



business meeting

## BECOMING A REGISTERED CHARITY

Although they aren't usually thought of in such terms, Canadian charities—as measured by the amount of money they receive and administer—can be big businesses. However, because they collect and disburse that money in order to support and advance causes which create a public benefit, charities are accorded special status under our tax laws. Our tax system effectively subsidizes the activities of registered charities both by exempting such organizations from the payment of tax and by providing a tax deduction or tax credit to companies and individuals that contribute to their charitable activities.



Wolters Kluwer

Given the amounts of money involved and the fact that registered charities are subsidized by our tax system, it's not surprising that there are many specific rules and policies which govern whether an organization will qualify for status as a registered charity and which both impose ongoing requirements on such organizations, including determining what kinds of activities they can—or cannot—engage in.

### **Distinguishing charities from non-profit organizations**

Although they are often referred to interchangeably in everyday usage, charities are not the same as non-profit organizations, and vice-versa. In fact, for purposes of our tax and regulatory systems, if an entity meets the definition of a charity, it cannot be considered a non-profit organization, even where that entity is not and cannot be registered as a charity. An organization can be one or the other, not both.

Confusion between the two types of entities is understandable, as there are similarities. For instance, both operate on a non-profit basis and are generally exempt from income tax, and both may have filing obligations with the federal government. However, a non-profit organization does not have to seek registration as such with the Canada Revenue Agency (CRA) and, more importantly, it cannot provide a charitable donations tax receipt for any donations it receives.

Perhaps the easiest way to distinguish between the two types of organizations is through an examination of the types of activities in which they can engage. The range of activities available to non-profit organizations is virtually limitless—they can involve themselves in efforts which promote or carry out any social welfare, civic improvement, pleasure, sport, or recreational endeavours. The only real restriction on the activities of non-profit organizations is that they cannot carry out their activities, of any kind, on a for-profit basis.

By contrast, the limitations on permitted activities of charities are much more stringent. While the list of possible charitable causes is almost limitless, such causes must, in order for the organization to qualify as a registered charity, fall under one or more of the four categories permitted by the CRA. Those four categories, with examples, are as follows:

- relief of poverty (food banks, soup kitchens, low-cost housing units)
- advancement of education (colleges, universities, research institutes)

- advancement of religion (places of worship, missionary organizations)
- purposes beneficial to the community (animal shelters, libraries, volunteer fire departments)

Conversely, the CRA provides the following examples of organizations which would qualify as not for profit organizations, but not as charities:

- social, recreational, or hobby groups (bridge clubs, curling clubs, golf clubs)
- certain amateur sports organizations (hockey associations, baseball leagues, soccer leagues)
- some festival organizations (parades, seasonal celebrations).

It's not hard to see that the line between charitable organizations and not for profit groups could be difficult to discern in some cases. In all cases, however, it is the CRA which determines whether an organization qualifies for certification as a registered charity, or for tax-exempt status as a non-profit organization.

### **Registered vs. non-registered charities**

As with the difference between “charities” and “not for profit organizations”, many Canadians don't distinguish between “charities” and “registered charities”. Or, if they do, they may conclude that being a registered charity just means taking on some additional paperwork obligations. Neither is the case, and the difference is a significant one, both for the charities involved and for any potential donors.

Where a charitable organization seeks and receives recognition from the CRA as a registered charity, there are three immediate major consequences. First, it means that the CRA has examined the activities and the structure of the organization and determined that it meets the requirements for registration. Second, a charity which has received registered charity status takes on a number of information filing obligations which keep the CRA apprised of its charitable activities and its finances. Finally, only a registered charity is entitled to issue a tax receipt for donations made to the charity and only donors who have received such a tax receipt can claim a tax credit for those donations on their annual tax return.

It's not fair to conclude that a charity which has not sought and received status as a registered charity is not a legitimate charity. Obtaining such registration status and complying with the resulting filing obligations is not a quick or simple process. For some very small charitable endeavours, taking on and discharg-



ing those obligations on an ongoing basis simply isn't realistic, in light of their size and limited resources.

An individual who is contemplating making a donation to a charity which is not a registered charity should, however, keep two things in mind. First, there is no government or other oversight of a charity which is not registered. Such charities do not file information returns or other documents which would allow such oversight, and so would-be donors must take the word of the charity with respect to how donations made will be used. Second, a charity which is not registered cannot issue a tax donation receipt to a donor, and as such no charitable tax donation credit can be claimed by that donor. A would-be donor who understands both these facts and still wishes to make a donation is, of course, free to do so.

### **Deciding whether to become a registered charity**

There are numerous advantages to an organization to having status as a registered charity, some of which are outlined on the CRA website as follows.

- Registration allows a charity to issue official donation receipts for gifts it receives. These receipts can be used to reduce the income tax payable of an individual donor or the taxable income of a corporate donor.
- Once registered, a charity is exempt from paying income tax.
- Registered charities are eligible to receive gifts from other registered charities, such as foundations.

- Registration provides increased credibility in the community, since registered charities must follow certain rules and guidelines in order to maintain their registration.
- Many goods and services provided by registered charities are exempt from goods and services tax/harmonized sales tax (GST/HST). Also, in many situations, registered charities can claim a partial rebate for the GST/HST they pay.

While there aren't any actual disadvantages to becoming a registered charity, such registration brings with it a number of new responsibilities. Many of those responsibilities come in the form of information filings with the federal government, which must be done on an annual basis. Those filings, which for the most part are made public, include information on the amount of funds raised and the amount spent on administrative costs, including detailed information on compensation paid to employees or directors of the charity. A registered charity also faces restrictions on how and to whom it can disburse the funds which it raises, and responsibility for seeing that funds disbursed are used in the intended way. It will also be required to meet a disbursement quota—the minimum calculated amount that a registered charity is required to spend each year on its own charitable programs or on gifts to qualified donees (such as other registered charities). Finally, an organization which seeks and obtains status as a registered charity must recognize that it will have to devote some portion of its resources—human and otherwise—to meeting all of its record-keeping, filing, and oversight obligations on an ongoing basis, for as long as it maintains that status.

## Applying for a charitable registration number

While the obligations and responsibilities that accompany becoming a registered charity aren't small, they also apparently aren't insurmountable, as there are tens of thousands of such registered charities in Canada.

The process of obtaining a charitable registration number (and, consequently, the status of a registered charity) begins with making certain that the organization has put in place all of the organizational structures and documents which will be required by the CRA. At a minimum, those documents will include the organization's governing documents, a description of the activities of the organization, and a proposed 12-month operating budget. The form that the governing documents will take can differ, depending on the organization's particular structure, but can include letters patent, articles of incorporation, a constitution, or a trust document. It's also necessary to include a copy of any bylaws of the organization.

Each of those documents is submitted along with the actual application form, which is Form T2050, *Application to Register a Charity Under the Income Tax Act*. The CRA also publishes a guide to the completion of Form T2050, which is available at <http://www.cra-arc.gc.ca/E/pub/tg/t4063/README.html>.

Once the charitable registration application is received by the CRA, it will be reviewed for completeness. Where the CRA assesses the application as complete, the organization will be so advised and will be provided with an approximate time frame within which their application will be assigned to an officer for review. Where the application is incomplete, it will simply be rejected and returned to the applicant.

Even where an application is complete when filed, the CRA may have further questions or require further information from the organization during its assessment and review process. It's also possible that the CRA will determine that the charitable purposes outlined in the application need to be amended, to bring them into line with the actual activities of the organization. In either case, the CRA will contact the organization which will have 60 days to provide the requested information or changes. If no response is received, the file will be closed and the application considered abandoned. If that happens, and the organization still wishes to obtain a charitable registration number, it must re-commence the application process from the beginning.

The CRA can also, of course, refuse an organization's application for registered charity status. Where that occurs, the organization is entitled to appeal that

decision, and the means by which that can be done are outlined on the CRA website at <http://www.cra-arc.gc.ca/chrts-gvng/chrts/pplyng/pprp-eng.html>.

## Operating as a registered charity

If an organization's application for registered charity status is approved, the CRA will provide it with a Notification of Registration, which includes the effective date of registration, the charitable registration number and an outline of the rights and responsibilities which come with status as a registered charity.

The rights of a registered charity are outlined above. The responsibilities that come with charitable registration status are more detailed, but can generally be divided into two categories. First, the charity has an obligation to ensure that both fundraising and disbursement of funds are carried out according to the applicable rules—specifically, that those funds are accounted for properly and used in ways which are consistent with the stated charitable purposes of the organization. Second, all registered charities are obliged to fulfill all of the information reporting requirements imposed by the CRA.

## Fundraising and issuing donation receipts

All charities, whether large or small, obtain their funds either from their own fundraising activities, or through amounts received from other registered charities. The receipt of gifts by charities from either source, and particularly the issuance of charitable donation receipts for gifts from donors, are governed by a detailed set of rules which regulate what types of donations qualify for issuance of a charitable donation receipt and which do not.

The listing of possible forms which a charitable donation can take is almost limitless, but can generally be divided into two major categories—property and services. Only the former may be eligible to receive a charitable donations tax receipt for the donation made.

No charitable donations receipt can be issued to someone who donates services or time to a registered charitable organization, as donations of time, skills, or effort do not qualify as charitable donations. Therefore, someone who donates funds to local food bank or food drive can obtain a charitable donation receipt for the amount of the donation, but someone who volunteers their time to help with a food drive or to work at the food bank is not considered to have made a charitable donation which qualifies for such a tax receipt. There is a bit of flexibility in this rule,



in that if a charity pays a service provider for services rendered and the service provider then chooses to donate the money back, the charity can issue a charitable donation receipt for the monetary donation.

While donations of property do generally qualify for issuance of a donation receipt, there are many qualification and exceptions. The CRA provides the following list of property transfers which do **not** qualify as charitable donations:

- a court ordered transfer of property to a qualified donee;
- the payment of a basic fee for admission to an event or program;
- the payment of membership fees that convey the right to attend events, receive literature, receive services, or be eligible for entitlements of any material value that exceed 80% of the value of the payment;
- a payment for a lottery ticket or other chance to win a prize;
- the purchase of goods or services from a charity;
- a donation for which the fair market value of any benefit provided to the donor exceeds 80% of the value of the donation;
- a gift in kind for which the fair market value cannot be determined;
- donations provided in exchange for advertising/ sponsorship;
- gift certificates donated by the issuer (with some exceptions);
- a pledge or promise to make a gift;
- loans of property;
- use of a timeshare; and
- the lease of premises.

Where a donation of property does qualify as a charitable donation under the rules, the charity can issue a charitable donations tax receipt which will entitle the individual donor to claim a tax credit on his or her tax return for that year, or any of the five subsequent tax years.

While the amount of any CPP disability benefit received will depend on the amount of contributions made, the maximum of such monthly benefit payable in 2016 is \$1,290.81.

### *Disbursing funds*

The primary purpose of charities, of course, is to disburse funds which have been raised for the benefit of those it seeks to assist. And, as with fundraising activities, there are detailed rules which govern and limit the amount and types of disbursements which charities may make.

The first and most important requirement is the disbursement quota—the minimum calculated amount that a registered charity is required to spend each year on its own charitable programs or on gifts to qualified donees, such as other registered charities. That disbursement quota, which is calculated separately for each charity, is based on the value of a charity's property not used for charitable activities or administration during the previous 24 months.

While the calculation can be complex, the general rule is that if the average value of a registered charity's property not used directly in charitable activities or administration during the 24 months before the beginning of a particular fiscal year exceeds \$100,000, then the charity is required to disburse 3.5% of the average value of that property during the fiscal year.

Charitable organizations that qualify as private or public foundations are similarly subject to the 3.5% disbursement requirement, but for such foundations the threshold average property value which triggers that requirement is \$25,000.

The rules do provide some flexibility in that an excess of disbursements made during a particular year can be carried forward for 5 years or back for one year to cover any shortfalls. In other words, a registered charity can draw on disbursement excesses from the five previous fiscal periods to help it meet a shortfall. If no excesses are available to draw on, the charity can try to spend enough the following year to create an excess that it can carry back to cover the shortfall from the year before.

### Filing information returns

The second major administrative responsibility of any registered charity is the filing of an annual information return in which it reports on its activities, sources of revenue, and expenditures for the year. That return, done on Form 3010, *Registered Charity Information Return*, must be filed with the CRA within 6 months after the end of a charity's fiscal year. The charity must also file its financial statements as part of a complete return.

Form 3010 is made up of a several different forms and schedules. Some of those forms and schedules must be completed by all registered charities, while others are specific to some types of charities (e.g., private foundations).

Uniquely among returns filed with the CRA, the annual information return filed by a charity is, for the most part, public information. Such returns are posted, as filed and without review by the CRA, on the Agency's website, and available to anyone who wishes to view them. There are, however, some aspects of the return which are withheld from the public posting, including the physical address of the charity, the address for the charity's books and records, the name and address of the individual who completed the return, information about fundraisers, information about donors not resident in Canada, and the home address, telephone number, and date of birth of directors, trustees, and similar officials of the charity.

### Permitted activities of charities—and going offside

Registered charities are, reasonably enough, expected to carry out charitable work. They can do so in two ways. First is the carrying out their own charitable activities, either through their own employees or volunteers or through intermediaries. Where intermediaries are used, the charity is expected to oversee and monitor the activities of the intermediary or, in the words used by the CRA, to “take an active and controlling part in a program or project that directly achieves its charitable purposes.” Secondly, charities can carry out their charitable purposes by making donations to other organizations which are qualified donees. To be a qualified donee, an organization must be located in Canada and must itself be a registered charity entitled to issue official donation receipts for gifts it receives from individuals and corporations.

Charities can also engage, to a limited extent, in business, political, and social activities, with the caveat that such activities must be what are termed “subordinate and incidental” to the charity's main purpose. The precise nature and extent of these restrictions can be difficult to meet, and the CRA has published a number of policy statements outlining its views on those restrictions. Links to those policy statements can be found on the CRA website at <http://www.cra-arc.gc.ca/chrts-gvng/chrts/prtnng/ctvts/thr-eng.html>.

It's important for registered charities to stay onside when it comes to permitted activities. Where those activities exceed what the CRA considers to be the limits imposed by the “subordinate and incidental” restrictions, a charity can run the risk of losing its charitable registration status.



### Losing charitable registration status

What the CRA gives, it can also take away, and that includes revocation of an organization's status as a registered charity. Revocation of that status, in most cases, will effectively bring an end to an organization's charitable work.

There are a number of immediate consequences to the loss of registered charity status. The first, of course, is the damage to the public image of the charity. Second, the organization will no longer be entitled to issue charitable donation tax receipts, which will seriously impact its ability to raise funds. Third, the organization is no longer exempt from income tax. Finally, a registered charity which has its status revoked must either transfer its assets to an eligible one (generally another registered charity which is in good standing) or must pay a “revocation tax” which is equal to the full value of the charity's property at the time of revocation.

Most often, revocation of a charity's status is the result of its failure to meet its information filing requirements. Less frequently, such revocation follows an audit by the CRA which discloses that the charity is not meeting its requirements for registration in that it is failing to devote its resources to charitable purposes and activities, is failing to maintain direction and control over its resources, or perhaps is not keeping adequate books and records.

The revocation of a charity's status is a last resort for the CRA. Whatever the reason for the potential revocation, the charity will be given advance notice and an opportunity to remedy any defects identified by the CRA, or to appeal against the CRA's finding of those defects. The time frames for those notice and appeal periods will differ, depending on the reason for the threatened revocation.

Where the CRA determines that it is necessary to revoke an organization's charitable registration (or where a charity has voluntarily asked for such registration to be revoked), a notice of that revocation, the reason for the revocation, and its effective date are all published on the CRA website.

## Conclusion

Registered charities enjoy a special status and receive a number of privileges under our tax system, and they in turn provide innumerable benefits to a great number of Canadians through their charitable work.

The special status accorded registered charities is accompanied by a number of responsibilities. First, of course, is the responsibility to raise and disburse funds honestly and efficiently and in accordance with the organization's charitable purposes. Becoming a registered charity also brings with it a number of ongoing administrative and oversight responsibilities.

An organization which is planning to apply for registered charity status should carefully consider whether obtaining such status is actually necessary for it to meet its goals and objectives. And, as well, it should consider whether it has both the resources and the level of commitment needed to fulfill the many ongoing responsibilities that come with being designated as a registered charity.

