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**RECENT FEDERAL COURT OF APPEAL DECISIONS  
REVOKING CHARITABLE STATUS OF CHARITIES**

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**A. INTRODUCTION**

In 2004 and 2005, there were two cases decided by the Federal Court of Appeal that registered charities should be aware of in relation to maintaining their charitable status. Both these cases were appeals by charitable organizations of the decision of the Minister of National Revenue (the “Minister”) to revoke their charitable status. This *Charity Law Bulletin* reviews those decisions, summarizes their content and discusses their implications for registered charities in Canada.

Under subsection 168(1) of the *Income Tax Act* (the “ITA”),<sup>1</sup> the Minister is entitled to revoke the registration of a registered charity if it fails to comply with the applicable requirements of the ITA. This was the basis for the Minister’s decision to revoke the registration of the Lord’s Evangelical Church of Deliverance and Prayer of Toronto and Collège Rabbiniq ue de Montréal Oir Hachaim D’Tash. Both revocations were up-held by the Federal Court of Appeal in *Lord’s Evangelical Church of Deliverance and Prayer of Toronto v. Canada* (the “Lord’s Evangelical Church case”)<sup>2</sup> and *Collège Rabbiniq ue de Montréal Oir Hachaim D’Tash v. Canada* (the “Collège Rabbiniq ue case”).<sup>3</sup>

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<sup>1</sup> R.S.C. 1985, C.1 (5<sup>th</sup> Supp.).

<sup>2</sup> 2004 FCA 397, [2004] F.C.J. No 1984 (F.C.A.).

<sup>3</sup> [2004] F.C.J. No 424.

## B. LORD'S EVANGELICAL CHURCH CASE

### 1. Facts of the Case

The Lord's Evangelical Church of Deliverance and Prayer of Toronto (the "Church") was registered with Canada Revenue Agency ("CRA") as a charitable organization. CRA conducted an audit of the Church in 2001 and informed the Church, in a letter dated March 15, 2002, that the audit revealed that there was a "serious contravention of the *Income Tax Act*" including the following:

- the adequacy of the Church's books and records;
- conformity of official donation receipts with regulatory requirements;
- payments made by the Church on behalf of employees and other benefits (personal telephone charges, rent, car lease payments, vehicle operating expenses, monthly mortgage payments) that were not included on T4 slips; and
- the gifting of approximately \$150,000 to the pastor of the Church and the further gifting of that amount by the pastor to her children as down payments on family homes. In particular, the \$150,000 gifted was derived from funds raised by the Church on a second mortgage loan secured on the Church's building. This figure represented approximately 47% of all gifts received by the Church in 1999.

CRA indicated in that letter that it was considering revoking the charitable status of the Church, but invited the Church to respond within 30 days if it disputed the results of the audit or wished to present any reasons why the Minister should not revoke the registration. Other than a letter from the Church's solicitor advising CRA that the Church would respond in 2 months, neither the Church nor its solicitor contacted CRA for 10 months. The Church's solicitor advised CRA in March 2003, after repeated contacts made by CRA, that the Church could not afford the service of a professional bookkeeper due to its small size. He further advised that the Church's accountant would assist the "volunteers" "as far as possible" and that he "anticipated compliance" with respect to various non-compliance issues that CRA had concerns with.<sup>4</sup> He also indicated that the \$150,000 would be set up as a loan receivable for the Church "with the ultimate obligation" being that of the pastor. CRA

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<sup>4</sup> *Supra*, note 2 at para. 5.

indicated that if they were to accept the \$150,000 as a loan, “there would need to be a mortgage in place and reasonable conditions of repayments.” CRA also requested further information regarding the other concerns that CRA had over the Church. The solicitors wrote to CRA in April 2003 informing CRA that the Church would commence “new record-keeping patterns” and that one of the pastor’s children’s houses was sold and that the balance of the gift would be documented as a loan.<sup>5</sup>

No further contact was made until May 28, 2003, when CRA informed the Church that its charitable status had been revoked. The Church appealed the decision to the Federal Court of Appeal, arguing that, because CRA did not respond to its proposed remedy before revoking its registration, it was denied natural justice and procedural fairness.

## 2. Findings of the Court

The Court recognized that the revocation of a charity’s registration has severe consequences, and as a result all registrants must be allowed “a full opportunity to meet the case made against it” before such an action is taken.<sup>6</sup> In addition, the Court found that it is axiomatic that procedural fairness be accorded before a decision is made to revoke a charitable registration.<sup>7</sup>

In its unanimous decision, the Court held that the Minister had treated the Church fairly. The initial letter to the Church was sufficient notice that its registration would be revoked if its concerns were not addressed. The Court was unimpressed with the Church’s apparent lack of interest with CRA’s concerns and found its response 10 months later to be insufficient. The Court concluded that the Church was unjustified in assuming that CRA agreed to its proposal of re-characterizing the \$150,000 payment as a loan. Such reasoning suggests that registrants will be required to obtain positive affirmation of their proposed remedies from CRA in order to establish a valid defence before the court hearing the appeal. In this case, the Court found that even if the Church was justified in assuming that it was acceptable to CRA to record the \$150,000 as a loan, it still failed to take any steps to execute this proposal, and the Minister was therefore justified in revoking its registration.

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<sup>5</sup> *Supra*, note 2 at para. 6.

<sup>6</sup> *Supra*, note 2 at para. 10.

<sup>7</sup> *Supra*, note 2 at para. 12.

The Court further found that, even if there were a breach of procedural fairness in relation to CRA's revocation of the charitable status of the Church upon the basis of the improper gift of \$150,000 to the pastor, the Minister's decision could still be upheld because the charitable status of the Church could have been revoked based on any of the other three areas of contraventions revealed by the 2001 audit, i.e.:

- the inadequacy of the Church's books and records – in contravention of subsection 230(2) of the Act requiring registered charities to keep records and books of account,
- the non-compliance of official donation receipts with regulatory requirements – in contravention of the requirements under section 3501 of the *Income Tax Regulations*; and
- payments made by the Church on behalf of employees and other benefits were not included on T4 slips – in contravention of paragraph (b) of the definition of charitable organizations prohibiting the payment of an income of a charity for the personal benefit of any "proprietor, member, shareholder, trustee or settlor" of the charity.

As a result, the charitable registration of the Church was revoked, effective March 5, 2005, and a news release concerning the revocation was published by CRA on the same day.

### C. THE COLLÈGE RABBINIQUE CASE

The decision of the Federal Court of Appeal in the Lord's Evangelical Church case echoes an earlier decision in 2004 by the same Court in the Collège Rabbinique case.<sup>8</sup> The judgment of the Court was delivered orally and it did not set out any background facts of the case or analysis by the Court. The three-paragraph judgment indicated that the revocation of the charitable status of Collège Rabbinique de Montréal Oir Hachaim D'Tash by the Minister was not in error because the grounds of revocation set out in the Notice of Intention to Revoke dated March 3, 2000 was sufficient notice to the charity and that charity was given full opportunity to response to the Minister. The grounds for revocation were very similar to those in the Lord's Evangelical Church case, namely:

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<sup>8</sup> *Supra*, note 3.

- providing official donation receipts for amounts that were not “gifts” within the meaning of subsection 118.1(1) of the Act;
- not devoting all of its resources to charitable purpose and activities;
- the failure to maintain proper records and books in accordance with subsection 230(2) of the Act; and
- making loans to non qualified donees and making loans which were not considered to be operating at arm’s length.

An application by Collège Rabbinique de Montréal Oir Hachaim D’Tash for leave to the Supreme Court of Canada was dismissed on September 30, 2004. As a result, their charitable registration was revoked, effective October 16, 2004, and a news release concerning the revocation was published by CRA on October 15, 2004.

#### **D. CONCLUSION**

These two cases indicate that registered charities need to be proactive in ensuring that they remain in full compliance with all requirements under the ITA. Registered charities also need to be aware that the contravention of any one of the requirements could be cause for revocation of their charitable status. The fact that a charity is unable to retain the service of a professional accountant due to its small size or its lack of resources, as in the Lord’s Evangelical Church case, is not sufficient reason for non-compliance with the requirements under the ITA. The following are some of the more common pitfalls for contravention as revealed by the two cases reviewed in this Bulletin:

- providing official donation receipts for amounts that were not “gifts” within the meaning of subsection 118.1(1) of the Act;
- not devoting all of its resources to charitable purpose and activities;
- making loans or other payments to non qualified donees;
- not keeping adequate books and records required under subsection 230(2) of the Act,
- not complying with the requirements, under section 3501 of the *Income Tax Regulations*, concerning official donation receipts; and

- making payments or providing other benefits for the personal benefit of employees and other individuals without including them on T4 slips.

Although penalties and sanctions were introduced by way of Bill C-33, *A Second Act to Implement Certain Provisions of the Budget Tabled in Parliament on March 23, 2004*, that came into force on May 13, 2005, the Minister continues to have the discretion to revoke the charitable registration of a charity.<sup>9</sup>

If a charity is contacted by CRA, it is important that it adequately respond to any concern or question raised by CRA in a timely and co-operative basis. If a charity is audited by CRA, the charity should be aware of the procedure involved in the audit process, what is expected of the charity by CRA, the powers that CRA has in the audit process, what CRA can and cannot do in the audit, the duties of CRA to provide the charity with the results of the audit, and what the charity can do after the audit, including compliance with irregularities revealed by the audit results, or objecting to or appealing the audit results. The charity may also find it helpful to retain the assistance of legal counsel and/or a professional accountant in communicating with CRA in the audit process. However, in this regard, the charity should be aware that its communication with the accountant would not be subject to any privilege. This means that the communication between the accountant and the charity would not be protected from CRA. However, if the charity retains the assistance of legal counsel, communication between the solicitor and the charity is generally protected from CRA.

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