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2006 CHARITY AND NOT-FOR-PROFIT LAW DEVELOPMENTS: THE YEAR IN REVIEW

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A. INTRODUCTION

The charitable sector in Canada has seen a number of important legislative, regulatory and common law developments during the last year which have significantly impacted how charities will operate both in Canada and abroad. The following Bulletin provides a brief summary of some of the more important of these developments, including recent changes under the *Income Tax Act* ("ITA"),[1] new policies and publications from the Charities Directorate of the Canada Revenue Agency ("CRA"),[2] select federal and provincial legislative issues affecting charities, as well as a selection of some of the more significant court decisions over the past year.

* During 2006, Terrance S. Carter and other lawyers at Carters Professional Corporation (Mervyn F. White, Karen J. Cooper, Theresa L.M. Man, U. Shen Goh, D. Ann Walters and Nancy E. Claridge) published numerous articles in *Charity Law Bulletin* (www.charitylaw.ca), as well as in *The Lawyers Weekly*, *Charity Talk* (Canadian Bar Association), *Charitable Thoughts* (Ontario Bar Association), *The Philanthropist*, *Canadian Fundraiser*, *Gift Planning in Canada*, *The Bottom Line*, *Checkmark* and *International Journal of Civil Society Law*. Portions from those articles have been incorporated in this summary. Terrance Carter acknowledges Sean Carter, student-at-law, for his assistance with articles related to anti-terrorism law (www.antiterrorismlaw.ca).

[1] R.S.C. 1985, c. 1 (5th Supp.) as amended.

[2] Charities Directorate of Canada Revenue Agency, online: www.cra-arc.gc.ca/tax/charities.

B. RECENT CHANGES, RULINGS AND INTERPRETATIONS UNDER THE *INCOME TAX ACT*

1. Budget 2006: Elimination of Tax on Gifts of Public Company Shares

In the 2006 Federal Budget released on May 2, 2006, the Conservative government upheld its commitment to remove the capital gains tax on publicly listed securities donated to charities and extended this measure to gifts of ecologically sensitive land, effective immediately. On June 22, 2006, Bill C-13, the *Budget Implementation Act, 2006*,[3] implementing these provisions through the enactment of amendments to the ITA, received Royal Assent. For qualifying gifts made on or after May 2, 2006, there will no longer be a taxable capital gain and the entire amount of the donation tax credit will be available to be used against other sources of income. In effect, this means that the tax benefit arising from a gift of publicly traded securities or ecologically sensitive land would be the same as if it were a gift of cash. From a practical perspective, donors of qualifying shares should instruct their broker to transfer the shares intended to be gifted directly to an investment account which the charity would need to set up with its own broker, with the transfer of shares being carried out electronically where possible. For purposes of valuation, CRA will accept the closing bid price of the share on the date it is received or the mid-point between the high and the low trading prices for the day, whichever provides the best indicator of fair market value. Any gift acceptance policy that a charity might develop with respect to the receipt of publicly traded shares should deal with these issues, as well as consider under which circumstances the organization might refuse to accept such a gift, for example where the business or activities of the corporation conflict with the objects and values of the organization. While the elimination of capital gains tax on publicly listed securities and gifts of ecologically sensitive land does not currently apply to gifts to private foundations at the time of writing, the government has indicated in the Budget that it is intending to extend the measure but in the interim will be consulting with the sector to develop some self-dealing rules to safeguard against potential conflicts of interest.

2. Bill C-33 – Proposed Amendment to the *Income Tax Act* Affecting Charities[4]

On November 9, 2006, the Department of Finance ("Department") released the long-awaited Notice of Ways and Means Motion to move forward with the proposed amendments to the ITA. The motion

[3] S.C. 2006, c. 4.
[4] For more information, see Theresa L.M. Man and Terrance S. Carter, "Bill C-33 – Proposed Amendments to the *Income Tax Act* Affecting Charities" in *Charity Law Bulletin* No. 104 (December 7, 2006).

was introduced as Bill C-33, and received its first reading in the House of Commons on November 22, 2006 as the *Income Tax Amendments Act, 2006*. The proposed changes were last released by the Department on July 18, 2005, which amended and consolidated earlier proposed amendments released on December 20, 2002, December 5, 2003 and February 27, 2004. A number of the proposed changes contained in Bill C-33 will significantly impact the operations of registered charities in Canada. Some of the most significant proposed changes involve the introduction of split-receipting rules and rules to curtail abusive donation tax shelter schemes. These changes are contained in subsections 248(30) to (41) of the ITA. Other proposed amendments include new definitions for charitable organizations and public foundations, rules affecting the revocation of charitable registrations, municipal or public bodies performing a function of government in Canada as new qualified donees, and new expanded disclosure of information concerning registered charities to the public. The provisions contained in Bill C-33 are, for the most part, the same as the amendments released in July 2005, with a few exceptions including the withdrawal of the reasonable inquiry requirement, a provision with respect to inter-charity gifts, and circumstances involving the non-application of the deemed fair market value rule.

3. Foundations Incurring Debts to Purchase Investments[5]

In a Technical Interpretation (2005-0154751I7) dated October 21, 2005,[6] CRA reversed its position with respect to public and private foundations incurring debts for the purpose of acquiring investments, enabling both to now do so. Previously, CRA had always been of the view that the phrase "debts incurred in connection with the purchase and sale of investments" in paragraphs 149.1(3)(d) and 149.1(4)(d) of the ITA would only permit a miscellaneous type of debt, such as brokerage fees or other incidental amounts that could relate either to the purchase or the sale of investments. CRA explained that the reason for the change in its policy was because "jurisprudence has confirmed that the phrase 'in connection with' has very broad meaning." However, CRA indicated that debt arrangements would continue to be reviewed by CRA, especially those involving non arm's length parties, in order to ensure that there are no other compliance issues, such as personal benefit.

[5] For more information, see Theresa L.M. Man, "Foundations Incurring Debts to Purchase Investments" in *Charity Law Bulletin* No. 86 (February 7, 2006).
[6] CRA Technical Interpretation 2005-0154751I7, Debts Incurred By Charitable Foundations, October 21, 2005.

4. Meaning of "Charitable Activities"

In a Technical Interpretation (2006-0168601E5) dated October 23, 2006,[7] CRA considered the meaning of "charitable activities" for the purpose of providing guidance on the difference between expenditures on charitable activities and the expenditures on management and administration when determining whether a registered charity has met its 80% disbursement quota. In cases where expenditures are partly attributable to charitable programs and partly to management and administration, it is necessary to allocate the expenditures between these two categories and the allocation should be made on a consistent and reasonable basis. CRA recognized that in practice it is not always easy to draw the line between these two categories and indicated that it has undertaken to review the issue further.

5. Reward Points/Airline Tickets[8]

In a Technical Interpretation (2006-0193261E5) dated July 18, 2006,[9] CRA reiterated its policy with respect to charitable donations of air travel points. Care must be taken to determine if the donation qualifies as a gift for the purposes of section 118.1 of the ITA, particularly with respect to whether the points may be transferred. A charity that receives premium points which qualify as a gift must include the value of the points in determining its income, and it may issue an official tax receipt for the gift. If a receipt is issued, the value of the premium points will be included in the calculation of the charity's disbursement quota. As long as the gift is used by the charity in connection with its charitable activities, there should be no other tax implications for the charity. It is not recommended that premium points be held for a long period of time because their value could possibly diminish or the points could expire, causing potential problems from a valuation perspective. It could also possibly expose the charity to the consequences of failing to devote its resources on charitable activities.

6. Charity Texas Hold'em Tournaments

On April 25, 2006, CRA released a Technical Interpretation (2005-014243)[10] in connection with subsections 248(31) and 248(32) of the ITA. CRA indicated that when determining the "eligible

[7] CRA Technical Interpretation 2006-0168601E5, Meaning of the term "charitable activities", October 23, 2006.
[8] For more information, see Karen J. Cooper, "Donations of Premium Points" in *Charity Law Bulletin* No. 99 (September 21, 2006).
[9] CRA Technical Interpretation 2006-0193261E5, Reward Points/Airline Tickets, July 18, 2006.
[10] CRA Technical Interpretation 2005-014243, Charitable Organizations and Split Receipts, April 25, 2006.

amount" of a gift for the purposes of an income tax receipt for a Texas Hold'em poker tournament, the amount of the "advantage" allocated to each participant will include the total prize money divided by the number of participants and an amount equal to what a participant would pay to play in a similar Texas Hold'em poker tournament that is not sponsored by a charity. However, charities should be aware that in many provincial jurisdictions, including Ontario, such tournaments may not be legal as they would not fall within the "charitable gaming" exception in the *Criminal Code*.[11]

7. Private Foundations Investing in Limited Partnerships

In an advance income tax ruling (2006-016742117) dated June 27, 2006,[12] CRA considered the issue of whether a private foundation would be considered to be carrying on a business by virtue of its foreign limited partnership such that the private foundation's registration could be revoked pursuant to paragraph 149.1(4)(a) of the ITA. CRA took the position that the foundation's registration could be revoked if it was established that the foreign limited partnership was a partnership for Canadian tax purposes.

C. NEW POLICIES AND PUBLICATIONS FROM CANADA REVENUE AGENCY

1. CRA Guidelines for Registering a Charity: Meeting the Public Benefit Test[13]

To be charitable at common law, an organization must not only engage in activities that are intended to achieve its charitable purpose, but such activities must also result in a benefit to the public, or a sufficient section of it. The meaning and significance of this notion of "public benefit," however, has been surrounded with much confusion, leading charitable organizations and legal commentators to express concerns with its lack of clarity and uncertainty. In response to this confusion, on March 10, 2006, CRA released its long-awaited policy on meeting the public benefit test, entitled "Guidelines for Registering a Charity: Meeting the Public Benefit Test."[14] The guidelines attempt to clarify the meaning of the term "public benefit" and explain how it factors into CRA's determination of charitable status. Thus, the Guidelines will be of great interest to both potential and current charitable organizations, as they set out CRA's requirements for meeting and maintaining its standards with

[11] R.S., 1985, c. C-46.
[12] CRA, Document number: 2006-016742117, Private Foundation Investing in Limited Partnership, June 27, 2006.
[13] For more information, see Terrance S. Carter and Karen J. Cooper, "CRA Releases New Policy on Meeting the Public Benefit Test" in *Charity Law Bulletin* No. 93 (April 19, 2006).

respect to the public benefit test. The test is described in the Guidelines' introduction as being "at the heart of every inquiry into an organization's claim to charitable status." CRA's Guidelines indicate that applicants for registered charitable status are required to establish three elements: (1) the benefit must generally be shown to be tangible; (2) the benefit must generally shown to be direct; and (3) there must be a net benefit for the public.

2. CRA Registered Charities Newsletter No. 26 – Winter 2006

In January 2006, CRA released the Winter 2006 edition of its Registered Charities Newsletter.[15] Many questions relating to books and records had been raised by charities involved in work outside of Canada in the wake of the December 2004 tsunami which devastated areas of south-east Asia. In response, CRA provided guidance in this newsletter concerning the ways in which charities can ensure that they are maintaining adequate books and records. Their summary for books and records is as follows: "A registered charity must keep adequate books and records at a Canadian address it has on file with us, so that we can verify official donation receipts issued, as well as its revenue and expenditures. It must also include information that will enable the Minister to determine if there are any grounds for revocation. A charity must also keep source documents that support the information in the records and books of account." There is also commentary on several Federal Court of Appeal decisions related to the books and records of charities.

3. CRA Registered Charities Newsletter No. 27 – Fall 2006

In December 2006, CRA released the Fall 2006 edition of its Registered Charities Newsletter.[16] Included in the newsletter is information concerning the application of new intermediate sanctions for non-compliance of charities. CRA's Guidelines concerning these penalties will be made available on the Charity Directorate's website at: www.cra-arc.gc.ca/charities. There is a series of questions and answers relating to identifying the donor with respect to official donation receipts,[17] enduring property, and planned giving arrangements, including charitable gift annuities,[18] life insurance policies

[14] CRA, Reference Number CPS-024, online: www.cra-arc.gc.ca/tax/charities/policy/cps/cps-024-e.html.
[15] CRA, online: www.cra-arc.gc.ca/tax/charities/newsletters-e.html.
[16] *Ibid.*
[17] See CRA Policy Commentary, Name on Official Donation Receipt, online: www.cra-arc.gc.ca/tax/charities/policy/cpc/cpc-010-e.html.
[18] See *Income Tax – Technical News No. 26*, online: www.cra-arc.gc.ca/E/pub/tp/itnews-26/README.html.

and charitable remainder trusts.[19] The newsletter also addresses CRA's policy on "public benefit",[20] debts incurred by charitable foundations,[21] restrictions on private foundations,[22] the definition of "non-qualified investment" under the ITA,[23] and the gift of residue qualifying as a "gift by an individual's will."[24] The decisions noted under Court News include: *A.Y.S.A. Amateur Youth Soccer Association v. Canada Revenue Agency* (in relation to the promotion of amateur sports),[25] *Bayit Lepletot v. Minister of National Revenue* (with regard to conducting activities in a foreign country),[26] and *MacDonald Estate v. The Queen* (with respect to donations where there is no provision in the will).

4. CRA Eliminates Charity Advisory Committee

Effective September 25, 2006, the Government announced that as a result of its decision to reduce program expenditures, the advisory committees of CRA would be eliminated, including the Charities Advisory Committee ("CAC"). The CAC functioned well over the last two years in providing an effective bridge between the charitable sector and CRA, as well as the Minister of National Revenue, and as such, it is disappointing that the CAC has been eliminated.

5. CRA Policy Regarding Pending Legislation

On November 28, 2006, at the Annual Conference of the Canadian Tax Foundation ("CTF") in Toronto,[27] a representative of CRA participated in a round-table discussion of the CRA's policies on a variety of issues, including the re-introduction and application of the draft technical amendments to the ITA. CRA was asked whether it has any further comments regarding the position enunciated at the 2005 CTF Annual Conference concerning the filing of income tax returns in the context of pending legislation amending the ITA. The response was that its administrative practice continues to be to ask taxpayers to file their returns based on proposed legislation. However, where proposed legislation

[19] See IT-226R, *Gift to a Charity of a Residual Interest in Real Property or an Equitable Interest in a Trust*, online: www.cra-arc.gc.ca/E/pub/tp/it226r/README.html.
[20] *Supra* note 14.
[21] *Supra* note 5 and 6.
[22] See CRA Policy Statement, "What is a related business?", online: www.cra-arc.gc.ca/tax/charities/policy/cps/cps-019-e.html.
[23] *Supra* note 1 at subsection 149.1(1).
[24] *Supra* note 1 at subsection 118.1(5).
[25] *Infra* note 38.
[26] *Infra* note 45.
[27] For more information, see Theresa L.M. Man and Terrance S. Carter, "Bill C-33 – Proposed Amendments to the *Income Tax Act* Affecting Charities" in *Charity Law Bulletin* No. 104 (December 7, 2006).

increases government expenditures (such as an increase in refundable tax credits), CRA's practice is to wait for the legislation to be enacted. When a taxpayer files a return in accordance with draft legislation and the implementation date for the legislation is subsequently postponed, CRA will permit the taxpayer to refile its return in accordance with the unamended legislation.

6. Policy Commentary on Publishing Magazines and Advancement of Education[28]

On February 3, 2006, CRA released a Policy Commentary, "Charitable purposes – Whether publishing a magazine can be considered a charitable activity under the advancement of education."[29] It clarifies the CRA's position on granting charitable status to organizations that publish magazines in furtherance of educational purposes, indicating that CRA accepts that registered charities can advance education through the publication and distribution of magazines, but the contents of the publications must be predominantly educational in the sense understood by charity law. Material that would not be considered educational, *e.g.*, games, entertainment, opinion and advertising, is allowable provided that it is highly limited and always remains ancillary and incidental to the main educational purpose.

7. CRA Clarification Regarding Fair Market Value

In an update to its "Gifts and Income Tax" Guide,[30] CRA clarified how the fair market value ("FMV") of a gift is to be calculated. With respect to the FMV of donated property, it is necessary to determine the "eligible amount" of the gift, which CRA also clarified. The Guide contains a section on donation appraisals with guidelines for donors and qualified donees approaching appraisers and dealers. One or more appraisals may be required in order to establish the FMV of the property a person is donating. The appraised FMV is used to calculate the eligible amount of the gift unless the deemed FMV rules apply.

[28] For more information, see Theresa L.M. Man, "Publication of Magazines for the Advancement of Education" in *Charity Law Bulletin* No. 92 (April 18, 2006).
[29] CRA, Reference Number CPC-027, online: www.cra-arc.gc.ca/tax/charities/policy/cpc/cpc-027-e.html.
[30] CRA, Gifts and Income Tax (P113), online: www.cra-arc.gc.ca/E/pub/tg/p113/README.html.

D. OTHER FEDERAL LEGISLATION AFFECTING CHARITIES

1. New Anti-Terrorism Legislation Passed/Granted Royal Assent[31]

On October 5, 2006, the Minister of Finance introduced Bill C-25, *An Act to amend the Proceeds of Crime (Money Laundering) and Terrorist Financing Act and the Income Tax Act and to make a consequential amendment to another Act*.[32] It received Royal Assent on December 14, 2006 and represents one of the most substantial pieces of anti-terrorism legislation since 2001. Some of the most important amendments in Bill C-25 that are applicable to charities and their legal counsel are amendments that will: (1) bolster client identification, record-keeping and reporting measures applicable to financial institutions and intermediaries; (2) allow the Financial Transactions and Reports Analysis Centre of Canada ("FINTRAC") to disclose additional information to both foreign and domestic law enforcement and intelligence agencies, and to make disclosures to additional agencies; (3) allow CRA to disclose to FINTRAC, RCMP and the Canadian Security Intelligence Service information about charities, including identifying information of the charities' directors and officers suspected of being involved in terrorist financing activities; and (4) exempt lawyers from reporting obligations under the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act*.[33] The Federation of Law Societies will likely reach an accord to voluntarily undertake professional standards to combat money laundering and terrorist financing. These amendments would increase the level of information sharing and collection among virtually all federal agencies that would potentially investigate or bring allegations and charges against charities and their directors and officers. These amendments also highlight the increasing focus on, and investigation of, charities and their possible links to terrorism.

2. Interim Report on *Anti-terrorism Act* Issued

On October 23, 2006, the Standing Committee on Public Safety and National Security recommended that two clauses contained in Canada's *Anti-terrorism Act*[34] that were to expire on December 31, 2006, should be extended for a further five years, and subjected to another review at that time. The clauses

[31] For more information, see Terrance S. Carter and Sean S. Carter, "Unprecedented Due Diligence Standards Emerge for Charities Internationally" in *Anti-Terrorism and Charity Law Alert* No. 9 (July 17, 2006) and Terrance S. Carter, "Canadian Charities: The Forgotten Victims of Canada's Anti-Terrorism Legislation" in *Anti-Terrorism and Charity Law Alert* No. 10 (September 20, 2006).
[32] Parliament of Canada, Bill C-25, online: www2.parl.gc.ca/HouseBills.
[33] 2000, c. 17.
[34] 2001, c. 41.

deal with investigative hearings and preventive detentions. The committee also recommended that the investigative hearing clause be amended so that it could only be used "when there is imminent peril that a terrorist offence will be committed." Two members of the committee submitted a dissenting opinion, suggesting that the clauses should only be renewed for three years. The two dissidents agreed with the amendment to the investigative hearing clause. A final report is required to be tabled no later than December 22, 2006, but was not available at the time of writing.

E. RECENT CASE LAW AFFECTING CHARITIES

1. Meaning of Charity and Gift

a) Court Decision Concerning the Requirements of a Gift[35]

On March 24, 2006, the Tax Court of Canada released a decision concerning gifts, *Benquesus et al. v. The Queen*.[36] In 1997, Mr. Benquesus transferred funds to a charitable foundation in Ontario. In a letter from Mr. Benquesus to the foundation accompanying the funds, he indicated that he was transferring the funds on behalf of his four children as interest-free loans, and that should the children require the funds, the foundation was to repay it. The letter further indicated that should the children forgive the loans, the foundation should then treat them as donations. In 1999, the children forgave part of the loan and charitable receipts were issued to the children by the foundation for the amounts forgiven. In reassessing the children's tax returns, CRA disallowed the children's charitable donation tax credits claimed for the forgiven loans. At issue was whether the father gifted the funds to the children, leaving it up to them to decide how much to donate to the foundation, or whether the father made the donations himself and transferred the donation credits to his children. After reviewing the three requirements for a valid gift at common law (*i.e.*, an intention to donate, acceptance of the gift by the donee, and delivery of the gift to the donee), the court found that all three requirements were met and found that Mr. Benquesus did gift the funds to the children and that it was up to the children to decide how much to donate to he foundation.

[35] T.L.M. Man, *Charity Law Update* (April 2006), online: www.carters.ca/pub/update/charity/06/apr06.pdf.
[36] 2006 TCC 193.

b) Amateur Sport Organizations Precluded from Attaining Charitable Status[37]

On April 5, 2006, in *A.Y.S.A. Amateur Youth Soccer Association v. Canada Revenue Agency*,[38] the Federal Court of Appeal ("FCA") released a decision with respect to the refusal of an application to register the appellant as a charitable organization. The purposes of the organization were to promote amateur youth soccer and offer youths the opportunity to develop pride in their ability and soccer skills. The appellant's main argument focused on the language in the Ontario court decision, *Re Laidlaw Foundation*,[39] which held that the promotion of amateur sport involving the pursuit of physical fitness is a charitable purpose. The appellant argued that since the common law in Ontario recognizes the promotion of amateur sport as a charitable purpose and the proposed activities are confined to Ontario, the law of Ontario should apply to the determination of its charitable status. The FCA held that there was no need to have recourse to the common law of Ontario since the ITA provides for the tax status of the appellant which precludes the possibility of it being registered as a charitable organization. In providing for the status of a registered Canadian amateur athletic association in 1972, "Parliament must have been taken to have been aware that no association which has, as its main purpose, the pursuit of amateur sport, could qualify as a charity under the common law, and hence, under the Act." The scheme of the ITA precludes the possibility of an amateur sport organization being registered as a charity, and only permits the separate registration of Canadian amateur athletic associations where they operate on a nation-wide basis. On September 21, 2006, the Supreme Court of Canada granted leave to appeal. At the time of writing, the appeal has not been inscribed for hearing.[40]

c) Promotion of "Ethical Tourism" Not Considered Charitable[41]

On October 24, 2006, the Federal Court of Appeal ("FCA") released its decision in *Travel Just v. Canada Revenue Agency*,[42] which represents an important decision concerning what is considered to be charitable at common law. This case involved the refusal by CRA to register a charity with the object "to create and develop model tourism development projects that contribute to the

[37] K.J. Cooper, *Charity Law Update* (April 2006), online: www.carters.ca/pub/update/charity/06/apr06.pdf, and *Charity Law Update* (September 2006), online: www.carters.ca/pub/update/charity/06/sep06.pdf.
[38] 2006 F.C.A. 136.
[39] (1984), 13 D.L.R. (4th) 491 at 506 and 523-24 (Ont. H.C.J.).
[40] [2006] S.C.C.A. No. 206.
[41] For more information, see Karen J. Cooper and Terrance S. Carter, "Promotion of Ethical Tourism Not Considered Charitable" in *Charity Law Bulletin* No. 106 (December 19, 2006).
[42] [2006] F.C.J. No. 1599.

realization of international human rights and environmental norms." The FCA concluded that the organization's objects were "vague and subjective" and were not sufficiently analogous to purposes already recognised by the Courts under the fourth category of charity: other purposes beneficial to the community. In addition, the language left open the possibility of the organization financing and operating luxury holiday resorts, activities with a strong commercial and/or private benefit aspect. The FCA also indicated that there no evidence of a connection with Québec, noting that the issue of whether an organization is charitable for the purposes of the ITA is likely a public law concept rendering the private law of Québec irrelevant, thus avoiding a decision on this issue.

2. Regulation of Charities

a) CRA Granted Order to Require Disclosure of Donor List[43]

In *All Saints Greek Orthodox Church v. Minister of National Revenue*,[44] a decision released on March 22, 2006, the Federal Court of Canada (the "Federal Court") considered an application by CRA for an order authorizing it to require that the Church furnish a list of all persons who made donations to it of comic books and trading cards. CRA had already obtained the information during the course of an audit of the charity but for it to be able to use the information in the context of a tax avoidance investigation related to donors, CRA would need to be granted a court order pursuant to section 231.2 of the ITA. While the court order was granted to CRA, since CRA had already used the names provided to it in the context of the charity audit to reassess many of the donors without initially advising the court of this fact, the Federal Court penalized CRA by ordering solicitor and client costs.

b) Court Decision Concerning Agency Relationships Outside of Canada

On March 28, 2006, in *Bayit Lepletot v. Minister of National Revenue*,[45] the Federal Court of Appeal ("FCA") considered whether a Canadian charitable organization was carrying on its own charitable activities when it funded an orphanage in Israel of the same name through an agent. The agent requested funds from the appellant, who approved the request, transferred the funds to the agent and then the agent disbursed them to the orphanage. The FCA noted that the agent was

[43] But see *Redeemer Foundation v. MNR*, *infra* note 50.
[44] [2006] F.C.J. No. 481.
[45] 2006 FCA 128.

part of the "Directorate in residence" of the orphanage and that he presumably exercised the same control over its operations, but that there was no evidence as to what extent. Moreover, there was no evidence that he exercised any control over the activities of the orphanage in his capacity as agent of the appellant. The FCA affirmed the position that CRA has taken over the years with respect to agency relationships: it must be shown that the agent is actually carrying on the charitable works of the Canadian charity and the activities of the agent must be subject to the Canadian charity's control.

c) Donation Tax Shelter Valuations[46]

On April 20, 2006, the Supreme Court of Canada dismissed an application for leave to appeal (without reasons)[47] from the Federal Court of Appeal ("FCA") decision in *Klotz v. Canada*,[48] which had affirmed the Tax Court of Canada's ruling[49] in connection with donation tax shelter valuations. At trial, Associate Chief Justice Bowman found that the best evidence of fair market value was the very transaction through which the taxpayers purchased art from the promoter. Mr. Klotz was one of 660 people who acquired limited edition prints which were immediately donated to prescribed colleges and universities under the ITA. The average cost of the prints was $300 yet the receipt that was issued was based on an average fair market value per print of about $1,000, which the Tax Court of Canada found to be unrealistic. The FCA agreed with the Tax Court Judge in finding "that the best evidence of the fair market value of the prints was the price paid by the taxpayer – that is $75,000."

d) CRA Audits of Registered Charities

On October 10, 2006, in *Redeemer Foundation v. Minister of National Revenue*,[50] the Federal Court of Appeal ("FCA") considered the process CRA must follow to obtain the names of donors during the course of an audit of a registered charity. After having audited a charity that operated a "forgivable loan program," CRA obtained from the charity, upon a verbal request, donor information with which CRA contacted the donors to advise them that they would be reassessed to

[46] For more information, see Karen J. Cooper and Terrance S. Carter, "Beware of Donation Tax Shelter Valuations" in *Charity Law Bulletin* No. 87 (February 8, 2006).
[47] [2005] S.C.C.A. No. 286.
[48] [2005] F.C.J. No. 754.
[49] [2004] T.C.J. No. 52.
[50] 2006 FCA 325.

disallow the donation tax credits claimed for their donations to the charity. After providing the list of donors to CRA, the Foundation brought an application in the FCA for judicial review of the auditor's request on the basis that the auditor should have followed the process provided for in subsection 231.2(2) of the ITA requiring prior judicial authorization. The initial decision of the FCA declared that the actions of the auditor were unlawful and ordered that the reassessments of the donors be vacated. This decision was appealed by CRA, and the FCA overturned the initial decision on the basis that there were other provisions in the ITA authorizing the auditor to make the request that he did and to use that information for the purposes of subsequent tax assessments. Specifically, subsection 231(2) of the ITA requires charitable organizations to maintain certain records, including duplicates of all receipts, and section 231.1 of the ITA authorizes an auditor to examine the organization's books and records. The FCA concluded that if an auditor is entitled to obtain the information and compile the list of donors by his own examination of the books and records of the organization, there is no reason for the auditor to have to resort to the process established in subsection 231.2(2) of the ITA.

e) *Khawaja* Decision Affords Little Relief for Charities[51]

Since the first wave of anti-terrorism legislation was declared in force in late 2001, its impact has loomed large over Canadian charities and their foreign operations. The case of Mohammad Momin Khawaja, the first person to be charged under the core "terrorism" provisions in Part II of the Criminal Code (the "Code"),[52] presented essentially the first chance to judicially review this controversial law. In *R. v. Khawaja*,[53] Mr. Justice Rutherford of the Ontario Superior Court of Justice struck down a portion of the definition of "terrorist activity" in the Code that dealt with purpose and motive. The decision, released on October 24, 2006, was met with mixed reviews by anti-terrorism legal commentators, some of whom initially heralded the case as a powerful blow to draconian legislation. However, the impact upon Canadian charities, which are particularly vulnerable to the sweeping "facilitation of terrorist activity" provision in section 83.19 of the Code, is not encouraging. The decision offers charities little relief from their susceptibility to unintentional contravention of the law because the court decided to uphold the legislation

[51] For more information, see Terrance S. Carter and Sean S. Carter, "*Khawaja* Decision Offers Little Relief for Charities" in *Anti-Terrorism and Charity Law Alert* No. 11 (December 20, 2006).
[52] *Supra* note 11.
[53] [2006] O.J. No. 4245.

notwithstanding its breadth and the limited *mens rea* requirement concerning the definition of "facilitation." As a result, there are significant risks that a charity involved in conducting aid or humanitarian programs in a conflict area could unwittingly be found to still have facilitated a terrorist activity.

3. Freedom of Religion

a) Supreme Court of Canada Gives Strong Endorsement to Freedom of Religion[54]

In a decision rendered on March 2, 2006, the Supreme Court of Canada (the "Court") sent a strong message that Canada's public education institutions must embrace diversity and develop an educational culture respectful of the right to freedom of religion. In *Multani v. Commission scolaire Marguerite-Bourgeoys*,[55] the Court confirmed the right of an orthodox Sikh student to wear his ceremonial dagger at school. The Court concluded that the *Canadian Charter of Rights and Freedoms*[56] establishes a minimum constitutional protection for freedom of religion that must be taken into account by the legislature and by administrative tribunals. Safety concerns must be unequivocally established for the infringement of a constitutional right to be justified. As such, the Court gave new guidance to administrative bodies dealing with Charter issues, declaring that administrative bodies must apply the principles of constitutional justification when a Charter right has been infringed.

[54] For more information, see Terrance S. Carter and Anne-Marie Langan, "Supreme Court of Canada Gives Strong Endorsement to Freedom of Religion" in *Church Law Bulletin* No. 17 (March 16, 2006).
[55] [2006] S.C.J. No. 6.
[56] *The Constitution Act, 1982*, being Schedule B to the *Canada Act 1982* (U.K.), 1982, c. 11.

F. CONCLUDING COMMENTS

The year 2006 brought a number of significant changes to charitable organizations which will be of particular concern for their directors and officers, as well as for their legal counsel. The number of legislative changes, CRA policy initiatives and rulings that have occurred during 2006, as well as the release of numerous significant decisions from the courts, underscore how complicated the law pertaining to charitable organizations has become in Canada. It is therefore important for board members, executive staff and their professional advisors to keep abreast of developments in the law as they occur.

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