
DIRECTORATE ANNOUNCES REFORMS TO THE CHARITABLE REGULATORY ENVIRONMENT

*By Terrance S. Carter, B.A., LL.B., Trade-mark Agent
Assisted by Nancy E. Claridge, B.A., M.A., LL.B. Candidate*

A. INTRODUCTION

Responding to initiatives announced in the 2004 Federal Budget which outline the most significant reform of the charities regulatory framework in more than 20 years, the Charities Directorate (the "Directorate") of Canada Revenue Agency (the "CRA"), released *Registered Charities Newsletter No. 19* (the "Newsletter") (available at <http://www.cra-arc.gc.ca/E/pub/tg/charitiesnews-19/README.html>). The initiatives brought forward in the 2004 Federal Budget and this Newsletter are intended to benefit the charitable sector by continuing to build public trust and confidence in charities and the CRA as a regulator. This *Charity Law Bulletin* (the "*Bulletin*") reviews the reforms outlined in the Newsletter.

B. NEW CHARITY REPRESENTATIVE POSITION CREATED

Beginning May 3, 2004, the Charities Representative will be a new resource person, acting independently to address issues that could not be dealt with through existing channels at the Directorate. The Charities Representative will deal with:

- complaints about the level and quality of service;

Main Office Location

211 Broadway, P.O. Box 440
Orangeville, Ontario, Canada, L9W 1K4
Tel: (519) 942-0001 Fax: (519) 942-0300

Toll Free: 1-877-942-0001

www.carters.ca

www.charitylaw.ca

Toronto Meeting Location

Toronto Dominion Bank Tower, Suite 4200
TD Centre, Toronto, Ontario, Canada
(by appointment) Tel: (416) 675-3766

- service standards that were not met;
- clients who do not feel they were treated in a fair, transparent manner;
- information requests from charities who need help to voluntarily comply; and
- other complaints of a general nature.

The Newsletter notes that this resource person should only be used after first trying to resolve issues through the Directorate's Client Assistance section, the individual dealing with the charity's file or audit, or the appropriate Manager. The Charities Representative will not be in a position to reverse application decisions or other technical determinations. This position is for a one-year trial period.

C. CHARITIES ADVISORY COMMITTEE

Then Minister of National Revenue, Stan Keyes, announced the creation of the Advisory Committee on matters related to the CRA's responsibility for the regulation of the charitable sector. The twelve-member Advisory Committee will provide a vehicle to: identify and discuss emerging issues and trends regarding regulatory oversight of the charitable sector; review compliance patterns and recommend enhancements; discuss the CRA's administrative policy development; and provide advice on developments and trends in the sector that may impact CRA policies and programs. The members of the Advisory Committee, who are appointed for a four-year term, are: Lois Hollstedt, Gordon Floyd, Laird Hunter, Bob Wyatt, Tad Brown, Catherine Cole, Carol Fitzwilliam, Kimberley Turner, Terrance Carter, Margaret Mason, Hilary Pearson, and Catherine Rowsell.

D. FIVE AREAS OF REFORM

After a decade of discussions concerning the role of the charitable sector as a partner of government and in communities, and the role of the federal government to support this, the CRA has now committed to focusing on the following five areas of reform.

1. Improving services for charities and the public

The CRA will be increasing the type and amount of information made publicly available, making it easier for charities to submit required information, and enhancing the communication methods that

charities and the public use to access this information. The type of information that will be available after the changes are introduced include:

- the names of charities that have been sanctioned under the new system;
- financial statements of charities filed with annual tax returns;
- letters relating to the grounds for the annulment of a charity's registration;
- the reasons for charity registration and revocation decisions;
- research used for decision-making; and
- information about special permissions or exemptions granted to individual charities.

The CRA will also expand its electronic services, enabling access to the following on-line:

- e-filing of annual returns;
- applications for registered status; and
- real-time interaction with CRA charity staff on issues including status inquiries, change of address, and information sessions.

2. Increasing public awareness and sector outreach

a) Public awareness

The CRA will soon be launching a campaign with the goal of increasing public awareness about the role of the CRA in regulating charities, giving greater confidence to donors that there is formal monitoring of charities, and encouraging Canadians to give to charitable causes in which they believe.

As part of this awareness campaign, the CRA will:

- raise its own profile as a reliable source of information about charities;
- educate donors about what they need to be aware of when giving to a charity, how to confirm the status of a charity, and how to make a complaint about a charity;

- improve public access to information about registered charities, in part by requiring that charities include contact information for the CRA on their receipts; and
- report annually to the public on regulatory activities related to registered charities.

b) Sector outreach

The CRA will expand its communication and educational activities to assist charities in understanding and following the rules and obligations associated with being a registered charity. In addition to the outreach campaign, the CRA will develop a Strategic Funding Program for education on charities regulation in the sector, by the sector. As well, the newly created Charities Advisory Committee will provide charities with a stronger voice in shaping the way in which charities are regulated.

3. Improving monitoring of charities – Introduction of intermediate sanctions

The 2004 Federal Budget noted that the harshness of the only penalty available to sanction infractions by charities – that of revoking charitable status – was inappropriate in many cases. The introduction of intermediate sanctions is intended to give the CRA a better alternative for dealing with minor infractions of already existing compliance requirements.

Through the new approach, the CRA will work with the charity when minor infractions are identified, entering into a compliance agreement to rectify the problem. These agreements will set out the concrete steps a charity must take to comply with the rules, as well as the consequences of continued infractions.

Revoking a charity's status will remain as the ultimate sanction for severe breaches of the *Income Tax Act* (the "Act"), including continued, repeated, or cumulative infractions. For less severe breaches of the Act, intermediate sanctions include small penalties, temporary suspension of receipting privileges, and partial loss of the tax-exempt status. Repeated infractions will result in escalating penalties.

4. Appeals process

Noting that there is currently no formal process for the internal review of decisions made by the CRA pertaining to charities, the CRA announced its commitment to establish an independent unit within the Appeal Branch to provide internal reconsideration of:

- applications for charitable status that have been denied;
- revocations or annulments of charitable registration; and
- sanctions the CRA proposes to impose.

This should provide an initial means of review that is impartial, fast, efficient, and inexpensive. The results will be communicated to the organization in writing and made public on the CRA's web site to ensure transparency.

5. Improving jurisdictional collaboration among federal, provincial, and territorial governments

Over the next five years, the CRA plans to initiate and build working relationships with provincial and territorial governments that seek collaboration on the regulation of charities. It is anticipated that increased cooperation among jurisdictions will provide opportunities for a more rigorous and client-centred response to the concerns of Canadians about charity regulation; cut down on duplication of effort; reduce confusion; and better address deceptive fundraising practices.

E. PROPOSED DISBURSEMENT QUOTA CHANGES

The 2004 Federal Budget proposed several changes to the disbursement quota (see *Charity Law Bulletin No. 41*, available at www.charitylaw.ca, for more details):

- The disbursement quota for assets of foundations not used in active charitable activities will be reduced from 4.5 percent to 3.5 percent per year, being more representative of historical long-term real rates of return on the typical investment portfolio held by a foundation. This rate will be reviewed periodically to ensure that it continues to be representative of long-term rates of return.

- Amendments will be made to allow charities to access capital gains realized on endowments (formerly 10 year gifts) to meet their disbursement requirements, something the current rules do not permit.
- The 3.5 percent disbursement quota will be extended to include charitable organizations, so that all registered charities will be subject to the same disbursement obligations on their capital assets not used directly on charitable activities. This is in recognition of the growing number of charitable organizations that receive endowments.
- All transfers between registered charities, other than specified gifts, will be subject to a disbursement requirement. In particular, an 80 percent disbursement requirement will be applied to transfers to charitable organizations.
- An endowment received by a registered charity from another registered charity will result in the same treatment as if the endowment had been received directly from the original donor.
- Gifts made by way of direct designation (the designation of the charity as the direct beneficiary of an RRSP, RRIF, or life insurance policy) will be treated as endowments for the purpose of the disbursement quota rules. This means that such gifts will be subject only to the 3.5 percent disbursement quota while they are held as capital, and the 80 percent disbursement requirement in the year they are liquidated.
- Endowments received and spent in the same year will be subject to the 80 percent disbursement requirement.

It is proposed that these measures apply to tax years that begin after March 22, 2004, except where otherwise indicated in the 2004 Federal Budget.

F. CONCLUSION

The new initiatives announced in the 2004 Federal Budget represent the most significant reform of the regulatory framework for charitable organizations operating in Canada in more than 20 years. In addition to

proposing changes to the disbursement quota to be more representative of the long-term real rates of return experienced by registered charities in their investment portfolios, the CRA is embarking on an ambitious plan to improve communication and transparency in the regulation of charitable organizations Canada. Charities and their boards of directors will need to monitor the changes as they are implemented, some within the next year, while others are part of the longer-term plans for the Directorate.

Main Office Location

211 Broadway, P.O. Box 440
Orangeville, Ontario, Canada, L9W 1K4
Tel: (519) 942-0001 Fax: (519) 942-0300
Toll Free: 1-877-942-0001

Toronto Meeting Location

Toronto Dominion Bank Tower, Suite 4200
TD Centre, Toronto, Ontario, Canada
(by appointment) Tel: (416) 675-3766
"Proactive Advice"®