



**WELLESLEY INSTITUTE**  
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Policy Brief

## A policy perspective on Canada's non-profit maze of regulatory and legislative barriers

Mapping the way forward for third sector organizations

Lynn Eakin, Heather Graham, Rick Blickstead, and Michael Shapcott

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## **A vital sector tangled in a financial and regulatory maze**

Canada's third sector – the vital web of non-profit, charitable and voluntary organizations that provide programs and services, and knit together communities – is also a significant economic force. In recent years, governments have increasingly relied on non-profit groups as the delivery agent of choice for government services. "Canada's non-profit maze" is powerful new research by Lynn Eakin and Associates, commissioned by the Wellesley Institute that provides a troubling picture of the financial and regulatory burdens facing the third sector. This policy brief builds on the key findings, and maps a way forward towards a strong and healthy non-profit sector.

One of the key characteristics of the third sector is its dedication to its work and its pragmatic approach to working around the obstacles it faces in pursuing its mission. For many years, this approach worked, and the non-profit and charitable sector grew and thrived. In the past fifteen years, however, the rate of change has accelerated and, with it, the complexity of the obstacles it faces because Canada's legislation and regulation of the sector has not kept pace.

The inadequacies our Canadian legislative and regulatory regime have become even more frustrating as we have watched other countries (Great Britain, United States, New Zealand and, most recently, Australia) embark on significant modernization of their charitable and non-profit frameworks. Canada is lagging behind, and that is not only bad for the third sector, but it is also a drag on our economy. It hinders our communities and affects many millions of individual Canadians who rely on third sector organizations for basic programs and services.

There are some positive developments in Canada. Newfoundland and Labrador has a cabinet minister responsible for the third sector. The City of Toronto has completed a co-operative review, with community-services organizations, of municipal funding and programs. In April, the Ontario government amended its draft anti-poverty legislation (following the advice of the Wellesley Institute) to recognize the critical importance of the third sector both in providing practical help to people suffering from poverty, and also in developing innovative plans to lift people out of poverty. However, these initiatives are not coordinated, the patchwork remains frayed, and the third sector continues to suffer as the recession impacts more Canadians.

## **Revenue sources are shifting**

Increasingly, non-profit and charitable organizations use three sources of revenue to support their work - government funding, earned income, and charitable donations. Of these three sources of income, the trends (1994-2004) showed that earned income is increasing and charitable donations and government funding is declining as a percentage of revenue for the core non-profit sector providing public benefit. We have every reason to believe this trend has continued between 2004 and 2008 and, with the economic crisis in 2009, the decline in government funding and charitable donations to the core non-profit sector is expected to accelerate. While this shift has been underway for quite some time, it is only recently we have come to understand the implications for the sector. Regulators, funders and even the sector have not yet adapted to the new reality.

## Currently there is no way out of the regulatory maze

*21<sup>st</sup> century non-profits are saddled with 20<sup>th</sup>, and even 19<sup>th</sup> century, legislation and regulations.*

The regulatory and legislative environment for charities wasn't designed to allow charities to raise revenues from earned income except in very limited situations. Moreover, the requirement that all activities be charitable, and the definition of what activities are charitable present serious problems for both the regulator and the charities. Canada Revenue Agency (CRA) has the regulatory challenge of making modern charitable organizations fit a notion of charity that no longer exists. And the sector, very adept at working around obstacles, increasingly finds there is no way to maneuver around the barriers to revenue generation and comply with charitable regulations. As their charitable revenue declines or stagnates, regulations prevent them from developing other sources of income.

*Non-profit corporations who do not have charitable status are left out and left behind.*

Non-profit organizations providing public benefit that are without charitable status are constrained by not being able to receive grants or social investment from charitable foundations. But neither are they eligible for the many grants and subsidies offered to for-profit business by government. In addition, current legislation and regulation does not support non-profit corporations to have access to the financing and capital tools available to for-profit business. Non-profit corporations without charitable status exist in a state of limbo, they are not charities and they are not for-profit corporations yet in Ontario they are not encouraged or supported as social enterprises dedicated to the public good.

*Declining government funding comes with stifling administration.*

Government funding of the sector continues to fall short of delivery costs and, in addition, no significant changes have been made to improve the administrative requirements for its grants and service contract agreements. Indeed, in several areas, administrative requirements, such as the new international audit requirements, may actually prevent international charities from undertaking their work abroad. It seems that no matter how non-profit organizations operate, as charities, or as non-profits, the legislation and regulation of the sector frustrates their ability to effectively conduct their work for the public good.

*The third sector is starting to take action...*

The sector, with its limited capacity, is beginning to organize. There is considerable energy devoted to establishing legislation and financing to support **social enterprise** and **social purpose business**. This flurry of activity is new for the sector and is very exciting. However, other revenue streams – *charitable gifts* and *government funding* – do not have the same momentum for reform. The sector scan of who is doing what in this area (attached as appendix two to the main research report) has identified some newly active groups that are beginning to get involved in regulatory issues. SIG National, SIG@MaRS, Causeway, and the Ontario Non-profit Network are all relative newcomers to the sector. They join other more established groups that have been focusing on the changes needed to enable the sector undertake its work. The Muttart Foundation, Imagine Canada, and Community Foundations of Canada all have initiatives underway.

*"Making do" is no longer making it for non-profits.*

The non-profit sector has a long tradition of “making do,” of finding a way around obstacles, but “making do” is no longer working for increasing numbers of charitable and non-profit organizations. We need to make change and we need government with us.

*Governments and politicians in Canada take the third sector for granted.*

As encouraging as it is to see some early calls for regulatory and legislative reform from the non-profit sector, how far can we get without government involvement? The striking gap uncovered in this scan is the absence of serious government engagement with the sector in the reform process. As large funders of the sector and as regulators, all three levels of government have many reasons to work with the sector to develop enabling operating conditions. The result is the **non-profit maze**: An impenetrable maze of legislation and regulation that is stopping non-profits and charities in their tracks.

## Mapping the way forward

This study is just a beginning, a starting point for a larger engagement of the third sector, government, and the legal community on the size, scope, and priorities for legislative and regulatory reform. The ability of charities and non-profit organizations to respond to changing circumstances and adapt to new demands is seriously impeded by outdated regulation and legislation. These constraints on the sector’s ability to adapt are about to become even more critical as the economy worsens, their revenues decline and the sector’s contributions are more necessary than ever. Here is a four-point plan for moving forward:

1. **Create political / policy responsibility for the third sector.** While many branches of government have a “piece” of the non-profit pie, there is no central responsibility. Federal and provincial governments need cabinet-level positions with responsibility for the third sector. Once the position is created, departmental and funding initiatives need to be aligned.
2. **Create multi-stakeholder initiatives to review and reform the regulatory and financial maze** facing the third sector at all levels. Governments in Canada needs to join other countries that have already moved into the 21<sup>st</sup> century with more efficient administrative structures that support third sector groups, rather than entangle them in endless red tape.
3. Within the third sector, **create cross-sectoral initiatives that effectively harness and leverage the growing number of initiatives for practical reform.** Share research and policy analysis, along with good practices from Canada and abroad, to move forward.
4. As the recession continues to bite deeper, **government stimulus initiatives need to take special account of the unique challenges and needs of the third sector.** Building a strong and healthy social infrastructure is every bit as important as roads and bridges.

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Visit us online at [www.wellesleyinstitute.com](http://www.wellesleyinstitute.com)

45 Charles St. East, Suite 101

Toronto, ON, Canada M4Y 1S2

Tel 416 972 1010

[www.wellesleyinstitute.com](http://www.wellesleyinstitute.com)