

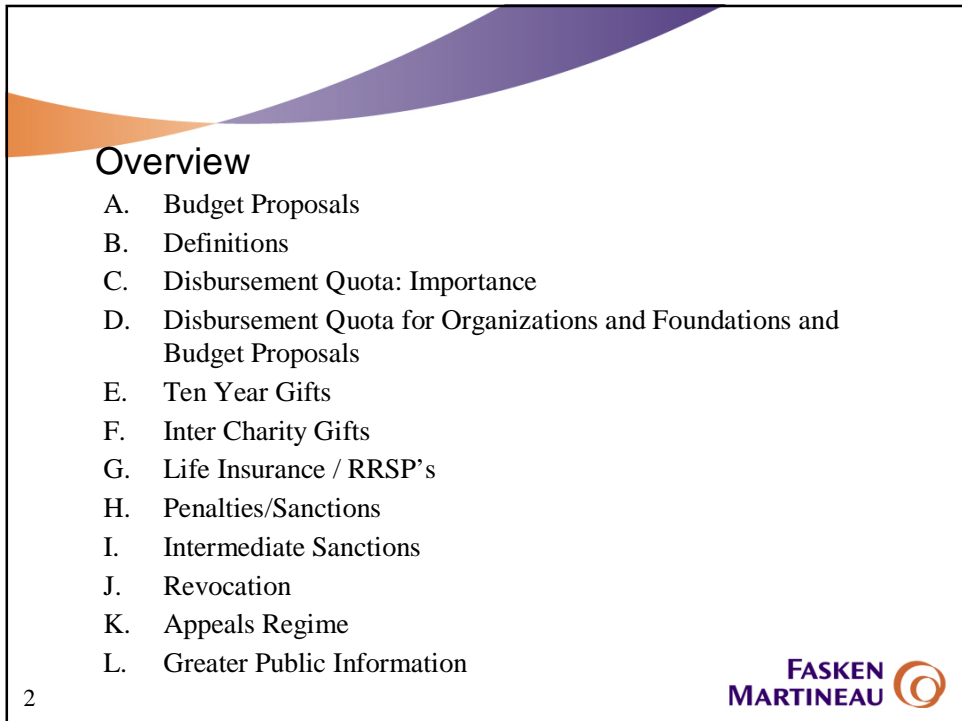


BUDGET PROPOSALS - MARCH 23, 2004

- Disbursement Quota
- Intermediate Taxes/Sanctions
- Appeals

**FASKEN
MARTINEAU** 


MAY 5, 2004
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Overview

- A. Budget Proposals
- B. Definitions
- C. Disbursement Quota: Importance
- D. Disbursement Quota for Organizations and Foundations and Budget Proposals
- E. Ten Year Gifts
- F. Inter Charity Gifts
- G. Life Insurance / RRSP's
- H. Penalties/Sanctions
- I. Intermediate Sanctions
- J. Revocation
- K. Appeals Regime
- L. Greater Public Information

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A. Budget 2004 Proposals

- Most sweeping changes since 1983
- Major themes
 - new compliance regime
 - more accessible appeals regime
 - more transparency, greater accessibility
 - improvement to DQ rules

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B. Definitions (1)

- Charitable Organization
 - all resources devoted to own charitable activities
 - more than 50% of directors, officers, trustees deal at arms' length
- Charitable Foundation
 - operated exclusively for charitable purposes
 - generally act as conduits for distributing funds to charitable organizations
 - can be public or private
 - public foundation: where more than 50% of directors, trustees deal at arms' length and broad based contributions

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Definitions (2)

- Changes proposed in December 2002 and tabled in February 27, 2004 technical amendments to replace “contribution” test with “control” test in respect of charitable organizations and public foundations
- Rationale: to allow such charities to receive large donations without concern they may be characterized as private foundations with more stringent controls on activities and disbursement requirements
- Previous Test: where more than 50% of capital contributed by one donor, charity was classified as private foundation
- New Test: even if more than 50% of capital contributed by one donor so long as donor or donor group does not control the charity, it can still remain characterized as a public foundation/organization

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Definitions (3)

- What is the Disbursement Quota?
 - A prescribed amount a registered charity is required to disburse annually to maintain charitable status
- Purpose
 - to ensure charities use charitable funds on charitable activities/purposes
 - to discourage charities from spending excessive amounts on fundraising and from accumulating excessive funds
- Different disbursement quota for the 3 categories of charity: charitable organizations, public foundations, private foundations

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C. Disbursement Quota: Importance

- Important for Donors and Donees
- Will affect consideration of
 - Nature of property gifted
 - Nature of restrictions imposed
- Before Budget Proposals: Source of gift and description of proposed charitable recipient

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D.1 Disbursement Quota Pre Budget Calculation

- All Charities
 - Received donations
 - 80% of prior year's received donations
 - exceptions - 10 year gift
 - bequests
 - excluded when received
 - 80% included when spent
- Foundations:
 - 4.5% test ("investment assets")
 - gifts from other charities in prior year
 - public foundation - 80%
 - private foundation - 100%
 - exception "Specified gifts"

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2 Disbursement Quota Post Budget Calculation (Proposal)

- All Charities
 - Received donations
 - 80% of prior year's received donations
 - exceptions - bequests
 - 10 year gifts (endorsements)
excluded when receives
included when spent (reduced by lesser of 80% of gain and 3.5% amount)
 - 100% of endowments gifted to other charities
- Gifts from other registered charities - prior year
 - organization and public foundation - 80%
 - private foundations - 100%
 - exceptions - specified gifts
 - endowments
- 3.5% test (investment assets)

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E. 10 Year Gifts

- Disbursement quota rules
 - not included in DQ when received
 - 80% brought back into DQ when spent
 - 4.5% (budget proposal 3.5%) of investment value included in DQ
- CRA documentary requirements
- Trust or direction
- Disbursement quota issues
 - if encroach on capital during 10 year hold period
 - if encroach on capital after 10 year hold period
 - 4.5%, (Budget proposal: reduce to 3.5%) disbursement quota still applies


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E. 10 Year Gifts

- Capital gains not considered “income”
- Inter charity transfers of 10 year gifts

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E. 10 Year Gifts (Budget Proposals)

- Budget Proposal to soften cumulative effect of the application of 3.5% test and 80% test to 10 year gifts (“endowments”)
- New Rule: lesser of 80% of the capital gain realized on disposition and 3.5% of the value of the property held
- Concerns
 - 1 two DQ regimes for 10 year gifts?
 - a Original capital - will current rules apply?
 - b Realized capital gain - new rule?
 - 2 Encroachment on 10 year gift without triggering capital gain - current rule applies?

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F. Inter Charity Gifts When Does the Issue Arise?

- Donor wishes to satisfy charitable pledge by gift from private foundation to public foundation
- Private foundation wishes to wind up and transfer its property to community foundation
- Organization wants to set up parallel foundation for asset protection purposes

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F. Inter Charity Gifts: Current Rules

- Gifts to Foundation: Foundation must disburse 80% (Public) or 100% (Private) irrespective of whether receipt issued
- Exception:
 - Specified gifts
- Gifts to charitable organization:
 - not subject to DQ of organization

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F. Inter Charity Gifts: Budget Proposals

- 80% DQ will also apply to Inter Charity gifts received by organization
- Specified gifts will continue to be an exception to this rule
- Facilitation of Inter Charity gifts of 10 year gifts (“endowment”) by treating endowment as having been received by transferee charity directly from donor

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F. Specified Gifts

- Gifts from one charity to another designated by donor charity as a specified gift will not count toward satisfaction of DQ of donor charity
- Donee charity does not have to include amount of gift in its DQ
- Important for donee Foundation to make inquiries
- Post Budget - also important for donee Organization to make inquiries
- Also important for Organization to ask because specified gifts not included in income of Organization which can't disburse more than 50% of its income to qualified donees

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G. Life Insurance/RRSP Gifts

- Currently receipt of life insurance proceeds/RRSPs does not appear to be caught by disbursement quota rules
- Budget proposals: treat such receipts as analogous to 10 year gifts (“endowments”)

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H. Penalties/Sanctions

- Pre-Budget - only sanction available to CRA - Deregistration
- Sanctions Introduced in Budget
 - monetary penalties
 - suspension of tax receipting privileges

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I. Intermediate Sanctions

- Tax at rates up to 100% on gross revenues from prohibited business activities
 - private foundation - any business
 - public foundation/charitable organization - unrelated business
 - foundation - acquiring control with a corporation
- Suspension of tax receipting privileges
- Monetary Penalties
 - late filing
 - failure to file
 - issuing incomplete receipts
 - 105-110% of amounts of undue personal benefit or restricted gifts

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I. Intermediate Sanctions (cont'd)

- Tax
 - 125% of amount receipted if no gift or receipt contains false information
 - suspension of receipting privileges if amount exceeds \$20,000
 - 10% of amounts transferred among charities to delay DQ requirement
- Sanctioned Charity
 - can transfer amount of tax/penalty to another (arms length) charity rather than CRA if tax/penalty >\$1000

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J. Revocation

- expedited revocation powers and revocation tax collection where registration obtained with false, misleading information
- Revocation Tax
 - in lieu of paying revocation tax to CRA
 - equivalent amount can be paid to eligible transferees
i.e. other registered charities dealing at arms length

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K. Appeals Regime

1. Internal Reconsideration Process

- existing internal objection review process will be extended to notices of decision re denial of application for charitable status, revocation, amendment of registration, designation of charity as charitable organization, private or public foundation or imposition of taxes/penalties
- notice of objection within 90 days of CRA notice of result of review in writing
- no appeal to court unless objection route taken

2. External Review Process

- appeals of taxes and penalties Tax Court
- appeals of refusal to register or deregistration Federal Court of Appeal

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L. Additional Information Available to Public

- Financial information registration annulment correspondence
- decisions re objections
- material filed and CRA responses re requested exemption, authorization, special status
- Sanction letters

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- Increased website information
 - reasons for registration decision
 - policies
 - procedures
 - research database
- Additional Information required on official tax receipts
 - name and website address of CRA
- Charities Advisory Committee
 - greater impact by charities into shaping of tax rules affecting charities

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