

CRA UPDATES GUIDANCES ON CHARITIES USING INTERMEDIARIES

*By Terrance S. Carter and Theresa L.M. Man**

A. INTRODUCTION

THE CANADA REVENUE AGENCY (the “CRA”) has released revised guidance documents for registered charities using intermediaries carrying out activities both outside and inside Canada. The CRA published updated [Guidance CG-002: Canadian registered charities carrying on activities outside Canada](#) (“CG-002”),¹ and [Guidance CG-004: Using an intermediary to carry on a charity’s activities within Canada](#) (“CG-004”),² on its website on November 27, 2020.

As a whole, there are no fundamental changes on the general requirements concerning how registered charities can work with non-qualified donee³ intermediaries to carry out activities outside and inside Canada. While there are a number of changes that relax some of the more onerous CRA requirements in the previous guidances, the majority of the revisions involve rewording the previous guidances to clarify the CRA’s long-term interpretation of the “own activities” test under the *Income Tax Act* (the “ITA”),⁴ and the requirement for a registered charity to exercise “direction and control” when working through intermediaries to meet that test. As such, in general terms, these changes preserve the *status quo* of the

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¹ Canada Revenue Agency, online <<https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/guidance-002-canadian-registered-charities-carrying-activities-outside-canada.html>>.

² Canada Revenue Agency, online: <<https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/using-intermediary-carry-a-charitys-activities-within-canada.html>>.

³ See s 149.1(1) of the *ITA*, *ibid*, for a definition of “qualified donees”.

⁴ RSC, 1985, c 1 (5th Supp).

CRA’s regulatory policy for registered charities rather than reflecting any substantial reform of the current “direction and control” regime that would have otherwise required amendments to the ITA.⁵ This *Bulletin* provides a brief explanation of the more notable changes to both CG-002 and CG-004.

B. THE OWN ACTIVITIES TEST

THE CONTENT and structure of CG-002 and CG-004 generally remain the same. Both CG-002 and CG-004 outline the basic requirements for a Canadian registered charity to carry on its activities outside and inside Canada, including the “own activities” test, “direction and control,” and how anti-terrorism laws apply to charities. CG-002 also describes the public benefit test in the context of what is charitable in Canada and abroad.

Both CG-002 and CG-004 explain that, in carrying out its operations, a registered charity must carry on its “own activities,” either through its own staff (including employees, volunteers, and directors), or through an intermediary. Alternatively, a registered charity may make gifts to qualified donees. Where a registered charity carries on its own activities by transferring resources to an intermediary, it must “direct and control” the use of those resources (*i.e.*, physical and financial resources, as well as staff and volunteers). The updated wording in CG-002 and CG-004 maintains the current *status quo* in this regard, subject to only minor wording changes throughout the guidances.

Similarly, section 5 of CG-002 and section 2 of CG-004 explain the restrictions on how a charity can use its resources in their activities, with “resources” being defined to refer to “physical and financial resources, as well as its staff and volunteers”, where the reference to “volunteers” is not contained in the previous guidances. Previously, the word “resource” referred to “all physical, financial, and material resources (for example, buildings, money, or donated goods), intellectual property, and its staff.”

The revised CG-002 and CG-004 expressly clarify the application of “charitable goods policy” [referred to in the Federal Court of Appeal decision *Canadian Magen David Adom for Israel v Canada (Minister of National Revenue)*] to transfers of “non-monetary” resources to non-qualified donees where certain

⁵ For more information, see Terrance S. Carter & Theresa L.M. Man, “Direction and Control: Current Regime and Alternatives” (Occasional paper delivered for The Pemsel Case Foundation, Edmonton, 2020), online: <https://www.carters.ca/pub/article/charity/2020/Direction-and-Control-Current-Regime-and-Alternatives.pdf>.

conditions are met.⁶ Under this policy, a transfer of charitable goods can also meet the own activities test. In this case, CG-002 and CG-004 explain that where a charity transfers resources “directly to beneficiaries of its charitable purposes,” such as giving school supplies to students, the charity does not have to direct and control the use of those resources.

CG-004 sets out requirements where a registered charity intends to “build or buy capital property” in partnership with an intermediary, and CG-002 also sets out extensive requirements (especially in Appendix B) that need to be complied with where a registered charity intends to transfer “ownership of real or capital property, such as land or buildings.” To avoid the confusion of the term “capital property,” the revised guidances clarify the application of these requirements by replacing the term “capital property” with “real property” to refer to “land and immovable property on land, such as buildings.”

C. TYPES OF INTERMEDIARIES

COMMON TYPES of intermediaries for charities operating outside and within Canada are listed in section 6 of CG-002 and section 3 of CG-004. The previous guidances provide that there are four common types of intermediaries a charity might use to carry out its own activities, namely agency, contractor, joint venture participant, and co-operative participant. The agency relationship has been removed from the guidances, with the contractor relationship expanded to include “consultant”, resulting in the revised guidances providing that there are three common types of intermediaries instead of four. The revised guidances also clarify that the listing of common types of intermediaries is not exhaustive, and that other arrangements can be entered into with intermediaries as long as the charity directs and controls the use of its resources.

Removing the use of agency relationship is a welcome change because the use of an agency relationship is generally not desirable for many reasons, including exposing the charity to liabilities of the intermediary due to the principal/agent relationship. However, what is problematic is that the term “consultant” is not well defined in the revised guidances. Firstly, the revised guidances provide that a consultant may be engaged to act as an intermediary “when the charity cannot send its own staff to a region, or it may hire a contractor to provide goods or services” but it is not clear what the differences are between the two. Secondly, the same examples used in the previous guidances for “agents” are used as examples for

⁶ *Canadian Magen David Adom for Israel v. Canada (Minister of National Revenue)*, 2002 FCA 323.

“consultants” in the revised guidances, which seems to imply that “agents” and “consultants” in fact mean the same thing from the CRA’s perspective.

With the removal of agency relationships in the revised guidances, the guidances clarify that charities that have existing agency agreements with intermediaries would continue to be acceptable to the CRA as long as the necessary direction and control is in place. This underscores that there does not appear to be any substantive difference between the two.

D. DIRECTION AND CONTROL

WHEN CARRYING ON activities through an intermediary, a charity must maintain “direction and control” of the use of its resources. Section 7 of CG-002 and section 4 of CG-004 describe the basic requirement of “direction and control” when charities transfer resources to their intermediaries. The revised guidances continue to provide that charities must make decisions and set parameters on an ongoing basis, such as:

- how the activity will be carried on
- the overall goals of the activity
- the area or region where the activity will be carried on
- who will benefit from the activity
- what goods and services the charity’s money will buy
- when the activity will begin and end

The revised guidances continue to recommend that charities adopt various types of measures in order to direct and control the use of a charity’s resources. While the list of measures is largely the same, there are some interesting differences. In this regard, the following measures are the same in both the previous and revised guidances:

- create a written agreement, and implement its terms
- communicate a clear, complete, and detailed description of the activity to the intermediary
- provide clear, complete, and detailed instructions to the intermediary on an ongoing basis
- make periodic transfers of resources to the intermediary, based on demonstrated performance

However, the following two measures have been updated:

- Firstly, charities are to “monitor and supervise the activity, *including requiring regular reporting*” with the words in italics being inserted in the revised guidances.
- Secondly, charities are to “arrange for the intermediary *to either keep the charity’s funds separate, or account for them separately in its books and records*” with the words in italics newly inserted to replace the previous requirement that the intermediary must “keep the charity’s funds separate from its own, and to keep separate books and records.” It is a welcome change that the segregation of funds by the intermediary is no longer required by the CRA. Although this requirement reflects the common law principle that funds of the principal are not funds of the agent and should therefore be segregated, there is no legal basis to support the CRA’s previous practice that funds be segregated in a separate bank account by all types of intermediaries, not just agents.

CRA recognises that where a charity engages in a one-time activity, the complications of developing a full, formal, written agreement may outweigh the benefits. Previously, where the money spent on a one-time activity was \$1,000 or less, other forms of communication might be used to show direction and control over the use of resources by intermediaries. There are two major changes in the revised guidances: (i) the cap has been increased to \$5,000, and (ii) other documents might be enough to show ongoing direction and control over the intermediary’s use of resources, and these might include written instructions, email records, meeting minutes, and regular reporting.

The CRA recognizes that some charities are registered as the Canadian representatives or offshoots of a larger organization, often located outside Canada, requiring payments from their Canadian charities, in the form of tithes, royalties, memberships, or similar transfers. These entities are referred to as “head bodies” in Appendix C of the previous CG-002. The term “head body” is no longer used in the revised CG-002, with charities in these situations simply being referred to as the “Canadian representative or affiliate of another (usually larger) organization that is a non-qualified donee, often located outside Canada.” The revised CG-002 continues to explain that charities cannot make gifts to these foreign entities, and explains how resources may be provided to these entities under the direction and control of the Canadian charity. However, the term “head body” continues to be used by the CRA in other policies,

such as [Guidance CG-028, *Head bodies and their internal divisions*](#).⁷ It is possible that the sudden loss of reference to this concept in CG-002 may not be understood by charities as they may not “make the connection” between the two. It would have been preferable that the revised CG-002 at least contain a brief reference to the term “head body.”

E. BOOKS AND RECORDS

SECTION 8 of CG-002 and section 5 of CG-004 state that a charity’s books and records must “contain enough information to allow the CRA to determine if the charity is operating in accordance with the [ITA].” As well, books and records must allow the CRA to check whether: the charity’s funds are being spent on its own activities or on gifts to qualified donees; the charity is directing and controlling the use of its resources; revenues, including charitable donations, can be verified, and that the charity’s purposes and activities continue to be charitable. This remains generally unchanged from the previous guidances.

Furthermore, the revised CG-002 provides that when the CRA considers whether a charity’s books and records are adequate, it looks at the risk of non-compliance for the particular activities. The risk level may relate to the location, the activity, or the type of resources. In this regard, the revised CG-002 sets out the following example of typical books and records requirements to differentiate lower-risk from higher-risk activities:

A **lower-risk** activity for a charity that has a purpose to advance education by providing books would be to purchase and send accredited high school textbooks to schools overseas. In this situation, adequate books and records might include receipts for the purchase of the textbooks, shipping bills of lading, and signed confirmations from the schools acknowledging receipt of the textbooks.

A **higher-risk** activity for a charity that has a purpose to relieve poverty by providing funds would be to transfer cash overseas. In this situation, adequate books and records might include:

- agreements between the charity and any intermediaries
- letters and reports showing ongoing communication between the charity and the overseas representatives and intermediaries

⁷ Canada Revenue Agency, *Guidance CG-028 on Head bodies and their internal divisions*, issued September 22, 2017, online <https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/head-bodies-and-their-internal-divisions.html>.

- detailed bank records showing funds being transferred to an overseas bank
- financial records for payment of salaries and other expenses, including invoices and receipts
- documents showing that recipients of funds meet defined criteria
- board minutes showing approval of agreements and expenditures

The amendments also make the revised guidances more applicable to modern technology, with new references to intermediaries reporting via videoconference and providing instructions to intermediaries via conference and telephone calls. The revised CG-002 guidance adds an acknowledgment in section 8 that while original source documents are recommended, the CRA “will usually accept photocopied or electronic (scanned) documents, as long as proper imaging practices are followed.”

In the previous CG-002, the requirement for charities to obtain source documents was a major concern to charities. In this regard, the CRA acknowledged in the previous CG-002 that the *ITA* does not require a charity to provide original source documents, such as receipts for purchases, to show that it is in compliance; nevertheless the CRA “recommend[ed] that a charity get original source documents whenever possible”, but where “getting original source documents may not be possible or practical”, then the charity would need to “explain why it cannot get them, and make all reasonable efforts to get copies and/or reports and records from staff and intermediaries to support its expenditures, and show that it has made such efforts” and that the charity would also “have to show when, how, and in what amounts funds were transferred.” In the revised CG-002, the onerous requirement for source documents is relaxed somewhat by stating that: (i) the CRA continues to recommend that a charity get original source documents, such as receipts for purchases, to document its expenditures; (ii) the CRA acknowledges this is not always possible or practical, and the CRA will usually accept photocopied or electronic (scanned) documents, as long as proper imaging practices are followed; and (iii) a charity should still make all reasonable efforts to get source documents and/or reports and records from staff and intermediaries to support its expenditures.

F. DISASTER AND EMERGENCY RELIEF

APPENDIX A of the previous CG-002 set out the requirements for applicants intending to carry out “disaster relief or other foreign activities.” The revised CG-002 continues to set out the same requirements but also

has it apply to “emergency relief.” However, the revised CG-002 does not explain what is meant by “emergency relief” and how that differs from “disaster relief.”

G. CONCLUSION

WHILE PROVIDING some helpful clarification, as well as introducing some administrative relief (*e.g.* raising the threshold from \$1,000 to \$5,000 before an agreement is needed), the updates to CG-002 and CG-004 largely maintain the current regime of “own activities” and related direction and control requirements. The CRA has done what it can to make the regime more manageable through its revision of CG-002 and CG-004. However, the continuation of the “own activities” and direction and control regime will still leave many Canadian charities subject to unnecessary administrative costs. Hopefully, the Department of Finance Canada will take this opportunity to possibly consider amending the *ITA* to remove the “own activities” test and replace it with statutory changes that focus on the application of charitable resources to charitable purposes.