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HALTON REGION & COMMUNITY PARTNERS PRESENT...

“Leadership Matters: Building Your Legal Know How”

Burlington – September 9, 2010

The Implications of the New CRA Fundraising Guidance for Charities

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1. OVERVIEW OF PRESENTATION

- Background
- Practical Explanation of CRA's Fundraising Guidance One Year Later
- Ongoing Concerns
- Possible Strategies to Consider

2. BACKGROUND

- Significant public and media pressure has been placed on CRA over the last few years to more fully disclose internal guidelines on fundraising
- The Guidance was developed in response to a growing demand from the media and the general public for more accountability from charities concerning fundraising
- Fundraising has now taken on a greater role with regards to the regulation of charities because of the DQ reform in the March 2010 Federal Budget

- However, there has been little consistency in how to report cost allocation for fundraising in the past
- CRA now wants to educate the sector and achieve consistency of inputs and transparency concerning fundraising
- On March 31, 2008, CRA released its proposed Policy on Fundraising for public consultation
- On June 26, 2008, CRA released a 30-page Background Information document explaining its proposed Policy on Fundraising

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- After public consultation, Guidance (CPS-028): Fundraising by Registered Charities (“Guidance”) was released on June 11, 2009, together with a 23 page Additional Information on the Guidance, which collectively need to be read as one document
<http://www.cra-arc.gc.ca/tx/chrts/plcv/cps/cps-028-eng.html>
<http://www.cra-arc.gc.ca/tx/chrts/plcv/cps/cps-028-ddneng.html#d1>
- For more information, see Charity Law Bulletin #169 “The Revised CRA Guidance on Fundraising: Improved But Still Challenging”, at <http://www.carters.ca/pub/bulletin/charity/2009/chv1b169.pdf>

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- There has been only limited response to the Guidance from the sector over the past year
- CRA is now seeking input from the sector and is expected to revise the Guidance likely sometime later in 2010
- CRA has advised that the Guidance does not represent a new policy position of CRA but rather provides information on the current treatment of fundraising under the ITA and the common law
- As such, the Guidance will have impact on current CRA audits, not just future audits

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- The Guidance is intended to provide general advice to registered charities only
- The Guidance applies to all registered charities, including foundations
- The Guidance applies to both receipted and non-receipted fundraising income
- Charities must still meet their other obligations, and in particular the disbursement quota (now only the 3.5% capital accumulation disbursement quota)

- 3. FUNDRAISING IS NOT CHARITABLE**
- All registered charities are required by law to have exclusively charitable purposes
 - CRA's position is that fundraising (either as a purpose or an activity) is not in and of itself charitable
 - As a result, CRA takes the position that direct fundraising costs cannot generally be reported as charitable expenditures on the T3010B
 - However, CRA states that fundraising activities which are appended to activities primarily directed at achieving a charitable purpose may be allocated between charitable and fundraising for purposes of reporting

- 4. WHAT IS FUNDRAISING?**
- Fundraising is an activity that involves any of the following:
 - “Solicitations of support” for cash or in-kind donations (including sales of goods or services to raise funds)
 - Research and planning for future solicitations of support
 - Other activities that are related to solicitations of support (e.g. efforts to raise the profile of a charity, donor stewardship, or donor recognition)

- Fundraising activities may be external activities (e.g. telemarketing, direct mail, putting on events, distributing information through the media or a charity's own publications)
- Fundraising activities may also be internal activities (e.g. researching prospective donors, hiring fundraisers, donor stewardship and recognition)
- Fundraising can be carried out internally by the charity itself (e.g. the charity's employees or volunteers) or externally by someone acting on its behalf (e.g. third party fundraisers)

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- Fundraising may include a single action, such as an advertisement, or a series of related actions, such as a capital campaign
- Fundraising for the purpose of the Guidance (both expense and income) does not include:
 - Requests for funding from governments
 - Requests for funding from other registered charities
 - Recruitment of volunteers
 - Related businesses
 - Fundraising to support terrorism (which is prohibited)

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- Donor recognition, as a form of solicitation of support, includes gifts or acknowledgements to thank donors, unless of nominal value (i.e. the lesser of \$75.00 or 10% of the value of the donation)
- Donor stewardship, as a form of solicitation of support, occurs when a charity invests resources in relationships with past donors to prompt additional gifts, such as providing past donors with access to privileges not available to others, (e.g. an invitation to a private reception)

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- **Sale of goods or services is always a solicitation of support except:**
 - **Where it serves the charities beneficiaries to fulfill a charitable purpose and is sold on a cost recovery basis, or**
 - **Is a related business (see CRA Policy Statement on Related Business)**
- **Membership programs will be considered to be a solicitation of support where membership requires a donation to join or where there is extensive use of donation incentives or premiums to recruit members**

- 5. PROHIBITED CONDUCT**
- **The following types of conduct related to fundraising activities are prohibited and will be grounds for revocation of a registered charity's status, the possible imposition of sanctions or other compliance actions, or for denial of charitable registration**

- a) **Conduct that is illegal or contrary to public policy**
 - **Activities that are criminally fraudulent**
 - **Violates federal or provincial statutes governing charitable fundraising, charitable gaming, the use of charitable property, or consumers protection**
 - **Failure to take adequate care to avoid involvement in a third party tax shelter scheme**
 - **Failure to keep books and records to verify donations to the charity**

- Activities that are contrary to recognized public policy
- Misrepresentation to the public about the cost of fundraising
- b) Conduct that is a main, or independent purpose of the charity (even if only secondary)
 - i.e. Fundraising becomes a collateral purpose
- c) Conduct that results in more than an incidental proportionate private benefit to individuals or corporations
 - e.g. A fundraising arrangement where a fundraiser enjoys a benefit exceeding fair market value

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- d) Conduct that is deceptive
 - A charity is to ensure representation made by it is a fair, truthful account and complete
 - A charity is responsible for misleading statements whether the charity's conduct is intentional or negligent
 - A charity must not misrepresent
 - o What charity will receive the donation
 - o The geographic area where the charity operates and the amount and type of work
 - o The percentage of funds that will go to charitable work

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6. PROCESS FOR ALLOCATION OF FUNDRAISING EXPENSES

- In general, charities are to report on their T3010B as fundraising expenditures all costs related to any activity that includes a solicitation of support, or is undertaken as part of the planning and preparation for future solicitations of support, unless it can be demonstrated that the activity would have been undertaken without the solicitation of support

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- This does not apply to asking for funding from governments or other charities
- However, it does apply to marketing and sale of goods or services not within the charities own charitable purposes, whether or not donation receipts are issued
- In order to demonstrate that an activity would have been undertaken without solicitation of support, a charity must demonstrate that it satisfies either Test A (The “Substantially All Test”) or Test B (The “Four Part Test”)

- Test A: The “Substantially All Test”
 - Where Test A (“Substantially All Test”) is met, all costs of the activity may be allocated as non-fundraising expenditures on the T3010B return, either as charitable, administrative or political expenditures
 - The “Substantially All Test” is met where “substantially all” of the activities advance an objective other than fundraising
 - “Substantially all” is considered to be 90% or more

- Generally, the determination will be the proportion of the fundraising content to the rest of the activity, as well as the resources devoted to it and prominence
- “Resources” include the total of a charity’s financial assets, as well as everything the charity can use to further its purposes (e.g. its staff, volunteers, directors, premises, and equipment)
- Amount of resources devoted to an activity is determined by the content, prominence given to the material, and costs associated with carrying out the activity

- **Test B: The “Four Part Test”**
 - Where Test B (“Four Part Test”) is met, a portion of the costs for the activity may be allocated on the T3010B return as non-fundraising expenditures as either charitable, administrative or political, and a portion as fundraising expenditures
 - The “Four Part Test” is met where the answers to all of the following four questions is “no”

Question 1. Was the main objective of the activity fundraising?

- a) Do the resources devoted to the fundraising component of the activity indicate that the main objective is fundraising?
- b) Does the nature of the activity indicate that the main objective is fundraising?

Content: Sometimes considered to be fundraising

- It may be hard to separate initiatives that are carried out to fulfill a charity’s purposes from a charity’s fundraising activities
- CRA will therefore look at the following features to see if there is a distinct objective other than fundraising and to assess how much of the content relates to that objective:

- (i) Advancing the programs, services, or facilities offered by the charity
- (ii) Raising awareness of an issue
- (iii) Providing useful knowledge to the public or the charity's stakeholders about the charity's work or an issue related to that work
- (iv) Being transparent and accountable for its practices by providing information about its structure, operations, or performance to the public or its stakeholders

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- Question 2. Did the activity include ongoing or repeated requests, emotive requests, gift incentives, donor premiums, or other fundraising merchandise?**
- a) Are solicitations ongoing or repeated?
 - b) Are requests emotive?
 - c) Are gift incentives, premiums, or other fundraising merchandise offered
- Question 3. Was the audience for the activity selected because of their ability to give?**
- Question 4. Was commission-based remuneration or compensation derived from the number or amount of donations used?**

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Exception:

- Even if an activity would not have been undertaken without solicitation of support, charities may still be allowed to allocate a portion of the costs other than to fundraising if the activity furthers its charitable programs
 - e.g. Charity promotes an event where revenues are based on the charity's work with its beneficiaries, such as a concert performance performed by autistic children

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7. EVALUATION OF FUNDRAISING ACTIVITIES

- **CRA recognizes that the charitable sector is very diverse and fundraising efforts will vary between organizations**
- **CRA will look at a number of factors to evaluate a charitable fundraising activity**
- **CRA has identified four types of factors to assist with the assessment**
 - a) **Fundraising Ratio and Approach of CRA**
 - b) **Basic Considerations**
 - c) **Best Practice Indicators**
 - d) **Area of Concern Indicators**

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a) Fundraising Ratio and Approach of CRA

- **One factor is the ratio of fundraising costs to fundraising revenue calculated on an annual basis**
- **Fundraising ratio provides a general guidance only and is not determinative on its own**
- **Fundraising ratio is totally distinct from the disbursement quota (consisting of 3.5% DQ but no longer the 80/20% DQ), although elements of the DQ may overlap in the ratio**

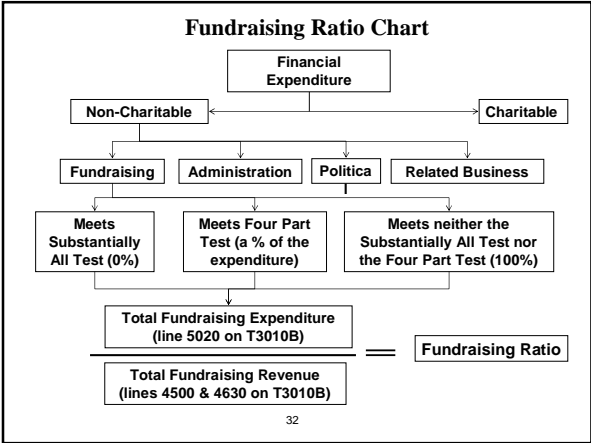
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- **Fundraising revenues include amounts reported in the T3010B on line 4500 (receipted donations) and line 4630 (all revenue generated as a direct result of fundraising expenses, which would include sponsorship funds)**
- **Fundraising expenditures include amounts reported on line 5020 as fundraising expenses in accordance with the Guidance**

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- The fundraising ratio will place a charity in one of three categories
 - Under 35%: Unlikely to generate questions or concerns by CRA
 - 35% and above: CRA will examine the average ratio over recent years to determine if there is a trend of high fundraising costs requiring a more detailed assessment of expenditures
 - Above 70%: This level will raise concerns with CRA. The charity must be able to provide an explanation and rationale for this level of expenditure, otherwise it will not be acceptable

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- b) **Basic Considerations that CRA will look at in assessing a charity's fundraising activities**
- The size of the charity which may have an impact on fundraising efficiency, i.e. revenues under \$100,000
 - Causes with limited appeal which could create particular fundraising challenges
 - Donor acquisition and planned giving campaigns which could result in situations where the financial returns are only realized in later years

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- c) **Best Practices Indicators that decrease the risk of CRA finding unacceptable fundraising**
 - **Prudent planning processes**
 - e.g. Where the charity researches anticipated costs and revenues
 - **Appropriate procurement processes**
 - e.g. Solicit bids from three or more potential suppliers or issuing RFP's
 - **Good staffing processes**
 - e.g. Setting compensation that is appropriate compared to other employees of the charity in light of respective responsibilities
 - e.g. Should avoid performance evaluation based solely or excessively on performance or results

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- **Ongoing management and supervision of fundraising practice**
 - e.g. Establish and implement a fundraising policy
- **Adequate evaluation processes**
 - e.g. At a minimum regularly assess its fundraising performance compared to CRA Guidance
- **Use made of volunteer time and volunteer services or resources**
 - Demonstrates a commitment to minimize the expenditure allowable for the fundraising activity

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- **Disclosure of fundraising costs, revenues and practice (including cause-related or social marketing arrangements)**
 - CRA expects charities to provide complete public disclosure for all fundraising costs and revenue
 - Generally greater disclosure required for solicitation to the public than to members
 - The higher the cost for a fundraising activity, the more there is a need for disclosure
 - Information must be accessible (e.g. the web and annual reports) and accurate, (e.g. the best information available)

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▪ A charity may need to consider disclosing information before, during and after a fundraising initiative, which information might include:

- Estimated fundraising costs and revenues in its annual budget
- Whether fundraisers are receiving commission or other payment based on the number or amount of donation
- The general terms of the fundraising contract, including the method of compensation and anticipated costs and revenues

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- How internal fundraisers are assessed and compensated
- The costs and revenues for specific types of fundraising or campaigns within a fiscal period (after completion)

– Cause-related ventures are not subject to scrutiny by CRA, provided that more than 90% of the costs are borne by a non-charitable partner and all costs and revenues are adequately disclosed (excluding costs of intellectual property)

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d) Areas of Concern Indicators that could cause CRA to further review a charity's fundraising activities

- Sole-sourced fundraising contracts without proof of fair market value
 - May lead to excessive and disproportionate private benefit
- Non-arm's length fundraising contracts without proof of fair market value
 - May result in undue benefit
- Fundraising initiatives or arrangements that are not well-documented
 - e.g. No minutes of board meeting or other meetings where fundraising contracts were approved
 - e.g. No documentation on any procurement processes

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- Fundraising merchandise purchases that are not at arms length, not at fair market value, or not purchased to increase fundraising revenue
 - e.g. Must be able to show that gift incentives or donor premiums will result in increased revenue
- Activities where most of the gross revenues go to contracted non-charitable parties
 - e.g. Must be able to show steps to determine the fair market value

- Commission-based fundraiser remuneration or payment of fundraisers based on amount or number of donations
 - Raises concern about disproportionate or excessive private benefit
 - e.g. Compensation based on calls completed or contacts made is preferable
- Total resources devoted to fundraising exceeding total resources devoted to program activities
 - Otherwise concern by CRA that fundraising may become a collateral purpose
 - Where discrepancies in costs of different functions occur, the cost of a particular function should be shown to be reasonable, but merely showing that costs of fundraising are at FMV is not sufficient

- Misrepresentations in fundraising solicitations or disclosures about fundraising or financial performance
 - e.g. Misrepresentation may result from either intentional conduct or an omission of information that creates a false impression
- Each of the above factors are explained in considerably more detail in the Guidance and must be carefully studied, particularly with regards to expectations by CRA concerning disclosure

8. ONGOING CONCERNS

- Many of the requirements, factors and criteria contained in the Guidance are open to subjective interpretation and accordingly, there could be inconsistencies in the administration of the Guidance and resulting CRA audits of charities
- The fundraising ratio is based on a ratio of fundraising costs and revenue calculated on an annual basis, but does not take into account the fact that the nature of fundraising activities of charities varies widely – What is needed is a rolling average approach

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- The Guidance is complicated and may be difficult for charities to understand and comply with at a practical level, particularly the Test B
- Although the initial threshold level of 35% in the ratio is generous, donors and the public may have difficulty in accepting this as an appropriate level. It would have been better if Test B was not as limiting in order to be able to allocate expenditures to categories other than fundraising
- There is potential confusion concerning charitable gaming and lotteries by requiring that such items are included in fundraising income and expenses but then administratively ignoring them because of overriding provincial jurisdiction

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9. POSSIBLE STRATEGIES TO CONSIDER

- Corporate sponsorship can generally be included as fundraising income under line 4630 on the T3010B and therefore possibly improve the fundraising ratio
- Greater focus will be required on disclosure of fundraising costs, revenues and practices which may impact the ability to attract donors unless there is appropriate education of donors
- However, not clear whether disclosure is to be done after each fundraising campaign in addition to doing so for the fiscal year

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- It may be possible to reduce fundraising expenses for a charity by utilizing an arms length parallel not-for-profit corporation to operate the fundraising event on a cost recovery basis, with the charity being the intended recipient of charitable donations
- The fundraising ratio is a function of line items on the T3010B, so it is very important that the board of a charity review and approve the T3010B before it is filed with CRA and posted on the CRA website

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