





We make the world of
charitable organizations

Charity Law Information Program (CLIP) Charity Checklist: Managing Legal Compliance Risks

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Introduction

- Legal information not legal advice
- Views expressed are our own
- Questions during and at end
- Review of handouts –T3010 report, case study, CLIP audit tool, evaluation form
- Logistics and timing



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Who We Are – Capacity Builders


- **The Charity Law Information Program (CLIP) provides training, workshops, and webinars to charitable organizations to enhance their understanding of their obligations under the *Income Tax Act* as well as improve governance and ethics**
- Capacity Builders is a division of the Ontario Community Support Association (OCSA) and it runs CLIP
- <http://www.capacitybuilders.ca/clip>
- CLIP Communiqué – sign up for free
- (416) 256 – 3010 x 232 or 1-877-484-3030
- clip@capacitybuilders.ca

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Who We Are – Blumbergs

- Blumberg Segal LLP is a law firm based in Toronto, Ontario
- Mark Blumberg is a partner at Blumbergs who focuses on non-profit and charity law
- Assists charities from across Canada with Canadian and international operations and foreign charities fundraising here
- www.canadiancharitylaw.ca and www.globalphilanthropy.ca
- Free Canadian Charity Law Newsletter. Sign up at: <http://www.canadiancharitylaw.ca/index.php/pages/subscribe>
- (416) 361 – 1982 or 1-866-961-1982
- mark@blumbergs.ca





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Charities Directorate of CRA

- Regulates registered charities
- Based in Ottawa and other offices throughout Canada
- Website: www.cra.gc.ca/charities
- E-mail list: www.cra-arc.gc.ca/esrvc-srvce/mlist/sbscrbchrts-eng.html
- Webinars: www.cra-arc.gc.ca/tx/cmmnctn/sssns/wbnrs-eng.html
- Telephone: 1-800-267-2384 (English)
1-888-892-5667 (Bilingual)
- Provided funding for the Capacity Builders' Charity Law Information Program (CLIP)



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Charity Law Basics

- Registered charities are regulated by Charities Directorate of the Canada Revenue Agency (CRA)
- Registered charities fall under both federal and provincial jurisdiction
- Non-profits and charities are both tax exempt
- *Income Tax Act* – concept of “registered charity” can issue “official donation receipt” with income tax savings for donor
- Benefits and restrictions on registered charities
- Doing good and charity are not synonymous



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Maintaining Charitable Status



- Conduct allowable charitable activities and avoid prohibited activities
- Keep adequate books and records
- Properly issue official donation receipts
- Meet annual spending requirement (disbursement quota)
- File T3010 Registered Charity Information Return
- Maintain status as a legal entity
- Inform CRA of certain changes

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Top Legal Compliance Concerns for Canadian Registered Charities



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1. Failure to File T3010

- Canadian Registered Charities must file their T3010 Registered Charity Information Return every year
- Within six months of the end of the charity's fiscal period
- For 2009 fiscal years file T3010B
- Form is mailed with labels to charity – also can download form from:
<http://www.cra-arc.gc.ca/tx/chrts/prtng/rtrn/flngb-eng.html>



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Why File T3010?

- Legally required
- Only uniform way to compare Canadian charities
- Advertisement for charity
- Important for transparency of charity
- Only beginning of transparency (website, annual report, newsletters, e-mail lists, etc.)



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Consequences for Failing to File

- Revocation of charitable status within months
- Cannot issue receipts
- Lose benefits of registered status
- Revocation tax if not re-registered within 1 year
- May not be able to reregister
- \$500 penalty



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Questions for Follow-Up

- Have you checked on the CRA website that you are a charity?
- When is your fiscal year end?
- When is 6 months from your fiscal year end?
- Have you diarized the date immediately above?
- Who is responsible for filing the T3010?
- Are you aware how the T3010A and T3010B are different?
- Have you filed your T3010 on time?
- Is your address with CRA up to date?



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2. Mistakes with T3010B

- T3010 must be the correct form, accurate and complete including schedules and financial statements otherwise may be returned or considered incomplete
- Lots of help on internet with T3010B – go to www.capacitybuilders.ca/clip for a list including our Annotated T3010B
- CRA has fillable T3010B



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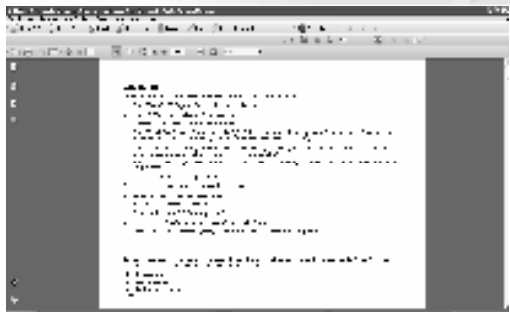
Problems with T3010B

- Using wrong form – T3010A for 2008
– T3010B for 2009 and later
- Not providing all information
- Not providing accurate information
- Not providing all schedules
- Not providing financial statements
- Not providing date of birth of directors



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Form T3010B





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Questions for Follow-Up

- Have you completed all required information?
- Have you checked CRA checklist for documents?
- Have you had lawyer/accountant/your board check T3010?
- For bigger organizations have you checked a few months after filing that CRA has inputted your T3010 information correctly?



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3. Incorrect Receipts

- Charities are required to issue correct receipts
- Some receipts:
 - Lack required information
 - Have mistakes
 - Include improper fair market value (FMV)

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What is a “Gift”

Charities can only issue receipts for a gift.

A gift must be:

1. **Voluntary** – given of free will (not compelled)
2. **Transferred** – from donor to charity/qualified donee
3. **Property** – cash or gifts in kinds (not services)
4. **Financial Sacrifice** on the part of the donor (donative intent – advantage must be less than 80% of amount unless Minister agrees)



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Don't Issue a Receipt When...

- You cannot determine the value of the donation or the benefit
- Donation of services to charity
- Donation is intended for another organization that is not a registered charity
- Cannot determine the name of the true donor
- Payment for event (concert)
- Payment for program (daycare)
- Tuition (except IC 75-23 - private religious schools)
- Business advertising expenses

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Mandatory Elements of Receipts

For gifts of cash: (Regulation 3501 of the *Income Tax Act*)

- A statement that it is an official receipt for income tax purposes;
- The name and address of the charity as on file with the CRA;
- The charity's registration number;
- The serial number of the receipt;
- The place or locality where the receipt was issued;
- The day or year the donation was received;



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Mandatory Elements of Receipts (cont.)

- The day on which the receipt was issued if it differs from the day of donation;
- The full name and address of the donor;
- The amount of the gift;
- The value and description of any advantage received by the donor (under proposed legislation);
- The signature of an individual authorized by the charity to acknowledge donations; and
- The name and Web site address of the Canadian Revenue Agency (www.cra.gc.ca/charities)

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Mandatory Elements for Gifts in Kind


For non-cash gifts (gifts in kind), these additional elements:

- The day on which the donation was received (if not already indicated);
- A brief description of the property transferred to the charity;
- The name and address of the appraiser (if property was appraised); and
- In place of the amount of the gift mentioned above, the deemed fair market value of the property (under proposed legislation).



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Sample Official Donation Receipts



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Split Receipting

- New legislative idea – from 2002
- Pre-2002 – if donor received any advantage, then no receipt
- Now donors can receive some advantage eg. concerts, golf tournament, gala dinners, etc.
- Charity must determine the eligible amount of that gift for receipting purposes in order to issue an official donation receipt
- <http://www.cra-arc.qc.ca/E/pub/tp/itnews-26/itnews-26-e.pdf>

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Consequences for Improper Receipts

- Incomplete or incorrect information: Penalty equal to 5% of the eligible amount stated on the receipt. Penalty increases to 10% for a repeat infraction within 5 years.
- If no gift or deliberately false information then charity is liable to a penalty equal to 125% of the eligible amount stated on the receipt where the total penalty does not exceed \$25,000
- When penalty over \$25,000 the charity gets penalty equal to 125% and the suspension of tax-receiving privileges.
- Can also have registration revoked.

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Questions for Follow-Up

- Are you only providing receipts when appropriate?
- Are you only providing receipts for donations to your organization (not acting as a conduit or lending registration)?
- Have you checked that all mandatory fields are included on receipts?

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4. Acting Outside Legal Objects

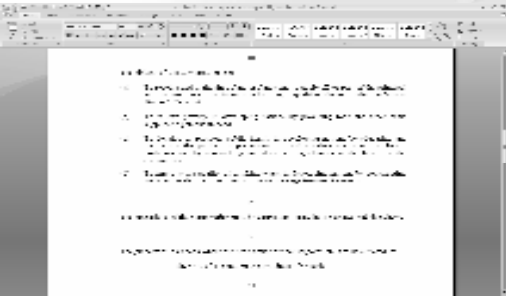
Most incorporated charities in Canada have legal objects in their Letters Patent (Articles of Incorporation).

Charities must not act outside of these legal objects.



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Check Your Letters Patent/Articles of Incorporation





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Questions for Follow-Up

- Have you reviewed your legal objects in the Letters Patent?
- Are all the activities of your charity within your objects?
- If something is not within your objects, have you discontinued such activities or modified the objects to include such activities?

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5. Non-Charitable Activities

A registered charity must devote its resources (funds, personnel, and property) to **charitable activities** (the work that advances the charitable purposes).

Certain non-charitable activities are allowed within limits like administration, fundraising, related business, social and political.

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What is a Charitable Purpose?

Four Heads of Charity:

1. Relief of **poverty**
2. Advancement of **education**
3. Advancement of **religion**
4. **Other purposes** *beneficial to the community in a way the law recognizes as charitable*



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Charitable Purpose – The 4th Head

- Agricultural and horticultural societies
- Welfare of domestic animals
- Parks, botanical gardens, zoos, aquariums, etc.
- Community recreation facilities, trails, etc.
- Community halls, libraries, cemeteries
- Summer camps, daycare/after-school care
- Crime prevention, public safety, and order
- Ambulance, fire, rescue, other emergency services
- Human rights, mediation services, consumer protection
- Support and services for charitable sector

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Questions for Follow-Up

- What activities does your charity undertake?
- Are they charitable, fundraising, admin, political, business, social and how much of each?
- Are you respecting the limits imposed by CRA on non-charitable activities?

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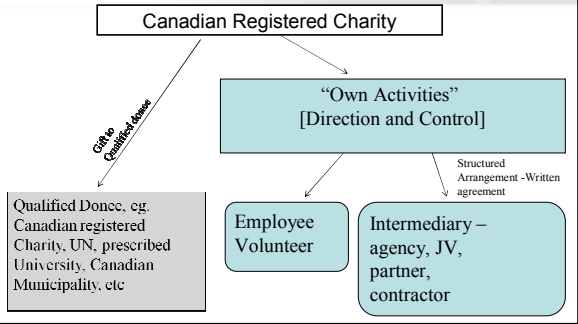
6. Gifts to Non-Qualified Donees

Charities conduct activities in two ways:

1. By gifting to “qualified donees”; or
2. By carrying on its own charitable activities.

Charities cannot gift to a non-qualified donee or be a “conduit”. (Gifts to non-qualified donees = 105% penalty on the amount of the gift and second infraction 110% penalty and greater chance of revocation.)



Need “direction and control” over funds and resources.



“Own Activities” or “Direction And Control”

When not working with qualified donee or own staff:



- Investigate Intermediary (due diligence)
- Written agreement
- Detailed description of activities
- Monitoring and Supervision
- Ongoing Instruction for changes
- Periodic Transfers
- Separate Activities and Funds
- Books and Records showing above

Questions for Follow-Up

- 1) Do you know what a qualified donee is?
- 2) Is your charity providing resources to organizations or individuals that are not qualified donees such as foreign charities?
- 3) Does your charity have an appropriate written agreement with all necessary elements?
- 4) Do you maintain "direction and control" over your resources?
- 5) Are you properly categorizing foreign activities on T3010?



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7. Fundraising Costs and Practice

- Fundraising is important for charities but it is not a charitable activity
- Lots of media and donor concern about costs and practices
- CRA Guidance on Fundraising recently released
- Must read for anyone very involved with fundraising:
<http://www.cra-arc.gc.ca/tx/chrts/plcy/cps/cps-028-eng.html>


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CRA Guidance for Fundraising

- Prohibited fundraising conduct (illegal, main purpose, too much private benefit, misleading or deceptive)
- Disclosure and transparency
- Apportioning expenses between fundraising and charitable
- Best practices
- Indicators of concern


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Indicators of Concern

- Sole-source fundraising contracts
- Non-arm's length fundraising contracts
- Fundraising initiatives that are not well-documented
- Fundraising merchandise purchases that are not at arm's length, not at fair market value, or not purchased to increase fundraising revenue.
- Most of the gross revenues for non-charitable parties.
- Commission-based fundraiser remuneration
- Misrepresentations in fundraising solicitations or in disclosures about fundraising or financial performance.

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CRA Guidance on Fundraising

Best Practices

- a. Prudent planning processes
- b. Appropriate procurement processes
- c. Good staffing processes
- d. Ongoing management and supervision of fundraising practice
- e. Adequate evaluation processes
- f. Use made of volunteer time and volunteered services or resources
- g. Disclosure of fundraising costs, revenues, and practice (including cause-related or social marketing arrangements)



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Fundraising Ratio of Costs to Revenues

Ratio of Costs to Revenues over Fiscal Period	CRA Approach (Cost to Revenue)
<ul style="list-style-type: none"> • Under 35% 	<ul style="list-style-type: none"> • <i>Unlikely</i> to generate questions or concerns.
<ul style="list-style-type: none"> • 35% and Above 	<ul style="list-style-type: none"> • The CRA will examine the <i>average ratio</i> over recent years to determine if there is a <i>trend</i> of high fundraising costs. The <i>higher the ratio</i>, the more likely it is that there will be concerns and a need for a more <i>detailed assessment of expenditures</i>.
<ul style="list-style-type: none"> • Above 70% 	<ul style="list-style-type: none"> • This level <i>will raise concerns</i> with the CRA. The charity must be able to provide an <i>explanation and rationale</i> for this level of expenditure to show that it is in compliance; <i>otherwise, it will not be acceptable.</i>



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Questions for Follow-Up

- Have you read the CRA Guidance on Fundraising and do you understand it?
- Are any of your activities prohibited?
- Do any of the indicators of concern apply to your charity?
- What are your charity's ratios of cost to revenue?
- Are your charity's ratios in line with CRA expectations?
- What steps are you taking to reduce your fundraising costs?



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8. Failure to Meet Disbursement Quota

The Disbursement Quota (DQ) is the amount that a registered charity must spend each year on its charitable activities or as gifts to qualified donees. ("80% rule")

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Two Key Disbursement Quota Elements

1. **Receipted Donations:** Each year, registered charities must spend amounts that are at least equal to 80% of the amounts for which it issued official donation receipts (with some exceptions) in the immediately preceding fiscal year.

PLUS

2. **Assets:** 3.5% of the average value of any assets the registered charity owned over the previous 24 months that were not used directly in charitable activities or in the administration of the registered charity (a complicated calculation).

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Why is There a Disbursement Quota?

The Disbursement Quota was established in the *Income Tax Act* (Canada) to achieve 3 purposes:

1. To ensure that most of a charity's funds are used to further its charitable purposes and activities;
2. To discourage charities from accumulating excessive funds; and
3. To keep other expenses at a reasonable level.

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Activities as Disbursements

- Only monies spent **directly** on charitable activities or on gifts to qualified donees are included in calculating the disbursement quota. This includes paying the salaries of persons performing actual charitable work (e.g. caring for the sick), buying equipment used in charitable activities.
- It should not include amounts spent on activities that support charitable objectives but do not directly accomplish them, such as management and administrative activities, fundraising or political activities.



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Questions for Follow-Up

- Review *Registered Charity Information Return Summary* received after filing T3010
- Optionally complete *T1259 Capital Gains and Disbursement Quota Worksheet* from CRA
- Do you have surplus or deficit in DQ?
- Have you reviewed T3010 resources at www.capacitybuilders.ca/clip?



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9. Political Activities

“A registered charity may pursue political activities to retain, oppose, or change the law, policy, or decision of any level of government inside or outside Canada provided the activities are non-partisan, related to its charitable purposes, and limited in extent.” (see T3010B)



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Political Activities

- Cannot have political purpose (object); only political activities
- No illegal or partisan political activities
- Political activities must be “connected and subordinate” to purpose (legal objects)
- Comply with “10% rule” and disbursement quota restrictions (political work on not charitable and only if DQ room)
- Informative, accurate, and well-reasoned (not false, inaccurate, or misleading)
- **Read CRA Policy Statement on Political Activities (CPS-022)**
<http://www.cra-arc.gc.ca/tax/charities/policy/cps/cps-022-e.html>


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An Activity can be...

- Prohibited activities (illegal and/or partisan political)
- Allowable political activities
- Charitable activities:
 - Public awareness campaigns
 - Communicating with an elected representative or public official
 - Education


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Questions for Follow-Up

- What are your charities legal "objects"?
 - Not mission or vision
- Does your organization engage in political activities?
- Are political activities reported on T3010?
- Are political activities connected and subordinate to legal objects?
- What percentage of expenses is political?
- Do you have DQ excess?

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10. Unrelated Business Activities

Income Tax Act prohibits "unrelated business activities" by all charities

Charitable organizations and public foundations are permitted to engage in "related business activities" but private foundations may not engage in any business activity

"Carrying on business" - activity is commercial in nature (derive revenue and provisions of goods and services, intention to earn profit) and continuous

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Why Prevent Unrelated Business?

- Unfair competition with private businesses
- Why should charities be able to compete tax-free?
- Business is not a charitable object
- Will encourage regular business to set up as charities
- In some countries, unrelated business is permitted, but the charity will be taxed on unrelated business income like a private business but not in Canada

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What is a Related Business?

There are two kinds of related businesses that a registered charity can conduct:

1. Businesses that are linked to a charity's purpose and subordinate to that purpose (for example, a hospital parking lot); and
2. Businesses that are run substantially (90%) by volunteers (for example, weekly bingos).

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Business Activities

For more guidance, see CRA's CPS-019 "What is a Related Business?"

- Penalties for unrelated business: 5% (1st infraction) on gross unrelated business revenue
- Earned in a taxation year
- 2nd infraction: 100% penalty on that revenue and suspension* of tax-receiving privileges



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CRA Website "What is a Related Business?"





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Questions for Follow-Up

- Read CPS-019 **What is a Related Business?** at <http://www.cra-arc.gc.ca/tx/chrts/plcy/cps/cps-019-eng.html>
- Is charity carrying on a **business**? i.e. activity commercial in nature (derive revenue and provisions of goods and services) (not issue of whether profitable or fees charged)
- If yes, then **are all goods donated?** (yes=fine)
- If not, is it **ongoing?** (no=fine)
- Is business related? (i.e. **90% volunteers** or **linked AND subordinate** to charity's purpose)
- If not, either then may be unrelated business



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11. Religious School Tuition Receipts

- If religious schools (either exclusively religious or dual (secular or religious)) are issuing tax receipts, they must ensure that they are only issuing receipts for religious portion of tuition, which, in the case of dual capacity schools, is based on the calculation set out in IC 75-23.
- Concern regarding inflated receipts

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12. Fraudulent Tax Receipts

- Tax receipts are sold for a small percentage of their face value
- No donation, or small donation, to charity
- No complicated scheme
- Keep tight control over receipts

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13. Charity Gifting Tax Shelters

- People can donate to registered charities in Canada and get an official donation receipt which is very valuable and can cost the tax system a lot. Promoters and “charities” cannot, through various games and tricks, abuse the tax system to issue whatever receipt they wish.
- Usually “investor” or “donor” is told that the tax benefits and deductions arising from the scheme will equal or exceed the costs of entering into the arrangement or the property.

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CRA Taxpayer Alerts on Tax Shelter Gifting





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Tax Shelter Gifting – Charity Concerns

1. Undermine public confidence in charities
2. Depletes tax revenues needed for basic services, many of which are delivered by charities
3. They are often illegal or fraudulent, usually unethical
4. Your donor will be audited (175,000 donors are currently being audited)
5. Determining the correct amount for the donation receipt



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Tax Shelter Gifting – Charity Concerns (cont.)

6. Disbursement quota problems
7. Fundraising by using commissions may violate codes of ethics
8. Tax Shelter Identification Numbers
9. You don't want to be considered a Promoter
10. Lawsuits



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Tax Shelter Gifting – Charity Concerns (cont.)

11. Questionable legal opinions
12. Civil penalties
13. Professional advisors
14. Advanced tax rulings
15. CRA's fundraising guidelines

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Tax Shelters

- "If it sounds too good to be true, it probably is."
- There are consequences
- Almost all schemes market themselves as being "different" from other schemes that CRA has warned about and promising that they are safe
- The CRA audits all charity gifting arrangements

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Is this an Abusive Tax Scheme?

1. Person donates \$100 to charity, receives no benefit and charity issues \$100 tax receipt.
2. Person donates \$100 to charity and receives \$10,000 tax receipt.
3. Person buys pharmaceuticals in India as part of a scheme for \$100, pharmaceuticals donated to charity and valued for purposes of tax receipt, at \$10,000, and tax receipt issued for \$10,000.

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14. Transactions with Directors

In Ontario, the Public Guardian and Trustee takes the position that directors of charities can only be reimbursed for reasonable out of pocket expenses – directors cannot be consultants or employees of charity.

In other provinces, more scrutiny of salaries, loans to directors, investments in companies of directors, transactions with businesses owned by directors, etc...



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Questions for Follow-Up

- 1) Does your charity have any transactions with directors except for repayment of reasonable expenses?
- 2) If in Ontario, have you received permission from court?



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15. Employment Issues

- Employee vs. Independent contractor
- Withholding source deductions
- Remitting source deductions
- Proper employment agreements
- Excessive compensation / private benefit



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Questions for Follow-Up

- 1) Are your "independent contractors" really independent contractors? See CRA publication *Employee or Self-employed?*: <http://www.cra-arc.gc.ca/E/pub/tg/rc4110/>
- 2) Is charity deducting appropriate amounts of CPP, EI, and income tax and remitting to CRA?
- 3) Do you have agreements with all employees and independent contractors?
- 4) Is compensation appropriate?



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16. Mishandling of Audit

- CRA has an obligation to audit registered charities to spot whether they are complying with the *Income Tax Act*
- Charities must assist with audit



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Tips for Handling Audit Properly

1. Respond quickly
2. Be cooperative and polite
3. Use your time wisely before the audit
4. Choose carefully which charity officer or employee represents the charity with CRA
5. The lawyer is generally best kept in the background
6. Have your records up-to-date



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Tips for Handling Audit Properly (cont.)

7. Answer questions at the audit truthfully and only if you know the answer
8. Providing documents – don't dump documents on CRA, remember solicitor-client privilege
9. Copying of documents – provide copies, keep originals, know what you have provided to CRA
10. Preliminary discussions and findings – take notes

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17. Failing to Keep Adequate Books and Records

A Canadian registered charity **must** keep *adequate* books and records, in either English or French. CRA must be able to:

- Verify revenues, including all charitable donations received;
- Verify that resources are spent on charitable programs; and
- Verify that the charity's purposes and activities continue to be charitable.



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Why We Need Adequate Books and Records

- Help with charity audits and can result in suspension of receipting privileges, or the loss of its registered status
- Knowing where expenses go and revenues come from
- Needed for issuing official donation receipts
- Help with decision making
- Makes it easier for you to complete filings
- Information on current and past financial position of charity
- Stakeholders may require



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Questions for Follow-Up

- 1) Do you have **governing documents** (incorporating documents, constitution, trust document), bylaws, **financial statements**, **copies of official donation receipts**, copies of T3010, written **agreements**, board and staff meeting **minutes**, **annual reports**, **ledgers**, **bank statements**, **expense accounts**, **inventories**, **payroll records**, **promotional materials**, and **fundraising materials**.
- 2) Do you have **source documents**? e.g., **invoices**, vouchers, work orders, delivery slips, purchase orders, and **bank deposit slips**.



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18. Other Legal Concerns for Charities

- Breaching contractual relationships (funding agreements, leases, etc.)
- Abuse of children and beneficiaries
- Criminal gangs and terrorism
- Fraud against charities, misuse of charitable assets
- Failure to respect donor restrictions (breach of trust)

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Charity Law Problem Solving

- Understand basic framework and definitions
- See CRA site for information
- See other sources of info (e.g. www.capacitybuilders.ca/clip, www.canadiancharitylaw.ca)
- Seminars and webinars
- Bolster board with diversity, skills, knowledge, passion, resources, active educational program
- Call CRA if you need
- Have charity lawyer on retainer or hire as needed

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Evaluation

- Your feedback is important to the Charity Law Information Program
- Please complete the Evaluation Form and add any comments that will help improve our program
- If you have any additional feedback contact clip@capacitybuilders.ca
- Thank you for your participation today!

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