving any assets, whether out of income or capital. Indeed, if such a transfer takes place, the Income Tax Act imposes at least 100 percent tax on the amount so paid ([Income Tax Act, Subsection 188.1\(4\)](#)).

## **C. Dissolution**

The dissolution of a corporation is governed by the applicable federal, provincial, or territorial law under which it was set up. In the case of a trust, the dissolution would be governed by the trust deed or, if the deed were silent on the subject, might require the intervention of a court.

In practical terms, aside from the legal procedures, the key element remains the federal Income Tax Act. For NPOs, there are statutory rules that deal with the conversion of such an organization into a taxable entity, including the winding up and distribution of assets to members. When this occurs, the law requires that the organization's tax-free

status be terminated, deeming a disposition of all the assets for tax purposes, and taxing the recipients of any money or assets.

On the other hand, to be registered as a charity, the entity's incorporating documents or by-laws must include a clause stating that upon winding up (or upon a loss of registered status) all the assets must go to another qualified donee. If this is not done, there is a 100 percent tax on recipients of any assets (Income Tax Act, [Subsection 149\(10\)](#) and [Subsection 188\(1\)](#)).

## **D. Activities**

### **1. General**

As discussed above, an NPO can be set up for any purpose other than to generate profit. In practice, this means that almost any sort of activity can be a legitimate purpose. Indeed, the Income Tax Act does not require registration of these organizations, and they self-assess their own status.

On the other hand, registered charities are limited to activities which are charitable as defined by common law, namely the relief of poverty, the advancement of education, the advancement of religion, or "such other purposes which are beneficial to the community" as recognized by case law (see [General Requirements for Charitable Registration](#)).

The Income Tax Act also deems certain activities to be charitable, including the transfer of funds to a qualified donee, the carrying on of a "related business" and, within strict limits, "political activity." These issues are discussed below.

### **2. Economic Activities**

NPOs, by definition, cannot be organized or operated for the purpose of making a profit. However, NPOs can engage in a range of activities that

generate revenue and, indeed, may generate a profit, if it is clear that this is not a purpose of the organization.

Registered charities (other than private foundations) are allowed to carry out "related business activities" ([Income Tax Act, Paragraph 149.1\(6\)](#)). This term is undefined. As a practical matter, when the issue first arose before a court, a two-to-one majority held that if the profits of an activity were used in charitable activities of the organization, that activity was a related business activity. This case was later distinguished by the same court, however, and it seems fair to say that the "destination test" will no longer apply in determining what qualifies as a related business. A discussion of this term can be found in the [CRA](#).

## **E. Political Activities**

There are no limits on the political activities of NPOs; indeed, political parties are a sub-category of the NPO category of organizations (as they are in the U.S.).

Charities pose a more complex case. The current law allows charities to engage in political activities so long as those activities are in furtherance of their charitable activities and are not partisan in nature (i.e., do not directly or indirectly support or oppose any political party or candidate for public office). ([Income Tax Act, Paragraph 149.1\(6.2\)](#)). The CRA has [clarified](#) that "direct" support or opposition means either that (1) the charity's external messaging communicates that it supports or opposes a political party or candidate, or (2) the charity transfers any of its resources to a political party or candidate, or allows a political party or candidate to use its resources at below fair market value; "indirect" support or opposition means either that (1) the charity's records or internal messaging explicitly reveal it carried on an activity to support or oppose a political party or candidate, or (2) the charity transfers any of its resources to a third party, to be used to support or oppose a political

party or candidate. The guidance provides illustrative examples of direct and indirect support or opposition.

While this limitation on direct and indirect support or opposition of political party or candidate for public office would seem to meet the U.S. ban on "electioneering" activities by qualified donees, the lack of guidance with respect to what is "political" under Canadian law may pose some issues for U.S. donors. Charities may pursue their stated charitable purposes by carrying on unlimited public policy dialogue and development activities in furtherance of those purposes. [\[4\]](#)

Guidance CG-027 also eliminates the requirement for registered charities to report on funds used for political activities using the T-3010 form.

## **F. Racial Discrimination**

Canada has produced a great deal of legislation to combat racial discrimination and the promotion of racial hatred, and the courts have not hesitated to apply this legislation to NPOs. In case after case, the courts, bolstered by legislation, have sought to ensure that any form of discrimination in the field of charities and NPOs is barred. [\[5\]](#)

That said, the tax authorities also have legislative power to recognize foreign universities as being the equivalent, for tax purposes, of a Canadian registered charity. Because the statutory test is simply that the institution "usually" has Canadian students and that it is accredited in its own jurisdiction, it is possible that some such universities might practice some forms of discrimination. A full list of such institutions will be found on the CRA [website](#). In the 2018 federal budget, the listings of foreign universities was simplified; qualifying institutions are listed on the CRA website.

## **G. Control of Organizations**

No restriction exists on the control of Canadian not-for-profit organizations by other organizations or persons. With respect to other forms of organizations, it is possible that a Canadian association or foundation may be controlled by a for-profit entity that establishes it, even though it does not own it (which will lead to additional IRS scrutiny). The same would be true for a Canadian association or foundation controlled but not owned by an American grantor charity (which requires that the charity specifically so provide in the affidavit).

## **VI. Tax Laws**

The following section discusses relevant tax legislation, recognizing that taxes may affect the amount of the grant actually flowing to the donee.

### **A. Tax Exemptions**

NPOs and registered charities are generally exempt from any taxes on income. [\[6\]](#) If an NPO actually turns out to have a profit motive, then it loses its NPO status and is treated as an ordinary taxable entity even if it is organized under corporate 'not for profit' acts.

Similarly, a registered charity is generally exempt from income tax. Any breach of the statutory rules might lead to a revocation of its registration. CRA enforced legislation creates a series of potential fines for breach of the rules; such breaches may also lead to a temporary suspension of the privilege of issuing receipts.

### **B. Tax Treatment of Donations**

For practical purposes, the main distinction between NPOs and charities (and other qualified donees) is that gifts to the former generally cannot qualify for tax relief for donations, while gifts to the latter may qualify. [\[7\]](#) Canada relies on a system of tax credits (as opposed to deductions) to give tax relief to individuals, while corporate donors receive tax benefits through the conventional deduction system. Thus,

for gifts to a charity, an individual donor may receive a tax credit while a corporate donor may receive a deduction. Both individual and corporate donors may receive a tax deduction for gifts made to a non-profit if the gift was made for the purpose of contributing to the non-profit's income.

In addition, it should be noted that Canada does not have gift taxes. There are also no death duties, per se, though there may be a deemed disposition of capital property on death.

Several types of organizations are "qualified donees" under the Income Tax Act. These include registered charities, foreign universities given this status, the United Nations and its agencies, among others. In 2019, as part of its undertaking to support non-profit journalism, the government also added journalism organizations to the list of organizations that may obtain "qualified donee" status. [\[8\]](#)

## **C. Sales Taxes**

Charities and NPOs are generally part of the combined federal and provincial sales tax regimes, and though they may have some special rules based on specific activities, there is no general exemption available. That said, the federal Goods and Services Tax does have a special feature: Once an organization has calculated its net tax liability, if any (GST collected net of input tax credits), if it is either a registered charity or an NPO which receives 40 percent of its funding from one or more levels of government, it is entitled to receive a rebate of one-half the net tax paid. [\[9\]](#) Moreover, there is no GST due on foreign grants.

Ontario, Newfoundland and Labrador, Nova Scotia, and Prince Edward Island adopted a "harmonized" sales tax (HST) whereby existing provincial sales taxes will be linked to the federal GST as a single levy. Charities and non-profits in the other provinces will have to comply with both federal GST and provincial sales tax (in applicable provinces).

## D. Tax Conventions

The United States and Canada have entered into a tax treaty that addresses cross-border donations. Specifically, the tax treaty permits charitable deductions for contributions made to Canadian charities if certain requirements are met. The most important part of the tax treaty rules is that the deduction may not exceed the amount of the donor's Canadian source income, which significantly diminishes the utility of this provision to many U.S. grantmakers. Moreover, under IRS Notice 99-47, I.R.B., 1996-36, page 344, all Canadian registered charities are deemed to be the equivalent of a tax-exempt organization under the Internal Revenue Code. Unfortunately, Notice 99-47 does not address whether private foundations may rely on this equivalency, so prudence suggests that U.S. grantmakers still undertake equivalency determinations. For a detailed discussion of this tax treaty, please see Appendix II of *Beyond our Borders*. [\[10\]](#)

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## Footnotes

[1] Other legal authorities consulted in preparing this Note include the following:

The best single source of information about the federal regulation of charities and NPOs is found on the website of the Charities Directorate of the Canada Revenue Agency ([CRA](#)). This site has interpretation bulletins, forms, newsletters, and a searchable database for registered charities.

The definitive work on the incorporation of NPOs and charities in Canada, covering all jurisdictions, is the [Corporate and Practice Manual for Charities and Not-For-Profit Corporations](#) by the late R. Jane Burke-Robertson and Terrance S. Carter, which is a newly-revised publication

available from Carswell, the Canadian arm of Thomson Professional Publishing.

The preeminent source of all law relating to charities and non-profits is the multi-volume work entitled Charities Taxation, Policy and Practice by Arthur Drache and Robert Hayhoe, also published by Carswell.

[2] Various other provinces have analogs of this act.

[3] Each province and territory has its own income tax act, but in the area of NPOs and charities, almost all precisely mirror federal legislation. Only Quebec has a separate registration regime for charities, but that registration is functionally automatic when evidence of federal registration is presented.

[4] More information and updates can be found on the CRA website, available at <https://www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/federal-government-budgets/budget-2018-equality-growth-strong-middle-class/public-policy-advocacy-activities-charities/qa.html>.

[5] See, for example, Canada Trust v. Ontario Human Rights Commission 74 OR (2d) 481; 69 DLR (4th) 321; Gould v. Yukon Order of Pioneers [1996] 1 SCR 571; re Ramsden Estate 139 DLR (4th) 746.

[6] There is in fact one small exception; where a non-profit organization is set up to provide "dining, recreational or sporting facilities" to its members, it is subject to tax on any passive investment income it might earn in excess of \$2,000.

[7] Payments made to an NPO may qualify for tax relief as business deductions in appropriate cases. Thus, lawyers would normally be able to deduct the fees they pay to the Canadian Bar Association (a non-profit) if the lawyer is practicing.



[8] Please refer to the [CRA's site](#) for more information on the government's plans to support Canadian Journalism.

[9] While for most organizations, this may be a relatively small concession, it is very valuable when major purchases are made or when a building is being constructed. Indeed, many organizations which might not otherwise wish to be registered as a charity do so to qualify for GST rebates.

[10] There is some question as to whether registered charities are subject to the limitations on grantmaking from Canada to the U.S. based on the donor's U.S. source income; however, according to the CRA, they are. A foundation known as The Prescient Foundation asked the Supreme Court of Canada to revise this interpretation of the Treaty, but the Court declined to do so.