



**DATE:** May 2, 2016  
**RE:** End of Operating Agreements: Legal Issues

---

All across Canada, non-profit housing providers are faced with the expiry of their federal operating agreements. Once the subsidy is withdrawn, the housing provider becomes responsible for the ongoing financial sustainability of their housing project. With this withdrawal of federal funding, housing providers are looking at all of their options to remain financially viable and continue to provide housing to low income Canadians. Many of the options have legal implications which are described in this Memorandum.

## **INTRODUCTION**

### **Scope of this Memorandum**

This Memorandum is intended to assist Ontario housing providers in analysing their options. While many of the rules governing housing across Canada are similar (or the same when federal statutes apply) we note that this memorandum applies to Ontario providers only. This Memorandum does not consider any special rules governing co-operatives.

**Please note that this summary of legal issues is provided for general information purposes only, and does not constitute legal advice. Housing providers should not rely on this document as legal advice. Legal advice specific to any particular circumstance should be obtained before taking any steps to implement one or more of the proposed strategies.**

A summary of the legal issues is set out below. First, the memo sets out some general legal considerations that apply in all cases, regardless of the strategy being considered. Every housing provider should be sure it understands these issues. Following that is a list of the potential strategies and the legal issues specific to each. In some cases a strategy is organized as a series of questions a Housing Provider and its board might ask itself to determine whether an issue applies in its case, followed by a short description of the legal issues that result.

### **Housing in Ontario**

The housing regime in Ontario is governed predominately by the *Housing Services Act, 2011* (the "**Act**"). The Act continues much of the regime established by its predecessor, the *Social*



*Housing Reform Act*, confirming the role of municipal and territorial<sup>1</sup> Service Managers as the agencies with responsibility for oversight of housing within their respective jurisdictions. They are tasked by the Act with developing and implementing a housing and homelessness plan. The Act and its regulations also:

- set out the rules for the calculation of Rent-geared-to-Income ("RGI") rent;
- establish the minimum requirements for RGI assistance to be provided by each Service Manager;
- establish the general duties of a housing provider to ensure a project is well managed and maintained in a satisfactory state of repair and fit for occupancy;
- set out rules relating to housing providers funded under the provincial non-profit programs and certain Federal/Provincial Programs ("Part VII Housing Projects"); and
- Impose consent requirements on the mortgaging and transferring of certain housing projects.

Any post operating agreement strategy has to be considered in the context of, and in conformity with, the Act. As some parts of the Act apply differently to providers funded under different programs, it is important to know the program under which a project was created. In most cases, a Project will be identified by name in the Regulations to the Act<sup>2</sup> with its funding program.

## **A. GENERAL GOVERNANCE AND CORPORATE CONSIDERATIONS**

### **1. Obligations of the Board**

For the most part, discussions relating to changes required to meet this challenge will make their way to the Board of Directors. Each housing provider will need to determine for itself which combination of the strategies discussed below it will use to adapt to its new reality based on their individual opportunities. Excess land or the availability of rent supplements, for example, will all differ from provider to provider. There is no "one-size fits-all" solution.

In considering its options, every Corporation's directors have fundamental duties to the Corporation which he or she must bear in mind:

- Directors owe fiduciary duties to the organization. This means that each director must act honestly, in good faith and in the best interests of the Corporation. In addition, directors must exercise reasonable care, skill, prudence and diligence in making decisions regarding the organization.
- Directors make decisions collectively as a board, and not as individuals. Directors should consider all aspects of the decision and the potential consequences, having regard to the specific needs and circumstances of the Corporation.
- Directors who have a conflict of interest (or potential conflict) arising out of any matter affecting the organization are legally required to disclose the nature and extent of the conflict to their fellow directors, and to refrain from attending meetings regarding the

---

<sup>1</sup> In Northern Ontario, the Service Manager function is carried out by territorial District Social Services Administration Boards.

<sup>2</sup> See Ontario Regulation 368/11 which shows project and the program pursuant to which they were funded.



conflict and voting on or otherwise influencing the Board's decision in relation to the matter.

- Any strategy employed by a board should consider potential legal and tax issues that can arise. Many of these issues could lead to serious legal and financial consequences for the organization if ignored or disregarded. The Board must take these issues into consideration before determining how it will proceed and which strategies it will adopt.

## 2. **Compliance with Income Tax Act**

A housing provider will generally be classified as one (and only one) of the following under the *Income Tax Act* (Canada):

- a registered charity;
- a non-profit organization; or
- a housing corporation constituted exclusively to provide low-cost housing to the aged.

These terms are defined by the *Income Tax Act* and have specific technical meanings. While those organizations which qualify as one of the above are exempt from tax, each exemption is based on specific rules and requirements. If those rules and requirements are not met, which could occur with some of the strategies discussed below, an organization could lose its tax exemption and be subject to both penalties and tax.

If it is uncertain of its status, a housing provider can check the Canada Revenue Agency's Charities Directorate database to confirm whether it is a registered charity<sup>3</sup>.

If it is not a registered charity, a housing provider may be a tax-exempt non-profit organization. A housing corporation may be able to confirm this by searching Industry Canada's database of federally incorporated entities.<sup>4</sup>

Housing providers can also check their past tax returns to confirm whether they have been claiming non-profit status.

The non-profit organization tax exemption is not automatic and there is considerable misunderstanding in the sector that the simple act of incorporation provides the exemption. It is necessary for a corporate non-profit to annually file a T2 Corporate Income Tax Return, and in some cases a T1044 Non-Profit Organization (NPO) Information Return, and to annually claim its tax exemption. If a non-profit organization has not filed these required returns, or has missed one or more years, it will be taxable. A non-profit organization should immediately seek legal advice if it finds itself in this situation. There is a voluntary disclosure process with the CRA which may assist the non-profit organization in avoiding the consequences of failing to file.

## 3. **Compliance with Articles and Letters Patent**

In addition to being mindful of the requirements to maintain its tax exempt status, a housing provider must be aware of the purposes set out in its Articles (used for *Business Corporations*

---

<sup>3</sup> <http://www.cra-arc.gc.ca/chrts-gvng/lstngs/menu-eng.html>

<sup>4</sup> [https://strategis.ic.gc.ca/app/scr/cc/CorporationsCanada/fdr1CrpSrch.html?locale=en\\_CA](https://strategis.ic.gc.ca/app/scr/cc/CorporationsCanada/fdr1CrpSrch.html?locale=en_CA)



Act companies) or Letters Patent or Articles (used for *Corporations Act* companies). These are the fundamental "constating documents" of the Corporation. Every housing provider will have constating documents which set out its name, purposes and other fundamental matters. Some housing providers may be very familiar with their constating documents. These documents tend to be static but may need to be amended to reflect changes over the years. In many cases, the constating documents will have been amended many times, with directors largely unaware of this governing document.

All non-profit organizations and charities incorporated as non-share capital corporations under the *Canada Corporations Act* before October 14, 2012 were recently required to undergo a formal transition process under the new *Canada Not-for-profit Corporations Act*. Federally incorporated organizations that failed to do so by October 14, 2014 face the prospect of dissolution (which would also result in the revocation of their charitable status). A similar transition process is expected to take place in Ontario's not-for-profit sector over the next few years under the *Not-for-profit Corporations Act, 2010*. For more information see [http://www.sse.gov.on.ca/mcs/en/Pages/Not\\_For\\_Profit.aspx](http://www.sse.gov.on.ca/mcs/en/Pages/Not_For_Profit.aspx). Ontario Non-Profits can also consider continuing under the *Canada Not-for-profit Corporations Act*.

Registered charities and non-profit organizations may only undertake activities (and expend funds) that advance the purposes stated in their constating documents. Activities or programs which do not advance those purposes are prohibited. It is, therefore, crucial that the purposes set out in a housing provider's constating documents accurately reflect what the organization is actually doing and are broad enough to encompass the strategies that it might decide to undertake, which are described below. In addition, the purposes of registered charities must fit within the purposes prescribed by the *Income Tax Act* and accepted at common law as charitable.

If necessary, a housing provider can amend its purposes to reflect its activities and objectives. In most cases, amendment of the Articles or Letters Patent requires that a special resolution of the members of the organization be passed to approve the change. Depending on the size and complexity of the organization's membership, a special resolution will often require a members' meeting to be held.

For housing providers that are registered charities, any change to the purposes of the organization must be sent to the Charities Directorate of the Canada Revenue Agency for approval, either before or after the amendment is passed. Neither a registered charity nor a non-profit organization can have, as a purpose, the generating of profit or the running of a business or commercial enterprise. This does not necessarily mean that a housing provider cannot undertake such an activity, only that it cannot be a purpose of the organization to do so. All revenue generating activities that are commercial in nature can only be carried out to advance one of the organization's charitable or non-profit purposes. It is important for charities or non-for-profit organizations to accumulate as little excess revenue as possible for each year. If the Canada Revenue Agency deems their reserves to be unreasonably high, the organization may lose its tax-exempt status. A charity or non-for-profit organization that accumulates high reserves may be advised to expand its activities consistent with its purposes in order to eliminate any unreasonably high reserves.



#### 4. **Compliance with Bylaws**

In addition to its Articles or Letters Patent, every housing provider has Bylaws that set out its governance framework. Compliance with an organization's Bylaws is mandatory. All decisions of the Board or an organization must be made in accordance with the Bylaws (except in circumstances where the Bylaws contain provisions that are contrary to legislation). It is possible that Bylaws may restrict or regulate the activities of the organization and should be drafted to promote processes that provide for efficiency and accountability.

### B. **SPECIFIC LEGAL ISSUES IN POTENTIAL STRATEGIES PROPOSALS**

Potential strategies are listed in the following pages, along with a summary of the legal considerations.

#### 1. **Increase Rent Revenues**

There are a number of different strategies a housing provider may use to increase rent revenue from its existing buildings. These may be used separately or in combination. Each has different (though overlapping) legal issues to consider.

##### 1.1 **Increasing market tenant rent**

Rent increases in the private market sector are regulated by the *Residential Tenancies Act, 2006* (the "RTA"). The RTA sets out a number of rules that restrict the ability of landlords to freely increase rent in market (as opposed to RGI) units.

A landlord cannot increase the rent in the first 12 months of a tenant entering a tenancy agreement. A landlord may increase rents once every 12 months for sitting tenants by the guideline amount without seeking approval from the Landlord and Tenant Board. The annual rent guideline averages the monthly Ontario Consumer Price Index over a 12 month period that ends at the end of May of the previous calendar year. If the calculation for the annual guideline amount exceeds 2.5% in any given year, it will be reduced to 2.5%. If an increase of more than 2.5% is sought, a landlord must either follow a prescribed process to seek approval for an Above Guideline Increase or, in certain circumstances, landlords and tenants can agree that the rent will be legally raised above the guideline.

Landlords must provide 90 days written notice before the effective date of any rental increase.

Because of these statutory restrictions, simply increasing market rents for existing non-RGI tenancies as a means to quickly recover lost subsidy income may not be feasible.

##### 1.2 **Increasing RGI tenant rent**

The rules about rent calculations in social housing are not part of the purview of the RTA. Rather, the current method for calculating RGI rent is established under the *Housing Services Act, 2011* and is quite complex.<sup>5</sup> It involves an analysis of all sources of gross income, a

---

<sup>5</sup> The RGI rules in the Act apply to the majority of providers including all former public housing, rent supplement programs, and most non-profits, identified in the Regulations to the Act as Programs 1(a), 1(b), 2(a), 2(b), 6(a) and 6(b). They do not apply to certain former federal programs and urban native



determination of whether utilities are paid by the housing provider or the household, amongst other factors. Tenants living in an RGI unit must declare every time their income changes. Changes in a tenant's income, assets or household composition may result in an increase or decrease in RGI rent.

Since the RGI Rent charged to a tenant is set by legislation based on these factors, it is not possible to "increase" RGI rent, per se. Further, since the subsidy associated with RGI rentals is intended to be the difference between the amount paid by the tenant and a market rental determined by the Ministry, there is no additional income to be gained from an RGI tenant so long as that tenant qualifies as an RGI tenant. It is possible, of course, that an RGI tenant will lose the subsidy because they have been successful in the job market. At that point, the rules of the RTA will apply.

### 1.3 Reducing Percentage of RGI units

#### (a) *Adjusting tenant mix may affect tax-exempt status*

Housing providers, whether registered charities or non-profit organizations, must maintain a high percentage of low-income or subsidized units in order to maintain tax-exempt status. Reducing the percentage of RGI units beyond a certain point will jeopardize tax exempt status and may lead to revocation of charitable registration (for registered charities) or loss of tax exempt status (for non-profit organizations). The Canada Revenue Agency (the "CRA") does not state a specific percentage in its current guidance, but previous CRA policy statement CPS-020 suggested that for registered charities, only up to 10% of a housing charity's units may be occupied by tenants paying market rents.

The CRA indicates that a registered charity must annually assess the eligibility of beneficiaries of housing that relieves poverty. It further suggests the eligibility criteria should include the income, as well as the assets and liabilities of the potential beneficiaries and that such persons can be described as "needy, necessitous, underprivileged, low-income, of small/limited means, or other judicially recognized synonyms".

#### (b) *Adjusting tenant mix has implications under the Residential Tenancy Act*

Converting a RGI tenancy into a market tenancy entails terminating the current tenancy. A landlord must have a valid reason (as described in the RTA) for terminating a tenancy. Fiscal necessity is not listed as a reason and is unlikely to be considered an adequate reason for unilaterally ending a tenancy.

Housing providers must be cautious to avoid liability for wrongful termination of tenancies contrary to the RTA. For a Corporation, the penalty can be as much as \$100,000.00.

#### (c) *Adjusting tenant mix may or may not be permissible under certain restrictive covenants and housing agreements with government*

---

housing. While these programs are funded by the municipality, they follow their original operating agreements for RGI calculations.



In addition to the considerations above, some properties may have a required minimum number of subsidized units set out in a restrictive covenant, a housing agreement registered on title to the property or a funding/contribution agreement. If there is such an obligation, the housing provider cannot contravene this covenant or agreement without risking significant consequences.

For example, affordable housing funding agreements over the last decade have provided capital subsidies and require a certain number of units to be affordable units. Failure to maintain such units as affordable can result in a severe consequence – repayment the original capital subsidy.

It may be possible to remove the covenant or agreement with the consent of the responsible party, usually the municipal government or an agency of the provincial or federal government.

#### 1.4 **Taking higher rent tenants at "turnover"**

The "turnover" of a rental unit provides private landlords in Ontario with their best opportunity to increase revenue from their properties. The RTA follows an approach known as "vacancy de-control", meaning that landlords are free to negotiate a fresh base rent with each new tenant. With respect to any existing market units, Housing Providers benefit from the same right. To the extent they can extract a higher rent from an incoming market tenant, they are free to do so.

On the vacancy of a tenant paying RGI rent, the Housing Provider can consider conversion to a market unit, subject to the concerns set out above,

Lastly, a housing provider must not discriminate against prospective tenants contrary to the *Human Rights Code*, on the basis of race, colour, ancestry, place of origin, religion, marital status, family status, physical or mental disability, sex, sexual orientation or age of the potential tenant.

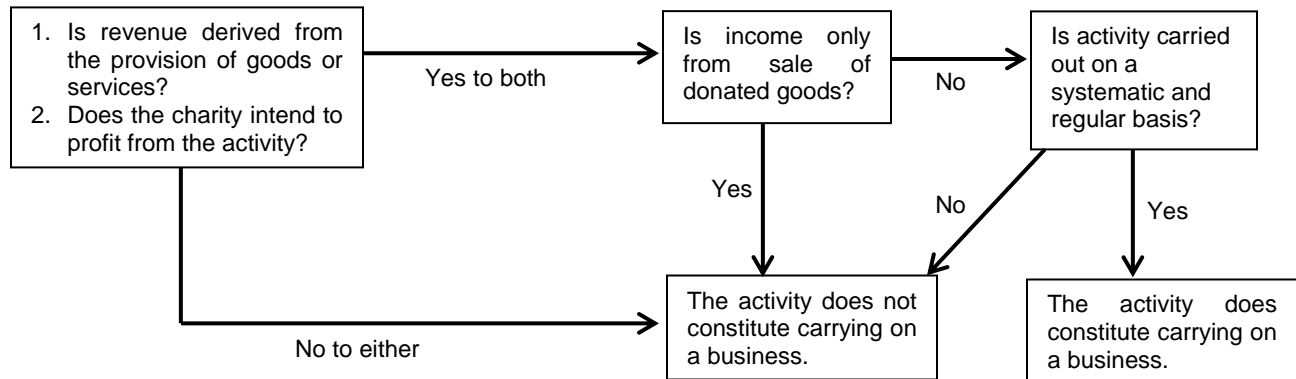
## 2. **Diversify Revenue Streams through business activities or commercial use of space**

The rules regarding whether (and how) a housing provider can conduct a business activity or rent space for commercial purposes vary significantly depending on whether the housing provider is a registered charity or a non-profit organization, as described above. Before considering this option in any detail, the housing provider must confirm its status.

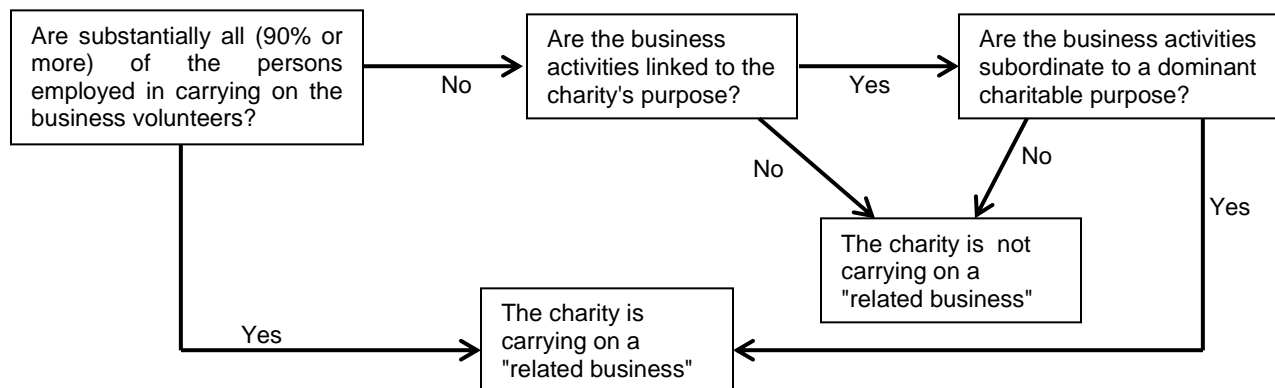
### 2.1 **Registered Charity**

Registered charities are permitted to carry on limited business or commercial activities and only those that are "related" to their charitable purposes. It would not be possible, for example, for a wildlife conservation organization to decide to operate a coffee shop out of its office premises because the operation of a coffee shop bears no relationship whatsoever to the charitable purpose for which it was established. It would however be possible for a hospital to operate a coffee shop, because as a public facility it is open to visitors and others who need to obtain food on the premises while visiting or assisting family members who are patients.

The decision tree below generally describes the Canada Revenue Agency's administrative policy regarding whether a charity is carrying on a business.



If a charity is found to be carrying on a business, the issue of whether it is a "related business" (i.e. a permissible business) can generally be determined as follows.



See the CRA's policy on related business for further detail on whether a business activity is "linked" and "subordinate" to the charity's purposes. <http://www.cra-arc.qc.ca/chrts-qvng/chrts/plcylcpslcp-019-eng.html>.

If a charity is running a "related business", then the business activity can likely be conducted within the charity. Otherwise, the business is an "unrelated business" and the charity cannot conduct that business activity itself.

Running an unrelated business within a charity is prohibited by the *Income Tax Act*. If a charity is found to be conducting an unrelated business, it may lead to the revocation of charitable registration, which entails the charity losing its receipting privileges and being required to transfer the entirety of its assets to another "eligible" charity.

If the charity determines that it is unable to conduct the business activity within the charity itself, a common solution is to incorporate a taxable subsidiary wholly owned by the charity to carry out the business activity. Creation of a taxable subsidiary requires separate incorporation and governance. Care must be taken to ensure that the requirements of the *Income Tax Act*





continue to be met, and there will be additional administrative and filing requirements. It is necessary also that any sharing of space, staff and equipment between the two organizations be carefully documented in writing to ensure that the charity does not provide any inappropriate benefit to the subsidiary. The subsidiary is fully taxable on its income, but may be able, within the restrictions of the *Income Tax Act*, to decrease its taxable income by making donations to its parent charity.

## 2.2 Non-Profit Organization

The *Income Tax Act* provides a tax exemption for organizations which, amongst other things, are organized *exclusively* for purposes other than the making of profit. This requirement places considerable constraints on the ability of a non-profit organization to operate a business or commercial activity. Moreover, the applicable provisions of the *Income Tax Act* are interpreted very narrowly by the Canada Revenue Agency.

The current position of Canada Revenue Agency is that non-profit organizations wishing to maintain their tax exemption can only generate profits which are "incidental and unintended". If a non-profit undertakes any activity with the intention of generating profit (i.e. revenue which will exceed expenses) then the organization no longer qualifies as a non-profit organization and will lose its tax exempt status, even if all the profit is used by the organization to carry out its non-profit purposes.

Accordingly, a non-profit organization cannot carry out a business or commercial activity (which by definition involves an intention of operating in a manner which generates revenue in excess of expenses) without seriously jeopardizing its tax-exempt status.

Loss of tax-exempt status would mean that, going forward, the housing provider is taxable on all its income, subject to normal deductions and credits for taxable entities. Loss of tax-exempt status may also trigger a deemed disposition and reacquisition of the organization's assets at fair market value immediately prior to the time that the organization ceased to be a non-profit.

As a result of these issues, housing providers which are non-profit organizations should be extremely cautious with respect to commencing commercial activities and should seek legal advice prior to doing so.

If the housing provider determines that the revenue-generating activity that it wishes to conduct may risk the provider's tax exemption, an acceptable solution may be to establish a taxable subsidiary to carry out the business activity, similar to that discussed for registered charities in 2.1 above.

## 2.3 Employee Issues

If a housing provider determines it is able (and wishes) to start a business activity to generate additional revenue, it must also consider:

- whether the business activity will utilize current employees;
- if so, whether the new activity will require changes to the duties of employees or to the nature of the current employees' employment; and
- whether the affected employees are unionized.



If the addition of a business activity to an organization significantly alters or reduces an employee's job title, duties, responsibilities or remuneration, for example by taking away the majority of an employee's former authority, or by reducing an employee's wages, or by adding significant new duties, the employee may have a claim for constructive dismissal.

A successful claim for constructive dismissal allows an employee to quit and sue his/her employer for termination pay and, if applicable, for severance pay as if he or she was terminated without cause. In order to establish a claim for constructive dismissal, an employee must lead evidence that the employment relationship has been fundamentally altered. The chances of a successful constructive dismissal claim will depend on how extreme the change is. While minor changes are likely to be acceptable to a court, significant changes are a source of risk for the housing provider.

If the affected employees are unionized, there may be a provision in the collective agreement that prevent certain changes to an employee's duties or which require consultation before changes are implemented. The housing provider should review any existing collective agreements and consult legal advice before taking any steps that would affect employees.

#### 2.4 **HST Issues**

Charities and many non-profits have special status under the harmonized sales tax ("HST") regime. The creation of a new business or commercial activity may have tax implications related to commodity taxes. This will depend in large measure on what goods and/or services will be provided by the business. The board should determine:

- (a) *whether the goods/services provided by the business are subject to HST*

Certain goods and services are subject to HST, while others are exempt or apply the tax at a rate of 0% (thus effectively making the supplies exempt). Thresholds and other requirements may apply. An organization that provides non-exempt goods or services without collecting and remitting the required tax may be liable to pay that tax, plus penalties. In certain situations, directors may be personally liable for unpaid tax.

- (b) *whether the organization is a HST registrant and will the proposed business require registration and filings as a result?*

Generally, unless the goods and services provided by the business are exempt, the organization will be required to register for, charge, and collect HST on its products or services, and remit the appropriate amounts to the government and make regular filings. The organization may be able to claim rebates or tax credits in some circumstances.

- (c) *change to HST rebate percentage*

Charities and non-profit organizations providing RGI housing may qualify to be designated as municipalities for HST purposes and as such can get a 100% rebate of the federal portion of the HST (5%) as well as a portion of the provincial portion of the HST. Charities and "qualifying" non-profit organizations that are not



designated as municipalities are also entitled to a rebate of HST, albeit at a lower rate.

In order to be considered a "qualifying" non-profit, an organization must receive 40% of its revenues from "government funding". Accordingly, if a non-profit organization replaces its subsidy revenue with other revenue, then this government funding threshold may not be met. More information can be found here: [http://www.fhcc.coop/eng/pdf/ontdocs/HST\\_Paper\\_final.pdf](http://www.fhcc.coop/eng/pdf/ontdocs/HST_Paper_final.pdf).

## 2.5 Use and Regulation of Property

Certain uses and activities on property may be restricted by local government zoning, or require specific permits and licences to conduct. Below are several questions for the board to consider in relation to the proposed business activity.

- (a) *Is the property zoned for the proposed business activity or use of space?*

Permitted land uses are set out in the local government's zoning bylaw. If a proposed business activity or use of space is not permitted in the zoning bylaw, the owner of the property would be required to apply to the local government to amend the zoning bylaw. The local government has the authority to refuse such an amendment, though Ontario does have an appeal process, through the Ontario Municipal Board.

- (b) *Does the proposed business activity require any development permits, building permits, or business licences?*

In addition to zoning, governments regulate land use through site plan control, building permits and, in some cases, business licences. The owner may require all or some such permits, depending on the proposed use and activity.

- (c) *Will the proposed business activity cause the property tax exemption to be revoked?*

In certain municipalities, registered charities can be granted an exemption from property taxes in accordance with the Assessment Act (Ontario) and its regulations. A change in the use of all or a portion of the property could mean that the organization is no longer eligible for property tax relief.

- (d) *Are there any restrictions on activities registered on title of the relevant property?*

Permitted uses and activities may be limited by a restrictive covenant registered on title to the property.

A title search should be conducted to ensure there are no restrictive covenants that would prevent the intended activity.



### 3. **Shared Services Arrangements**

Some housing providers may elect to try to realize economies of scale by sharing certain administrative functions and the associated costs with one or more other organizations. For example, two organizations may share payroll and human resources services.

If a housing provider is considering entering into such an arrangement, there are several legal issues to keep in mind.

#### 3.1 **Contractual Considerations**

Any plan to share administrative services with another organization (whether housing provider or otherwise) will require the organizations to enter into an agreement in writing. The organizations should seek legal advice to ensure that the agreement is binding and enforceable.

The agreement should describe how the parties will share the cost of the services, including the percentage or formula for calculating each party's "fair share" of the total cost.

Many contribution agreements associated with project funding include very strict provisions regarding reporting, and sometimes the portion of funds which may be used for administration. Care must be taken to ensure that a shared administrative services contract does not violate the requirements of any such agreement.

If an organization which is a non-profit is considering contracting out the services of its administrative staff to another organization, it must be careful to ensure that the fee charged is on a cost-recovery basis to avoid the potential loss of its tax exemption as discussed above.

#### 3.2 **Personnel Considerations**

(a) *Who is the employer of the shared service staff?*

Having multiple organizations utilizing an individual(s) for payroll or human resources may create confusion regarding reporting and lines of authority.

It is advised that shared personnel obtain an employment agreement which defines the organization that is his or her "home" employer. The shared services agreement should then clearly define how the services will be divided and how payments will be made between the organizations.

(b) *Is the staff of either organization unionized?*

If the organization's workforce is unionized, a shared services agreement may violate certain contracting out provisions of the Collective Agreement. Further, the transfer of work from the organization to the third party may trigger successorship rights thereby expanding the union's representation to the third party. Check the Collective Agreement before proceeding.



- (c) *Will the shared service agreement result in staff terminations or changing terms of employment?*

Legal advice should be sought.

- (d) *Privacy Considerations*

Privacy rights are governed by the *Personal Information Protection and Electronic Documents Act* (PIPEDA). PIPEDA applies to all commercial activity (such as taking information in course of doing business). PIPEDA applies to employment related information as well, but only where an entity is a federal undertaking. Nevertheless, protecting employees' private information including SINs, etc. in compliance with PIPEDA is a wise course of action. If an organization agrees to a shared services agreement for certain administrative functions that would require the organization to disclose its employees' personal information to a third party, the organization must reach an agreement with the third party providing the services to ensure that its employees' personal information will continue to be protected. In some circumstances, you may need employees' consent to share certain personal information with third parties. Some housing providers, such as Municipal non-profits are subject to the *Municipal Freedom of Information and Protection of Privacy Act*. The rules are similar.

#### 4. **Merger/Amalgamation/Consolidation with another Not for Profit Housing Provider**

A merger, amalgamation or consolidation of two or more housing providers is a significant undertaking. The questions below will assist the Board of a housing provider to identify the relevant issues, but the organization should obtain legal advice before proceeding.

- (a) *What is the governing legislation under which the organization is established?*

A housing provider in Ontario may be incorporated under any one of a number of different statutes, some of which are provincial and others federal. The *Corporations Act* (Ontario), the *Co-operative Corporations Act*, and the *Canada Not-for-Profit Corporations Act* are the most likely. In order for a merger to occur, the corporations must be governed by the same statute. Where corporations are governed by different but similar statutes, there may be processes to continue one of them under the same statute.

All of the assets, liabilities and obligations of the amalgamating corporations become the assets, liabilities and obligations of the amalgamated corporation which could result in unintended consequences. Legal counsel should be sought to identify such risks.

- (b) *Is the organization incorporated under the Corporations Act (Ontario)?*

Many housing providers in Ontario are incorporated pursuant to the *Corporations Act* (Ontario). After an amalgamation agreement has been executed and the amalgamation has been approved by the Board and members of each of the amalgamating corporations, an Application for Letters Patent of Amalgamation is to be filed with the



Companies and Personal Property Security Branch of the Ontario Ministry of Government services along with the following:

- a filing fee of \$155.00;
- a name search report if amalgamated corporation is to have different name of any of the amalgamating corporations; and
- a certified copy of the approved amalgamation agreement.

Once filed with the government, it may take between 6-8 weeks before a Certificate of Letters Patent is issued.

Prior to undertaking an amalgamation, however, a provider should consider its options given the transition requirements to Ontario's *Not-for-Profit Corporations Act, 2010* so that the most cost effective means of completing the transition and amalgamation can be undertaken. There is no reason to engage an organization in two corporate restructurings if one will do.

(c) *Is the Organization a registered charity or a non-profit organization pursuant to the Income Tax Act?*

Different considerations apply depending on whether the organization is a registered charity or non-profit organization, as discussed above.

Whereas the *Canada Corporation Act* does not permit the amalgamation of federally incorporated organization, the *Canada Not-for-profit Corporations Act* explicitly permits two or more corporations governed by that statute to amalgamate. Non-share capital corporations incorporated under the *Corporations Act* (Ontario) are also permitted to amalgamate with one another, provided that approval is given by Ontario's Public Guardian and Trustee. Ontario's *Not-for-Profit Corporations Act, 2010* also explicitly permits the amalgamation of two or more corporations that are governed by that statute.

Registered charities must tread carefully when considering whether to join together and continue operating as one body. The CRA in fact distinguishes between three different mechanisms pursuant to which this can be achieved – an amalgamation, a merger, or a consolidation. Each of these approaches involves a different process and produces different results for the original entities and the resulting entity. The CRA encourages any charity that is considering an amalgamation, merger, or consolidation to submit to the CRA a letter containing the details of the proposed changes for review.

(d) *What are the differences between an amalgamation, a merger, and a consolidation?*

When organization amalgamate, they bring their memberships, assets, and liabilities into a single entity that emerges. The original entities do not cease to exist or dissolve, although they cease to maintain separate identities. The organizations continue to exist as a single entity - the amalgamated organization. The terms of the amalgamation are set out in an amalgamation agreement, and the amalgamated entity is governed by its own Articles or Letters Patent and Bylaws.



A merger between two entities occurs where one winds-up its affairs and transfers all of its assets to the other. The Articles of the organization being wound-up may provide restrictions as to the types of organizations to which its remaining assets can be distributed. Where a merger occurs, there is generally an agreement which sets out the framework whereby the obligations of both parties, and the purposes, membership, governance, and financial matters of the receiving organization are described.

A consolidation occurs where two or more organizations wind-up and transfer their assets to a new entity. The new entity would have to apply for a new business number and, if charitable status is desirable, would have to make a fresh application to the Charities Directorate.

(e) *Are there any contractual obligations that restrict fundamental changes, reorganizations or changes in control?*

Sometimes contracts binding on an organization prohibit or restrict "changes in control", which generally includes a change in control as a result of amalgamation. Funding agreements and leases generally include such provisions. Often the contractual language will allow a change in control, but only with the written consent of the other party to the contract. Before proceeding with an amalgamation, it is important for a housing provider to ensure that it is aware of, and taking the required steps to deal with, any such restrictions or requirements.

(f) *Does an amalgamation/transfer of real property trigger any tax consequences?*

Generally, an amalgamation or merger between two housing providers that are themselves tax-exempt entities should not give rise to any adverse income tax consequences, including in connection with the transfer of real property from one housing provider to the other.

However, it should be noted that since charities are required to apply their assets for exclusively charitable purposes, difficulties may arise if a registered charity and a non-charitable not-profit organization wish to amalgamate or merge with one another; because of this requirement the amalgamated entity would itself be required to obtain charitable status. Similarly, because charities may only transfer their assets to "qualified donees" (e.g. other registered charities) upon dissolution, a charity would not be able to wind-up and merge into a non-profit without charitable status (although the non-profit may be able to wind-up and transfer its assets to the charity).

A transfer of real property may be subject to land transfer tax. While the *Housing Services Act* does contain an exemption to land transfer tax, the applicability of the exemption is limited to transfers from housing providers to the Service Manager, municipality or a municipally controlled non-profit. Property in the City of Toronto may also be subject to municipal land transfer tax.

Additionally, certain transfers of property may be subject to HST and it is recommended that the Board obtain tax advice on this question.

(g) *Is consent required to a corporate reorganization?*



Housing Providers must have regard to the consent requirements contained in Section 166 of the *Housing Services Act*, which provide that certain amalgamations require the consent of the Service Manager. Again, the consent requirements apply differently depending on the program pursuant to which a project was funded. The starting point is to identify the funding program by finding the project Regulation 368/11 and then applying restrictions in Section 166.

## 5. Portfolio Management

### 5.1 Financing

Financing involves the organization incurring debt, which may be secured against property or be unsecured. Most lenders will require security against assets to extend a loan of any significance. Financing transactions can involve a restructuring of current debts, or a reorganization of the organization's structure. In all cases, the documents involved can be lengthy and complex.

- (a) *Does the proposed transaction involve "investing" in a partnership or limited partnership?*

When a charity is a member of a partnership, the CRA views the charity as carrying on business as opposed to making an investment; this is the case even if the charity plays no active role in the business of the partnership. Therefore, where a charity is a limited partner of a partnership, consideration must be given as to whether the activities carried on by the partnership constitute a related business (see discussion above).

Because a partnership is legally defined as a relation that subsists between persons carrying on business in common with a view to profit, it is quite clear that a not-for-profit entity cannot enter into such an arrangement without putting its status as a tax-exempt entity in serious jeopardy.

- (b) *Is the organization governed by the Housing Services Act?*

Many Ontario housing providers are subject to the consent obligations contained in section 161 and 162 of the *Housing Services Act*. Pursuant to this section, a housing provider, to whom the Act applies, may not mortgage a property absent the consent of its Service Manager or transfer a property without the consent of the Minister of Housing. Any provider will, have to satisfy its lender that either no consent is requested, or, if required, has been obtained.

### 5.2 Redevelopment

- (a) *Do the Restrictions in the Housing Services Act apply?*

Where a sale of a portion of the land is to be sold as part of the redevelopment land, consent of the Minister of Municipal Affairs may be required in accordance with Sections 161 and 162 of the Act. The nature of the consent will depend on the program pursuant to which the housing was funded, and should be carried out on a case by case basis.





(b) *How will the redevelopment affect existing tenants?*

A landlord may issue a Notice of Termination to tenants on the grounds that it is going to undertake the demolition of the building, conversion to non-residential properties, or undertake a major renovation that requires vacant possession of the units. The date of termination must be at least 120 days after the notice is given and must fall on the last day of a rental period or, if the tenancy is for a fixed term, the last day of the fixed term. Similarly, if a landlord intends to redevelop a building to convert rental units into non-residential use, it may validly terminate any existing fixed term tenancies

However, as a general rule, all terminated tenants will be entitled to three month's rent as compensation or offered another unit that is similar.

In addition, many municipalities will require a formal Rental Replacement and/ or Tenant Relocation Plan which may provide for replacement of any lost units in the same area, and in some cases for the provision of accommodation for displaced tenants.

(c) *Will redevelopment affect the tax-exempt status of the organization?*

A housing organization's tax exempt status, whether as a non-profit organization or a registered charity, depends on it being devoted to providing housing to low-income or marginalized persons on a non-profit basis.

If the redevelopment increases the amount of commercial or market space at the expense of non-profit housing units, this may not be in keeping with the organization's purposes, and may also have implications for the organization's tax exemption as either a registered charity or a non-profit organization.

(d) *Is the property zoned for the proposed redevelopment?*

Redevelopment may be restricted or otherwise require approval by local government through zoning, permits and licences. These should be investigated before a decision is made.

Permitted land uses are set out in a local government's zoning bylaw. If a proposed redevelopment is not permitted in the zoning bylaw, the owner would need to apply to the local government to amend the zoning bylaw. The local government has the authority to refuse or accept such an amendment. An appeal of the municipalities action (or non-action) is available to the Ontario Municipal Board.

(e) *Does the proposed redevelopment require any development permits or building permits?*

In addition to zoning, local governments regulate land use by requiring site plan agreements and building permits. The organization may require some such permits, depending on the nature of the proposed redevelopment.



- (f) *Are there any restrictions on activities registered on title of the relevant property?*

Redevelopment may be limited by a restrictive covenant registered on title to the property. A title search must be conducted to ensure there are no restrictive covenants that would prevent the proposed redevelopment.

### 5.3 **Other property considerations**

Any property subject to a potential redevelopment should be thoroughly reviewed. Depending on the type of redeveloped property and its location, several other considerations may apply, including:

1. *Subdivision of land.* In Ontario, an owner cannot sell land and retain adjoining land. To do so, requires consent of the local municipality either through the committee of adjustments or a formal subdivision agreement. A Housing Provider selling a piece of its land would, for example, require the consent of the committee of adjustment to do so.
2. *Environmental contamination.* In a redevelopment, this may be both subsurface contamination and contamination located in building materials such as asbestos or lead based paint. Note that some Housing Providers which received former public housing, may have recourse to the Province of Ontario for the cost of remediation.
3. *Encroachments.* Any encroachments onto the land to be redeveloped will have to be considered.
4. *Flood and hazard mitigation.* Land located in a flood plain, or beside a railway, for example, may be subject to additional restrictions.
5. *Construction.* Construction entails its own risks. In Ontario, absent the right structure, the owner and its directors could be held responsible for site safety under the Occupational Health and Safety Act.

A Redevelopment can be among the most dramatic and rewarding strategies to undertake. However, it is also the most complex. It should be approached with a group of advisors in place to assist the Housing Provider. These advisors should include legal, development consulting and insurance, at a minimum. The team will ultimately grow to include other disciplines such as architecture etc.

### 5.4 **Sale of Portfolio Assets**

There are a number of important legal considerations involved in selling one of the housing provider's properties.

#### **Initial Considerations**

- (a) *Is the legal and beneficial title to the property held by the organization?*

Private property developers often take title in the name of a trustee while retaining beneficial title separately. A title search through the Land Registry



Office will confirm the legal title to the property. Beneficial title means the right to use, or direct the use, of the property notwithstanding that the beneficial title holder is not registered as an owner of the property in the Land Registry Office.

This is a relatively rare occurrence for non-profit housing providers in Ontario who generally have both legal and beneficial title. Nevertheless, if there is a trust with respect to the property, then additional documentation will be required to convey the property.

(b) *Does the Housing Provider retain abutting land?*

For the reasons described above, a consent will be required if a Housing Provider is selling a part of its land.

### Restrictions on Sale and Mortgage

(a) *Is consent required under the Housing Services Act?*

Some housing providers will require the consent of the Minister of Municipal Affairs and Housing to the sale of a housing asset pursuant to Sections 161 and 162 of the *Housing Services Act*. This depends of the nature of the funding program under which the project was developed. This must be reviewed on a case by case basis.

(b) *Are there any existing contractual obligations that would prevent the sale of the property?*

The Board should review all relevant agreements, including funding agreements, to determine if sale of the property would violate any contractual obligations.

(c) *Do the organization's Articles/ Letters Patent or Bylaws restrict the disposition of property, or require approval by members or third parties?*

The Board should review the organization's Articles or Letters Patent, and Bylaws to determine if there are any restrictions on selling property or assets.

(d) *Are there any restrictive covenants registered on title to the property?*

Sale of subsidized units may be limited by a restrictive covenant or an option to purchase the units registered on title to the property.

(e) *Does the sale involve the conversion rental units to condominium units?*

If the sale entails conversion of rental units to condo units, the lost rental units will likely need to be replaced.

### Contractual Issues

Any sale of property requires a contract of purchase and sale with the prospective buyer. These contracts deal with a wide variety of complex issues. The Board should seek legal advice. Generally, sale of property will require the



discharge of the current mortgage, if any.

### Tenant Issues

(a) *Will a sale involve terminating existing tenancies?*

A fixed term tenancy may not be terminated on the basis that the rental unit is being sold to a purchaser unless the purchaser is an individual who intends, or has a family member who intends, to occupy the rental unit.

A fixed term tenancy must be honoured by a purchaser and thus, upon sale of a building with multiple fixed term tenancies, the tenants' consent (Form N11 - Agreement to Terminate a Tenancy) will likely be necessary in order to terminate such tenancies.

(b) *Are there records of tenancy or a tenancy agreement?*

Dealing with tenancy issues is made much easier where there is a clear tenancy agreement between the tenant and landlord. Where the tenancy agreement, or other records related to the tenancy, have been lost, it is difficult to enforce provisions other than those in the RTA, since there is no evidence of any specific agreement between the parties.

(c) *Are there commercial tenancies?*

Commercial tenancies are often retained in a sale transaction as the purchaser wishes to benefit from the rental stream. A purchaser will want confirmation from the tenant that it is not in default and the Lease is in good standing.

### Tax Issues

(a) *Does the vendor need to charge HST on the sale?*

The sale of real property to a purchaser may be subject to HST, payable by the purchaser to the vendor, who must then remit payment to the government. However, in many cases the purchaser will self-assess the HST.

(b) *Will Land Transfer Tax apply to the sale?*

The purchaser of real property will be required to pay land transfer tax, unless one of the previously described exemptions apply.



**ACKNOWLEDGEMENT**

This Memorandum is based on work originally produced by Bull, Housser & Tupper LLP for use in British Columbia. Providers from British Columbia should have reference to their memorandum.

**ROBINS APPLEBY LLP**

Robins is available to assist service managers and providers exploring these strategies. Please call John Fox at 416-360-3349.

JF: ms

[robapp\2997245.5](#)