

## BRIEFING MEMORANDUM

### LEGAL CONSIDERATIONS AND THE EXPIRY OF OPERATING AGREEMENTS

**May 2016**

In British Columbia, and generally in other provinces of Canada, non-profit housing societies are faced with the expiry of their operating agreements with either the provincial or federal governments, or both. Such operating agreements generally include a subsidy tied to the amortization period of the mortgage. Once the mortgage no longer exists, the subsidy is withdrawn and the individual housing societies are then solely responsible for the ongoing financial sustainability of their housing project. Planning for the withdrawal of the subsidy and potentially a new model for the financial sustainability of a project requires the consideration of a number of legal issues which are described in this Briefing Memorandum.

#### **INTRODUCTION**

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. There is no one-size-fits-all solution. Before making any changes to the organization or its operations, the Board and management must carefully consider which of the potential strategies are viable and appropriate given the organization's unique circumstances. Some strategies may be suitable for one organization, but completely unworkable for another.

In considering the strategies, directors must remember that they each owe fiduciary duties to the organization. This means that each director must act honestly, in good faith and in the best interests of the organization as a whole. 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 organization.

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

In addition to the operational issues which may arise, each of the strategies described below bring a variety of potential legal and tax issues. 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.

A summary of the legal issues is set out below. First are listed 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 Board might ask itself to determine whether an issue applies in its case, followed by an short description of the legal issues that result.

***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 should be obtained before taking any steps to implement one or more of the proposed strategies.***

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

The following are governance and corporate matters of general application to all strategies to be considered.

### **1. 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 (<http://www.cra-arc.gc.ca/chrts-gvng/lstngs/menu-eng.html>) to confirm whether it is a registered charity.

If it is not a registered charity, a housing provider is likely a tax-exempt non-profit organization. There is no database to confirm this status but the housing provider can check its past tax returns to confirm whether it has been claiming this 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 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.

## **2. Compliance with Constitution/Articles**

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 Constitution (in some cases called the ~~%Articles+or %Letters Patent+~~) of the organization.

Every housing provider will have a Constitution which sets out its name, purposes and other fundamental matters. Some housing providers may be very familiar with their Constitution and will have kept it up to date over the years. Others may be unaware of this important document.

Regardless of whether an organization is a registered charity or a non-profit organization, it is only permitted to undertake activities (and expend funds) that advance the purposes stated in its Constitution. Activities or programs which are not within its purposes are prohibited. It is crucial therefore that the purposes set out in a housing provider's Constitution accurately reflect what the organization is actually doing and are broad enough to encompass the strategies described below that it might decide to undertake.

If necessary, a housing provider can amend its purposes to reflect its activities and objectives. In most cases, amendment of the Constitution 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 membersqmeeting 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.

### **3. Compliance with Bylaws**

In addition to its Constitution, every housing provider has Bylaws that set out its governance framework. Like the Constitution, 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 or the ability of its Board to make certain decisions in a way which would affect one of the proposed strategies. The Board would need to be aware of such issue before taking action. It is recommended that housing providers confirm whether any such restriction exists in their Bylaws, and obtain legal advice if in any doubt.

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

Each of the proposed strategies is listed in the following pages, along with a series of questions to help identify potential issues and 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 are regulated by the *Residential Tenancy Act* (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 rent in the first 12 months of a tenant entering a tenancy agreement, and cannot increase rent more than once every 12 months. Any rent increase is limited to 2% of the current rent, plus inflation. In addition to such restrictions, the RTA also requires a landlord to provide the affected tenant with at least 3 months' notice before the effective date of any rent 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. This is a long term strategy.

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

In contrast to market units, increasing rent for RGI units is not governed by the RTA. Section 2 of the *Residential Tenancy Regulation*, BC Reg 477/2003 provides that the RTA does not apply in relation to rent increases and assignment and subletting where the rent of the units is related to a tenant's income. In practice increasing rent of RGI units beyond a certain threshold will have implications for eligibility for government grants and subsidies, since the units may no longer qualify as RGI units.

If the effect of the RGI rent increase effectively to make the RGI units inaccessible to those with low income, raising rents of RGI units above a certain threshold could have consequences for the organization's tax-exempt status and could also be in breach of the purposes set out in the housing provider's Constitution. For example, a housing provider that is a registered charity is required to conduct exclusively charitable activities. Providing low income housing is charitable; providing market housing is not. A housing provider that is a tax exempt non-profit cannot conduct any activities intended to generate a profit. If market rent is charged on certain units, the implication is that the non-profit organization intends to earn a profit on the rental of such units.

A housing provider must provide the same notice of any rent increase for an RGI unit as is required for a market unit (i.e. at least three months).

### **1.3 Reducing Percentage of RGI units**

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

As noted above, 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 guidelines but our experience has been that for registered charities at least 90% of the units need to be provided to low income tenants.

The CRA indicates that a registered charity must establish low income eligibility criteria and 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, other than at turnover, entails terminating the current tenancy. With the exception of fixed tenancies where the term has come to an end, 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.

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

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

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”**

Subject to the concerns described in 1.3(a) about maintaining tax exempt status, and the concerns in 1.3(c) about restrictive covenants and housing agreements, a housing provider can take tenants with higher income at turnover of fixed tenancies.

The housing provider will need to consider whether with the higher rent the unit still qualifies as an RGI unit since at some income threshold, tenants no longer qualify for RGI subsidy. In addition, the housing provider must keep in mind that if it eliminates or reduces its low income or RGI units, it may be jeopardizing its tax-exempt status by

adjusting the ratio of market to RGI units past the acceptable limit for a non-profit/charitable organization.

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 its charitable purposes. It would not be possible, for example, for a salmon 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 its charitable purpose of conserving salmon. 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 nature and extent of the commercial activities allowed are regulated by the related business rules in the *Income Tax Act* and the administrative policies of the Canada Revenue Agency. Below is an outline of the applicable test to determine whether a proposed activity of a registered charity falls within the related business rules.

- (a) *Is the proposed business activity related to the housing provider's charitable purposes?*

If yes, go to (b). If no, is it feasible to amend purposes and maintain charitable registration? If not, the housing provider cannot conduct the business activity.

- (b) *Will the business activity be operated predominantly by volunteers (90% or more)?*



If yes, it can be carried out within the charity. If no, go to (c).

- (c) *Will the business activity be linked and subordinate to the organization's charitable purposes? See the CRA's policy on related business for further detail on whether a business activity is linked and subordinate.*  
<http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cps/cps-019-eng.html>

If yes, then the business activity can likely be conducted within the charity. If no, then 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 potentially 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, the usual 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 care to ensure that the requirements of the *Income Tax Act* are 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 ability of a non-profit organization to operate a business or commercial activity, including a social enterprise, is very limited. 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 accidental and unanticipated. 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 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 of the organization's capital assets which could result in a substantial amount of tax owing.

As a result of these issues, housing providers which are non-profit organizations should be extremely cautious with respect to commencing commercial or social enterprise+ 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, the usual solution is to create 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 their employer for severance as if he or she were 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 requires 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 GST Issues**

The creation of a new business or commercial activity may have tax implications related to commodity taxes, such as GST and PST. 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 GST/PST*

The GST and PST regimes are separate and each is complicated. Certain goods and services are subject to tax, others are exempt or partially 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 GST 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 GST and PST, charge and collect GST and/or PST on its product, 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 GST rebate percentage*

Non-profit organizations providing RGI housing qualify to apply to be designated as municipalities for GST purposes and as such get a 100% GST rebate. For other non-profit organizations to qualify, they must receive 40% of their revenues from government funding and the rebate percentage is lower. If a non-profit

organization replaces its subsidy revenue with other revenue, then the government funding threshold may not be met. More information can be found here: [https://www.bchousing.org/resources/Partner\\_Resources/Finance/GST\\_Guide.pdf](https://www.bchousing.org/resources/Partner_Resources/Finance/GST_Guide.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 licenses 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.

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

In addition to zoning, local governments regulate land use by requiring development permits, building permits and business licenses. 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. 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

- (e) *Does the kind of business activity require provincial licensing, consents or certifications?*

Some uses . for example, child care facilities . may require provincial licensing and compliance with applicable provincial regulations.

### **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 or transfer agreements include very strict provisions regarding the portion of the funding provided 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.

Shared personnel must have 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*

As an employer, an organization has obligations under the *Personal Information Protection Act* to protect its employees' private information including SINs, etc. 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.

#### **4. Merger/Amalgamation 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 BC may be incorporated under any one of a number of different statutes, some of which are provincial and others federal. The *Society Act*, *Co-operative Associations Act*, and the *Canada Not-for-Profit Corporations Act* are the most likely. Depending on the governing legislation, different rules

and concepts may apply to a merger or amalgamation with another housing provider. The Board must be sure which statute applies to the organization (and the organization with which it will merge) and should obtain legal advice regarding the requirements of the applicable statute and the process to amalgamate. In British Columbia at the present time it is not technically possible to merge (in the legal sense) organizations incorporated under two different statutes and an asset transfer agreement would need to be utilized as further discussed below.

*(b) Is the organization incorporated under BC's Society Act?*

Many housing providers in BC are incorporated as societies pursuant to the *Society Act*. The provisions in the *Society Act* related to amalgamation are legally problematic. They can create unanticipated problems for societies which formally amalgamate. These issues are more problematic for registered charities, which are required to re-register with Canada Revenue Agency, which application typically requires 3 - 6+ months for processing.

Instead, societies that wish to merge (registered charities in particular) typically do so indirectly, by:

- entering into an asset transfer agreement between the participating organizations;
- restructuring one of the organizations to include the purposes, membership and governance of both;
- transferring the assets and liabilities (including contracts) from one organization to the restructured organization;
- rationalizing the personnel of the two organizations; and
- dissolving the transferring organization.

We note however that the *Society Act* will be replaced by the *Societies Act* effective November 28, 2016. The new Act fixes the technical problem regarding amalgamations in the *Society Act* and we therefore anticipate that after the new Act is in force societies will amalgamate rather than using the asset and liability transfer procedure outlined above.

*(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.

A registered charity can only amalgamate with or transfer assets to another registered charity. Also, dissolution of a registered charity (in the event of a merger by asset transfer and dissolution) entails additional filing obligations with the CRA for the voluntary revocation of charitable registration.

*(d) How will the amalgamated/remaining organization structure itself?*

Organizations that wish to amalgamate must first enter an amalgamation agreement that sets out the operational, financial and governance framework for the new organization that will be created by amalgamation. The amalgamated organization will require its own Constitution/Articles and Bylaws.

Where a merger occurs indirectly, 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.

*(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 the amalgamation/transfer of real property trigger any tax consequences?*

Generally, formal amalgamation between two housing providers will be exempt from capital gains tax. Likewise, a transfer of property, including real property from one housing provider to another as part of a merger should be exempt from capital gains, so long as both parties are registered charities or non-profit organizations.

However, a transfer of real property in an asset transfer situation (as opposed to a formal amalgamation) will be subject to property transfer tax, unless the



transfer is made to an incorporated registered charity, or falls within another exemption in the *Property Transfer Tax Act*.

Certain transfers of property may be subject to GST/PST and it is recommended that the Board obtain tax advice on this question.

## 5. **Portfolio Management**

### 5.1 ***Financing***

Financing involves the organization incurring debt, which may be secured against property or unsecured. Most lenders will require security 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?*

Charities and non-profit organizations are not able to invest in partnerships, even as a limited partner. If any financial transaction involving a limited partnership is presented, seek legal advice.

(b) *Is the organization incorporated under the BC Society Act?*

A housing provider that is a BC society cannot enter in secured financing arrangements (where the lender takes security for the loan/financing) without the prior approval of its members by special resolution. A special resolution must be passed by 75% of votes cast at a duly called meeting of the members of the organization.

Please note that this requirement has been removed in the new *Societies Act* effective November 28, 2016.

### 5.2 ***Redevelopment***

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

A landlord may issue a Notice to End Tenancy to fixed term tenants on the grounds that it is going to undertake the demolition of the building or undertake a major renovation that requires vacant possession of the units. 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 one month's rent as compensation.

*(b) 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.

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

Redevelopment may be restricted or otherwise require approval by local government through zoning, permits and licenses. 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.

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

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

*(e) 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***

Depending on the type of redeveloped property and its location, several other considerations may apply:

- Subdivision of land
- Environmental contamination and remediation
- Encroachment on a watercourse
- Flood and hazard mitigation

### 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?*

The housing provider cannot sell a property for which it does not hold both legal and beneficial title. A title search through the office of the Registrar of Land Title will confirm the legal title to the property and suggest whether there are any other parties that may hold beneficial title. 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 Title Office.

If there is a trust with respect to the property (whether or not the trust is registered against title), then it is likely that the organization will be unable to unilaterally sell the property, as it does not hold the beneficial interest.

#### *Restrictions on Sale*

- (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 Constitution or Bylaws restrict the disposition of property, or require approval by members or third parties?*

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

Under the new *Societies Act* (in force November 28, 2016) any society disposing of virtually all its assets (technically its ~~undertaking~~) is obligated to obtain a special resolution of its members prior to so doing.

(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 strata units?*

If the sale entails conversion of rental units to strata units, the building may require an upgrade and an approval from the local approving officer.

#### 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 a property will require the discharge of the current mortgage, if any.

#### Tenant Issues

(f) *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.

Where a sale of a building with multiple fixed term tenancies is contemplated, it is likely that a landlord will need to obtain the consent of the tenants if it wishes to terminate any fixed term tenancies.

(g) *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.



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*Tax Issues*

The sale of real property to a purchaser may be subject to GST/PST, payable by the purchaser to the vendor, who must then remit payment to the government.

The Purchaser of real property will incur Property Transfer Tax, unless the organization is an incorporated registered charity.