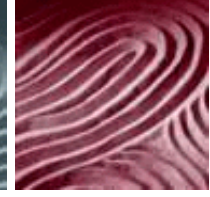
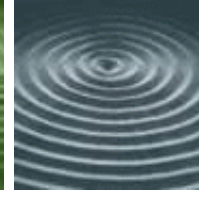
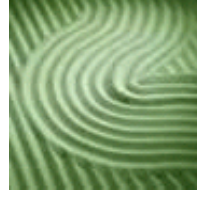


2500, 20 Queen Street West
Toronto, ON
Canada M5H 3S1
Tel. 416.595.8500
Fax. 416.595.8695
www.millerthomson.com



MILLER THOMSON LLP

Barristers & Solicitors, Patent & Trade-Mark Agents

TORONTO

VANCOUVER

CALGARY

EDMONTON

WATERLOO-WELLINGTON

MARKHAM

WHITEHORSE

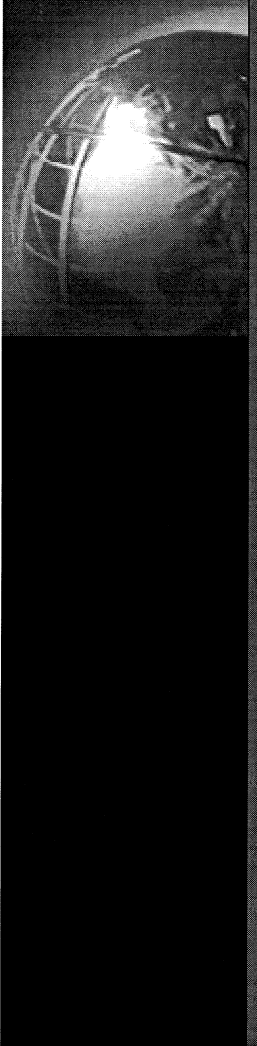
WASHINGTON, D.C.

Current Issues for Charities and CCRA Charity Audits

by Susan M. Manwaring
January 30, 2003

This article is provided as an information service only and is not meant as legal advice. Readers are cautioned not to act on the information provided without seeking specific legal advice with respect to their unique circumstances.

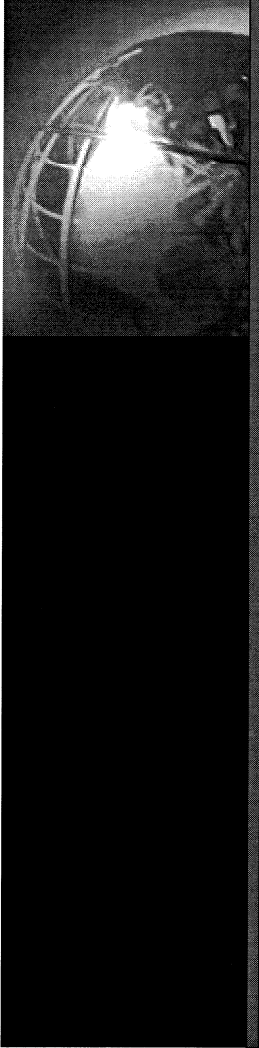
© Miller Thomson LLP 1998-2003



CCRA Audit Concerns / Current Issues

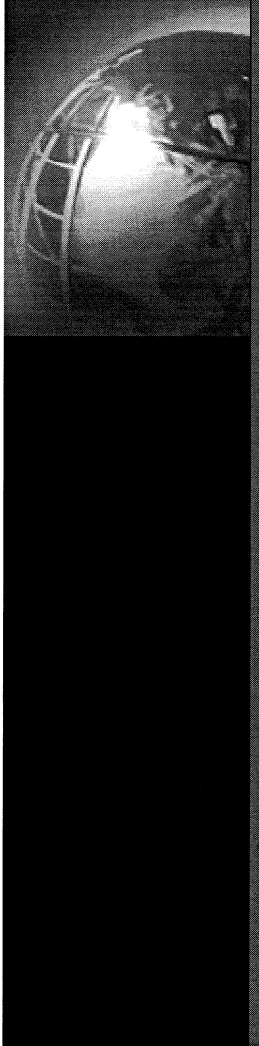
- **Political activity**
- **Split Receipting**
- **Directed gifts**
- **Art donation programs**
- **Related business**

MILLER THOMSON LLP



Political Activities

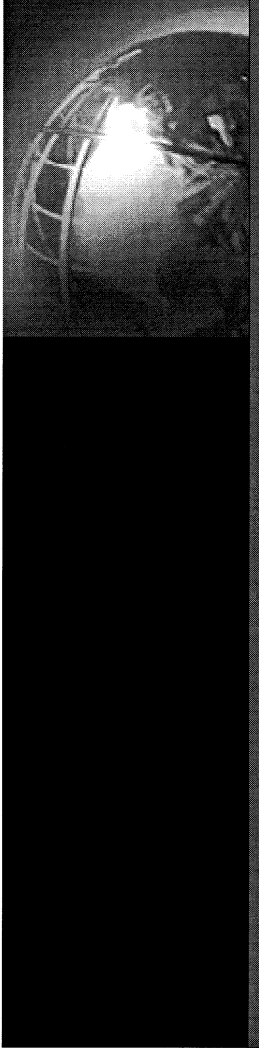
- **Not charitable at common law**
- **Not permitted by ITA**
 - **exception: “incidental” (less than 10% of resources) political activity**
 - **absolute prohibition on partisan activity**
- **Difficult to distinguish between education head and political advocacy**



Political Activities (cont.)

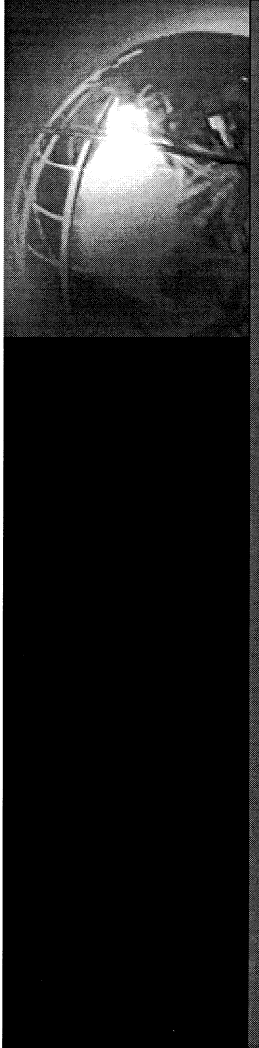
- **Significant audit activity (particularly in BC)**
- **CCRA 2002 Concept Draft Information Circular - “Registered Charities - Political Activities”**

MILLER THOMSON LLP



Political Activities (cont.)

- **Draft states: “Political purposes are those that seek to support a political party or candidate for public office; or to retain, oppose or change the law or policy or decisions of any level of government, in Canada or a foreign country.”**
- **Comments to CCRA by March 31**



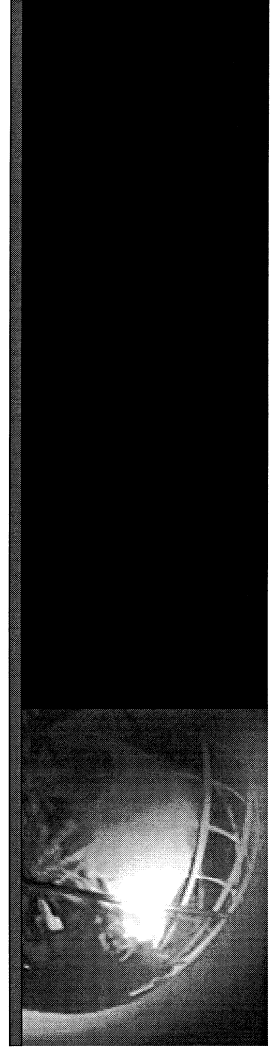
Split Receipting

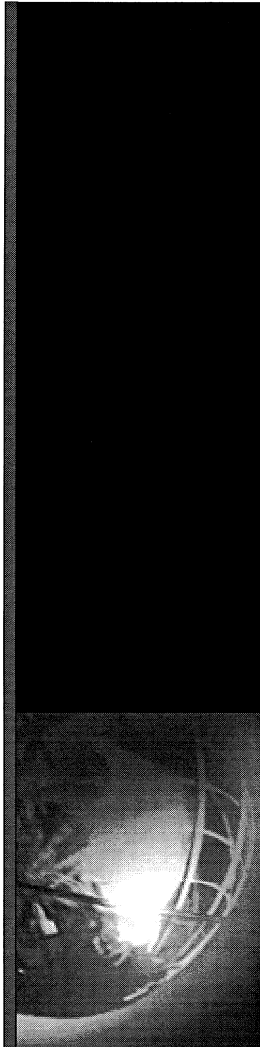
- **Common law definition of gift prohibited any consideration flowing back to donor**
- **Quebec civil law defined bargain sale to be a gift**
- **Different tax law in Quebec?**

Finance on Split Receipting

- December 20, 2002 technical bill:

- new rules legislate mechanism for providing receipt where there is partial consideration
- these rules are effective December 20, 2002
- consideration received cannot have a value that is greater than 80% of the value of the gift unless proof of donative intent





Finance (cont.)

- tax credit / deduction will be available for the “eligible amount” of gift
- eligible amount is difference between fair market value of donated property and any “advantage” received by donor
- new form of donation receipt - Charity is required to determine amount if any of the “advantage” and identify it on receipt

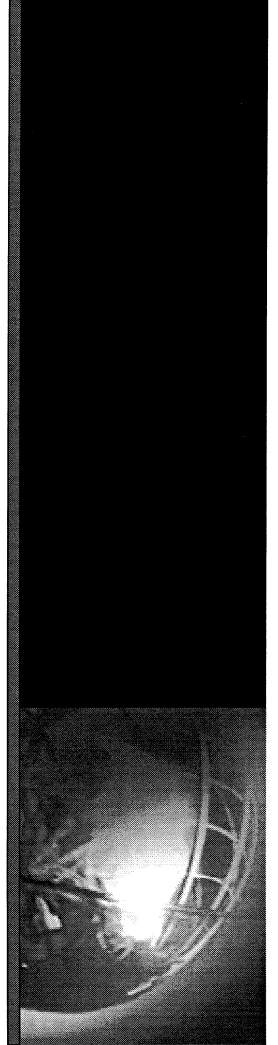
CCRA on Split Receipting

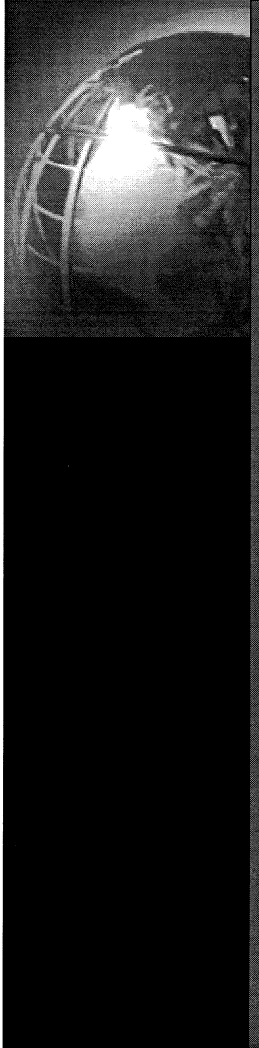
- Draft Technical News 26 published Dec. 24, 2002

– proposed split receipting rules will apply for common fundraising events

- dinners
- auctions
- concerts
- golf events

MILLER THOMSON LLP

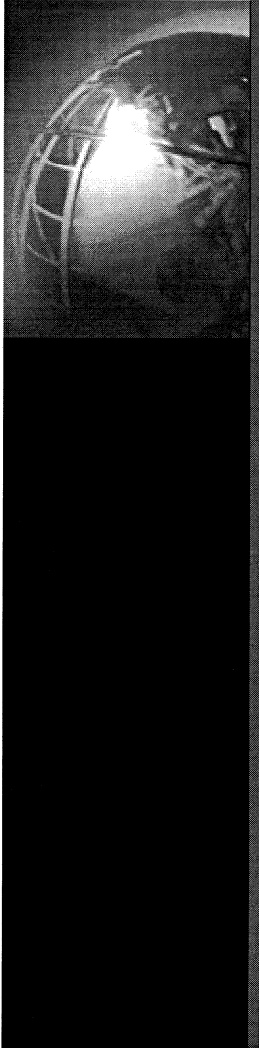




CCRA (cont.)

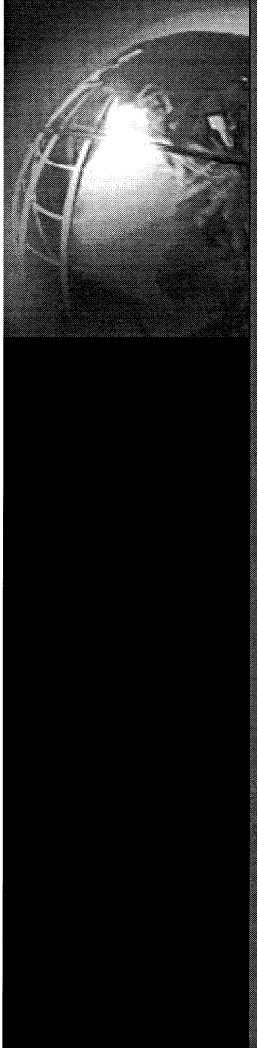
- **new tax treatment of gift annuities-
IT -111R2 no longer applies**
- **gifts of real property subject to
mortgage with Charity assuming
mortgage will now be permitted**
- **consider other gifts providing
benefit to donor or other gifts of
property subject to debt?**

MILLER THOMSON LLP



Directed Gifts

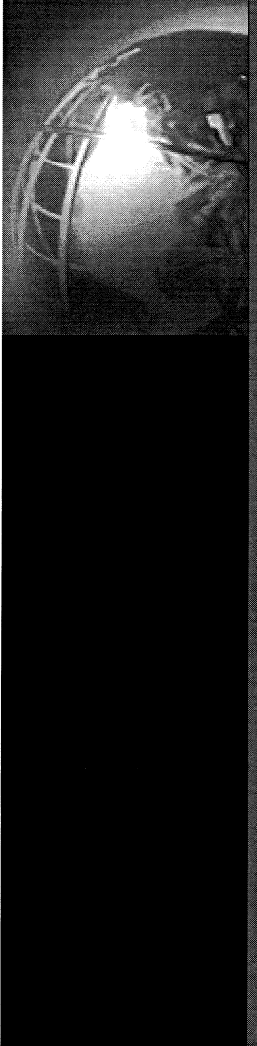
- **FCA (*Woolner*) definition of gift:**
“This Court has held that a gift, within the meaning of the common law, is a voluntary transfer of property from one person to another gratuitously and not as the result of a contractual obligation without anticipation or expectation of material benefit”



Directed Gifts (cont.)

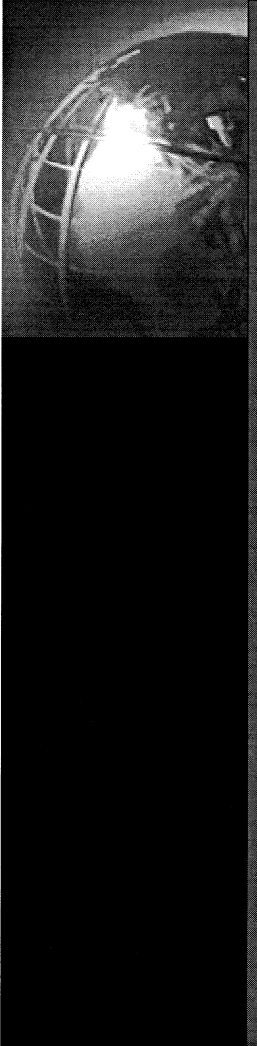
- **IT-110R3 “Gifts and Official Donation Receipts” paragraph 15(f):**

(f) A charity may not issue an official receipt for income tax purposes if the donor has directed the charity to give the funds to a specified person or family... However, donations subject to a general direction from the donor that the gift be used in a particular program operated by the charity are acceptable, provided that no benefit accrues to the donor, the directed gift does not benefit any person not dealing at arm's length with the donor, and decisions regarding utilization of the donation within a program rest with the charity.



Directed Gifts (cont.)

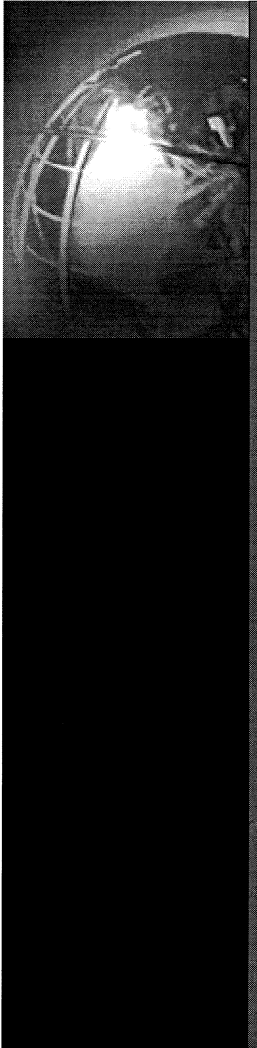
- **CCRA asking (itself) whether new split receipting rules apply - Is there an advantage?**
- **Religious Education**
- **Deputation**



Art Donation Programs

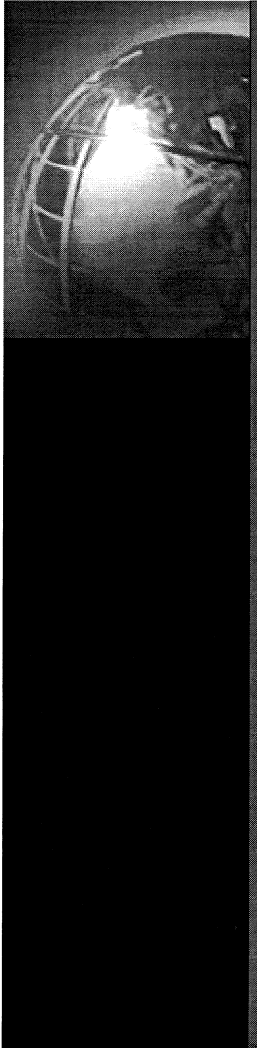
- **Donations of art through promoters**
 - high valuations
- **CCRA considers these abusive**
 - challenge gift
 - challenge valuation of gift
 - disbursement quota issues

MILLER THOMSON LLP



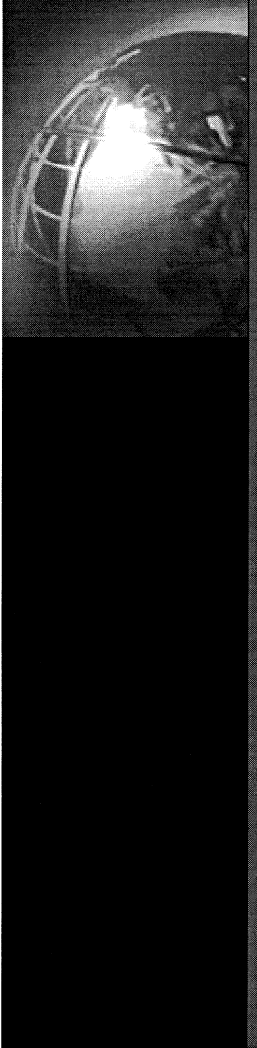
Related Business

- ***ITA*** permits charitable organizations and public foundations to carry on “related business”
- **Revocation of registration as penalty for unrelated business**
- ***Alberta Institute for Mental Retardation case***
 - **business is related if it raises funds to be used for the charity’s charitable purposes**



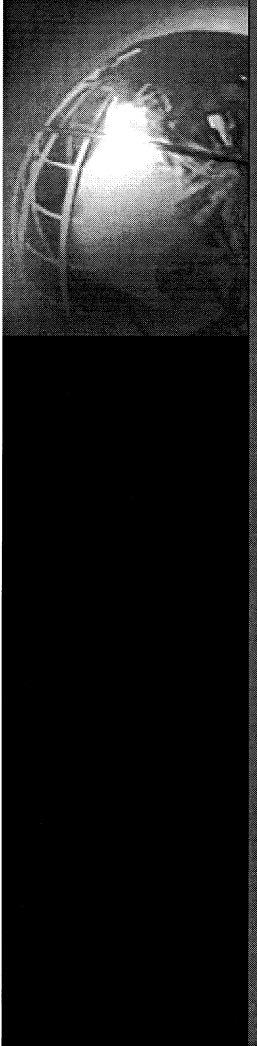
Related Business (cont.)

- ***CCRA Consultation on Proposed Policy: Guidelines for Registered Charities on Related Business***
 - **Selling donated goods is not a business**
 - **Related means:**
 - (a) **linked to a charitable purpose**
 - (b) **subordinate to that purpose**



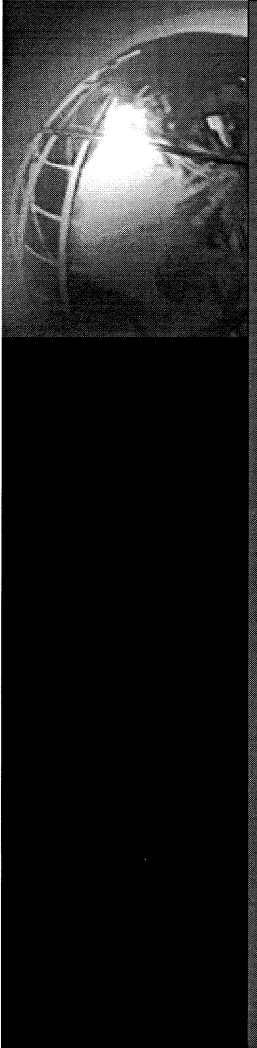
Related Business (cont.)

- **Proposal rejects destination of funds test**
- **more restrictive than previous CCRA position**
- **any “commercial” activity can be reviewed**



Related Business (cont.)

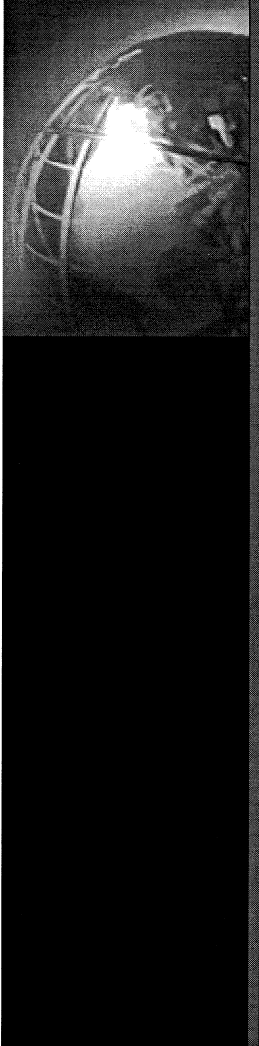
- ***Earth Fund case***
 - rejects *Alberta Institute* approach
 - does not provide explicit guidance on defining related business
 - justification for new audit program?
- **Revocation safe harbour**
 - cease business activity, or
 - transfer business activity into a taxable subsidiary



CCRA Charities Audits

- **CCRA Charities Directorate**
 - Charities Directorate auditors
 - Consulting and Audit Canada auditors
 - CCRA Tax Services Office auditors
- **Other audits:**
 - GST/HST
 - payroll

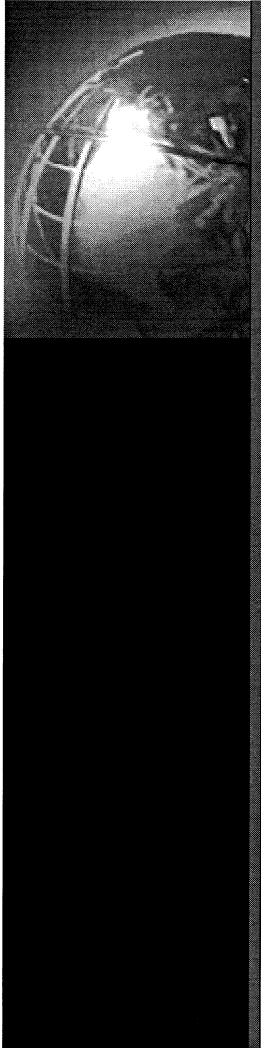
MILLER THOMSON LLP



CCRA Audit Authority

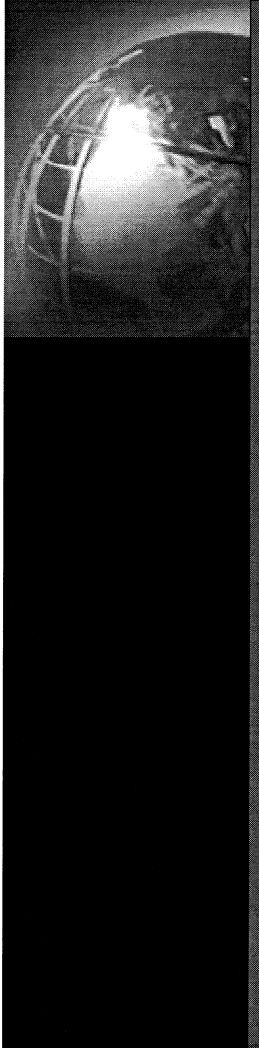
- **Escalating series of information gathering tools**
- ***ITA 231.1* audit power**
 - power to inspect records to ensure compliance

MILLER THOMSON LLP



CCRA Audit Authority (cont.)

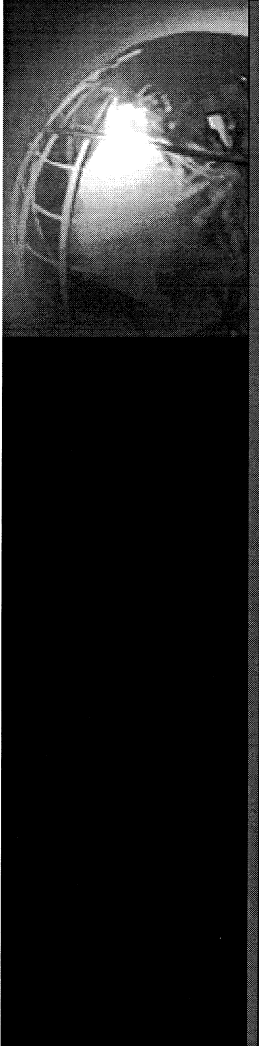
- ***ITA 231.2***
 - requirement to provide information
 - revocation / fines / imprisonment for failure to comply
 - FCTD judicial review
- ***ITA 231.3***
 - search warrants
 - suspicion of criminal wrongdoing



CCRA Audit Selection

- **400-500 audits / year**
- **Random**
- **Problem areas**
- **Complaints**
 - **public record:**
 - **constating documents**
 - **T2050 application for registration**
 - **T3010 information returns**
 - **Friends of Clayoquot Sound revocation**

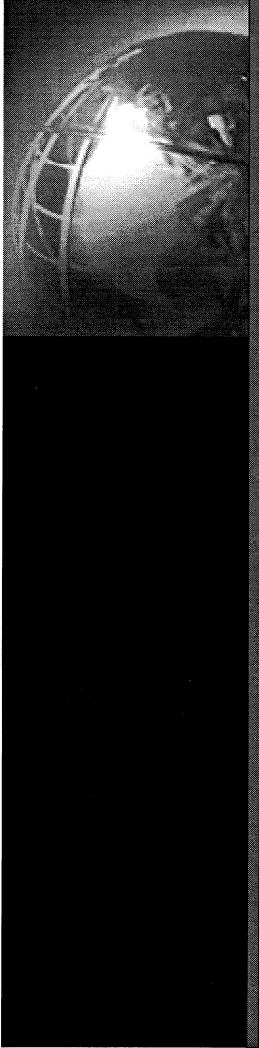
MILLER THOMSON LLP



Registered Charity's Audit Philosophy

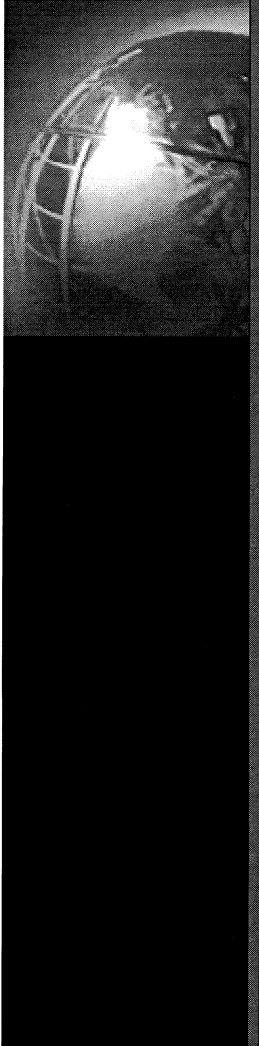
- ***ITA* requires “all reasonable assistance” to auditor**
- **Disclose only required information**
- **Pre-audit compliance**

MILLER THOMSON LLP



***ITA* Recordkeeping Requirements**

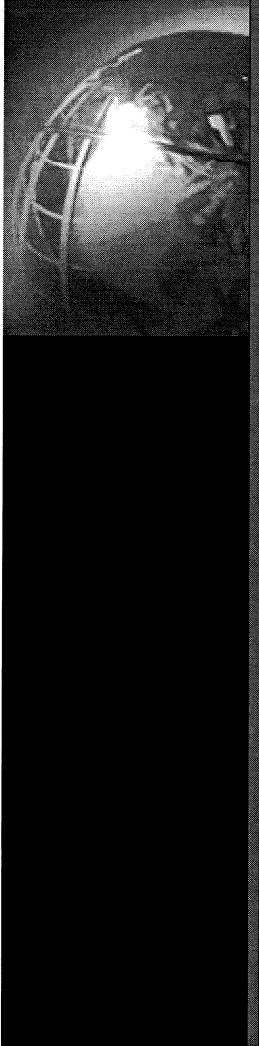
- ***ITA* 230(2) requires charity to keep complete records**
- ***ITA* 230(4.1) electronic data acceptable**
- ***ITA* 230(4) minimum retention:**
 - **6 years from end of year:**
 - **records to show charitable status**



ITA Record Retention Requirements

- ***IT Reg. 5800* minimum retention:**
 - **2 years after deregistration (if ever):**
 - **directors' and members' meeting minutes**
 - **all governing documents**
 - **records of 10 year trust gifts**
 - **2 years from end of year:**
 - **duplicate receipts and supporting documents**

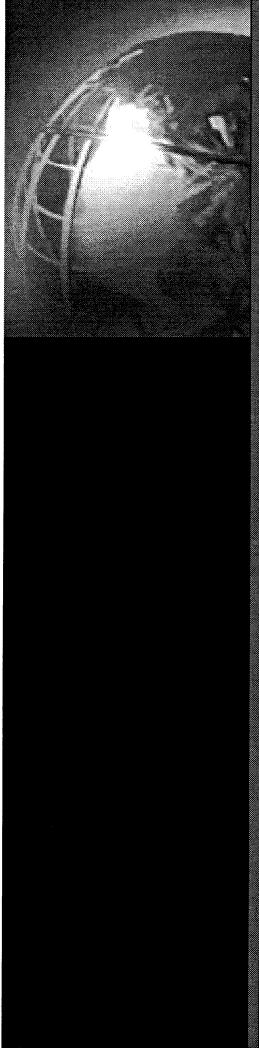
MILLER THOMSON LLP



Audit Notification

- **Initial CCRA letter or call to charity**
 - schedule audit
- **Charity should contact professional advisors**
 - for advice, not representation
- **Confirm audit parameters**
 - limit scope
 - prepare specific responses / have specific items available

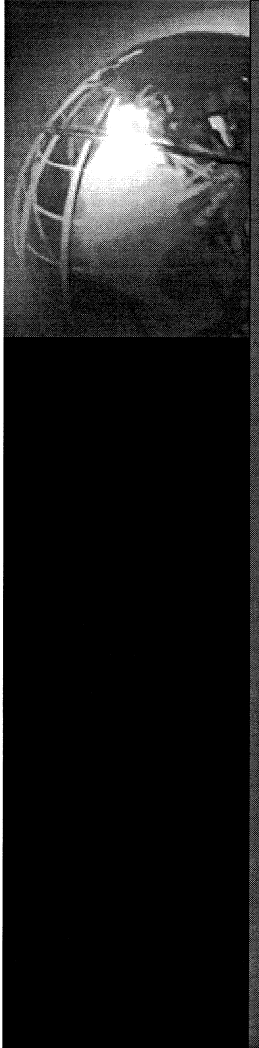
MILLER THOMSON LLP



Pre-Audit Review

- **Legal issues**
- **Accounting issues**
 - **consider privilege**
 - **accounting review for purpose of supporting legal advice**
- **Repair non-compliance**
 - **creativity, not dishonesty**

MILLER THOMSON LLP

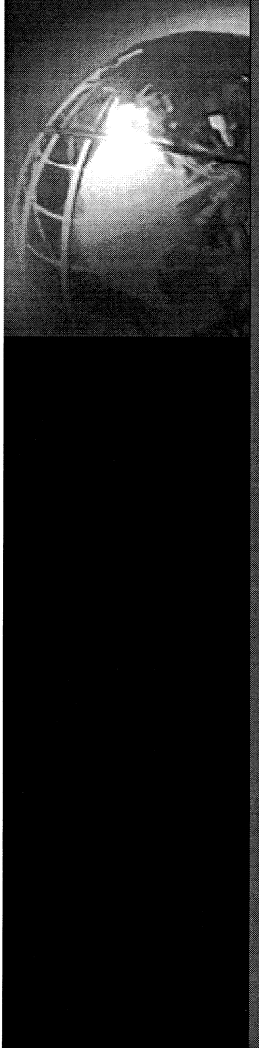


Audit Day

- ***ITA 231.1* requires “all reasonable assistance”**
- **Civility**
- **Limited staff access**
- **Privileged documents**
- **Written questions**

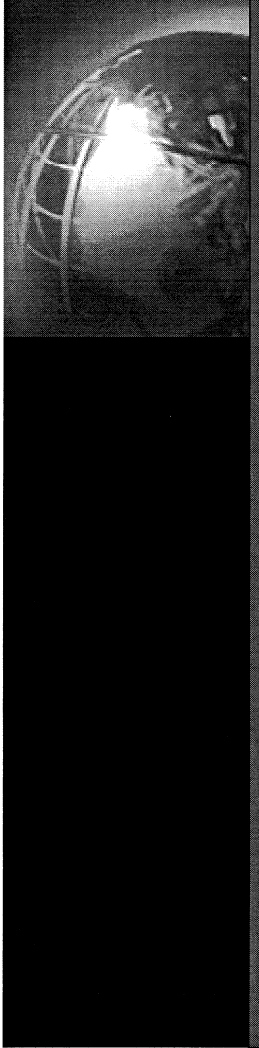
- **Auditor is not a source of free professional advice**

MILLER THOMSON LLP



Post-Audit

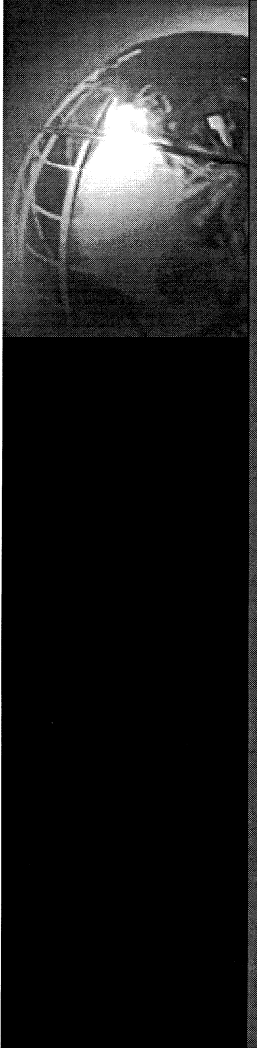
- **Auditor reviews initial findings with charity**
 - opportunity to correct inaccuracies
- **Auditor returns file to Charities Directorate**
 - slow CCRA turnaround (maybe never)
- **Consider compliance changes before Charities Directorate contact**



Clean Audit Report

- **Confirmation of Compliance**
- **Education Letter**
 - **minor issues only**
 - **no compliance action proposed**

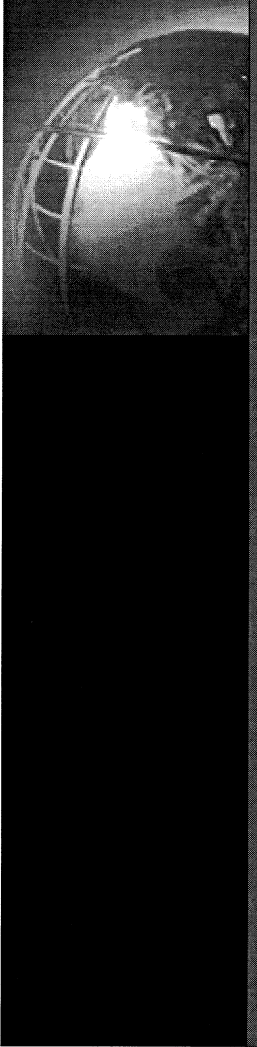
MILLER THOMSON LLP



Audit Report (Issues Raised)

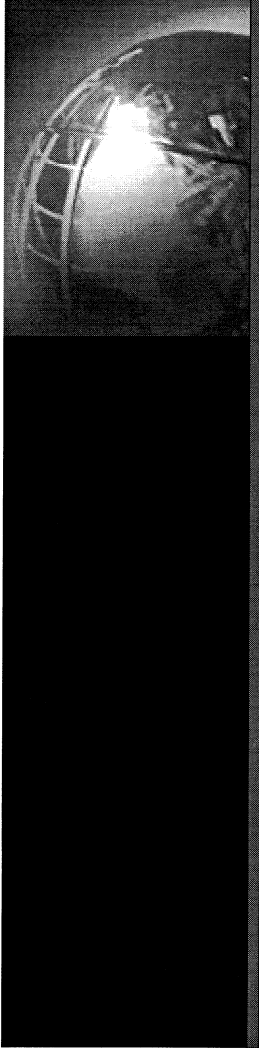
- **First offense / clean operation**
 - **Undertakings Letter**
 - correct for future
- **Subsequent offense / serious violation**
 - **Administrative Fairness Letter**
 - proposal to revoke registration
 - revocation is often threatened - rarely carried out
- **Legal representation and submissions**

MILLER THOMSON LLP



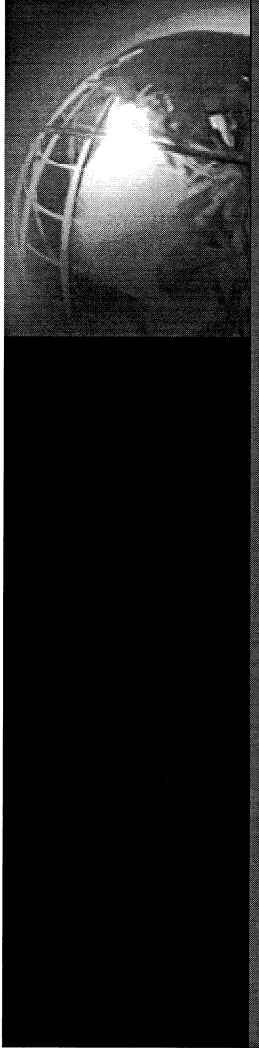
Revocation of Registration

- **Only penalty available for most offences**
 - no intermediate sanctions
 - VSI JRT proposal
- ***ITA 168* revocation for:**
 - ceasing to comply with requirements for registration
 - improper receipting
 - interfering with audit



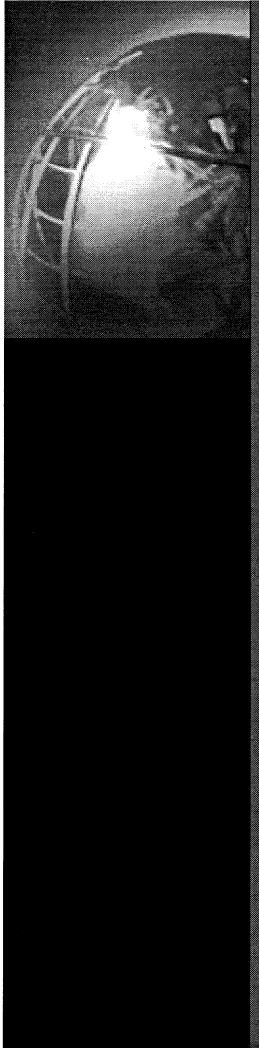
Result of Revocation

- **Penalty tax equal to assets**
 - unless transfer assets to another registered charity
- **Pre-register transferee charity in cases of risky activities**



Revocation Appeal

- **Federal Court of Appeal judicial review**
 - limited to CCRA file record
 - very expensive
- **Filing appeal often leads to settlement as senior CCRA staff / Justice counsel become involved**
- **VSI JRT proposes trial *de novo* at Tax Court of Canada**



CCRA Charity Audits

Susan M. Manwaring
smanwaring@millerthomson.ca
416.595.8583

January 30, 2003

MILLER THOMSON LLP