

Guidance for United States Tax-Exempt Organizations Commencing Charitable Operations in Canada*

TERRANCE S. CARTER¹

*Wardlaw, Mullin, Carter, Thwaites & Ward, Barristers & Solicitors,
Orangeville, Ontario*

Introduction

It is not unusual for a tax-exempt organization in the United States at some time to consider commencing operations in Canada, either because donors who are residents of Canada require charitable receipts that can be used for taxation purposes in Canada or because of a strategic plan to expand charitable activities into Canada.

This article is intended to provide attorneys, as well as senior executive staff members of U.S. tax-exempt organizations, with a practical outline of the various issues to be addressed and steps to be taken in commencing charitable operations in Canada, preferably as part of implementing an overall structure for international operations. This article should not be treated as a replacement for specific legal advice that should be obtained in Canada before a definitive legal opinion is given to a U.S. client.

It should be noted that only those organizations in the United States that meet the requirements of what is considered by the courts in Canada to be charitable at law would be able to become Canadian registered charities as defined below. It is for this reason that the article is directed at commencing "charitable operations" in Canada instead of establishing a "tax-exempt organization" in Canada.

What are the Advantages of Establishing a Canadian Registered Charity?

Why would a U.S. tax-exempt organization not simply carry on its own operations in Canada? Although there is nothing to stop a U.S. tax-exempt organization from doing so, a U.S. organization would not be entitled to receive the tax and other advantages that are available only to a registered charity in Canada. Applicable advantages include:

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- (1) Canadian donors who make donations to a U.S. tax-exempt organization are unable to benefit from charitable receipts issued by the U.S. organization for income tax purposes except when applying the receipted amount against income earned in the United States² or where the Canadian taxpayer lives near the Canadian-U.S. border throughout a taxation year and is employed or carries on business in the United States.³ On the other hand, a Canadian registered charity can issue charitable donation receipts that can be used as tax credits by donors who are residents in Canada.
- (2) A Canadian registered charity is exempt from paying income tax in Canada.
- (3) A Canadian registered charity is entitled to receive a partial refund of the Goods and Services Tax (GST) that is imposed under the *Excise Tax Act*⁴ for goods and services acquired by the Canadian charity.
- (4) There is a psychological advantage in raising money in Canada if the organization that is raising the money is a Canadian registered charity as opposed to one that is a U.S. or other foreign organization.

What are the Basic Requirements For Becoming a Canadian Registered Charity?

The requirements are set out under sections 248 (1) and 149.1 (1) of the *Income Tax Act* and are explained in *Information Circular 80-10R*, entitled "Registered Charities: Operating a Registered Charity",⁵ as well as in a recent draft publication issued by Charities Division, Canada Customs and Revenue Agency (formerly Revenue Canada) entitled "Registered Charities: Operating Outside of Canada".⁶ Those requirements can be summarized as:

- (1) The organization must be created or established in Canada.
- (2) The organization must be resident in Canada. This is generally understood as meaning that a majority of its directors or trustees must be Canadian residents.
- (3) The purposes and activities of the organization must be charitable at law.
- (4) The organization must apply for registration and be designated by CCRA as a charitable organization, a public foundation or a private foundation. A charitable organization is loosely characterized as an "initiator of charitable activities as distinct from an organization which funds the activities of others".⁷ A public foundation is generally described as "constituting a public body that is formed for the purpose of funding the charitable activities of other registered organizations".⁸ A private foundation is a foundation that does not constitute a public foundation because either 50 per cent or more of its directors, trustees,

officers or similar officials of the foundation do not deal with each other at "arm's length", or more than 50 per cent of the capital contributed or otherwise paid to the foundation is paid by one person or by a group of persons who do not deal with each other at "arm's length".⁹

- (5) The organization must devote all of its resources to charitable activities carried on by the organization itself if it is a charitable organization, or it must be constituted and operated exclusively for charitable purposes if it is either a public foundation or a private foundation.
- (6) The organization must ensure that no part of its income is payable to, or is otherwise available for the personal benefit of any of its members, proprietors, trustees or directors.
- (7) The organization must expend its resources on its own charitable activities and ensure that the transfer or gift of funds to other organizations is limited to organizations that are identified in the *Income Tax Act* as "qualified donees". A qualified donee is defined later in this article.
- (8) The organization must control and direct the use of its own funds and resources.
- (9) The organization must spend a certain amount of money each year on charitable activities to meet a prescribed minimum disbursement quota under the *Income Tax Act*, which is 80 per cent of the receipted income from the previous taxation year, subject to certain exceptions. Where the charity is either a public foundation or a private foundation, it must also expend at least 4.5 per cent of any assets of the foundation owned over the previous 24 months that were not used directly in charitable activities or in the administration of the foundation, less any amount calculated in its 80 per cent disbursement quota.¹⁰
- (10) The organization must maintain sufficient books and records in Canada to satisfy the requirements of CCRA¹¹ to enable the Agency to verify that the funds of the charity have been properly spent and that the charity retains control and direction over the use of its resources.

The most difficult of these requirements is to satisfy CCRA that the purposes and activities of the applicant are exclusively charitable at law.

What is Considered to be "Charitable" at Law in Canada?

Although the *Income Tax Act* defines the requirements for becoming a registered charity, the *Act* does not define what a charity is or what is meant by charitable, notwithstanding the fact that CCRA must be satisfied that all of the purposes and activities of the applicant are charitable at law before charitable registration can be granted. Applicable case law has generally held that a

purpose will be considered to be charitable if it is one that is directed to any one of the following heads of charity:¹²

- (1) the relief of poverty;
- (2) the advancement of education;
- (3) the advancement of religion; or
- (4) other purposes benefiting the community as a whole as determined by the courts.

The Charities Division of CCRA will scrutinize an organization applying for registration to determine whether the purposes stated in its constating documents are exclusively charitable and whether or not its activities as proposed in its statement of activities will be undertaken exclusively in fulfilment of those charitable purposes.

In this regard, there are a number of important restrictions imposed by the Charities Division concerning what a registered charity can and cannot do. Some of the more important restrictions include:

- (1) The charitable purposes and activities must not violate Canadian public policy as interpreted by the Charities Division.
- (2) A registered charity must not engage in political activities that exceed the restrictions established under the *Income Tax Act* as interpreted by the Charities Division and the courts.¹³
- (3) A registered charity must not generate revenue through unrelated business activities, although there are certain limited business activities that can be carried out by a registered charity if they fulfil the requirements of a deemed “related business activity” under the *Income Tax Act*.¹⁴

What Legal Forms are Available for a Canadian Registered Charity?

A Canadian registered charity that is designated as a charitable organization by the Charities Division can be structured as a charitable unincorporated association, a charitable trust, or a charitable not-for-profit corporation. For a registered charity to be designated as either a public foundation or a private foundation, the organization must be established as either a charitable trust or a charitable not-for-profit corporation. Briefly, these legal forms are:

- (1) *Charitable Unincorporated Association*: A charitable unincorporated association is technically not a separate legal entity at common law in Canada.¹⁵ Rather, it is considered to be a collection of individuals who have agreed, either explicitly or by implication, to work together in a contractual relationship as an association, to pursue a stated charitable purpose. A charitable unincorporated association is particularly attractive for churches and small charitable organizations because of the

ease with which it can be created, the lack of formalities in operation, and the ability to establish a customized organizational structure without the intrusion of governmental review or requirements. However, a charitable unincorporated association does not provide limited liability protection for its members. This can be of concern if the association faces the risk of legal action due to injuries or even claims for sexual or child abuse. As such, the unincorporated association is not the preferred legal form through which charitable operations are carried out in Canada.

- (2) *Charitable Trust*: A charitable trust requires a written trust agreement signed by a settlor or settlors appointing one or more individuals to act as trustees of certain charitable property pursuant to a clearly delineated statement of charitable purposes. The advantage of the charitable trust is that it is relatively easy to create and avoids the formalities associated with incorporation. The difficulty with a charitable trust is that it requires the appointment of successive trustees, unless the unincorporated association is a religious organization that can rely upon provincial legislation to provide for perpetual trustees notwithstanding that successive trustees have not been appointed on a continuous basis.¹⁶ In addition, trustees may be exposed to potential liability on a personal basis. As such, unless the charity operates as a passive public foundation or private foundation only, with little or no exposure to legal risk or liability, it is generally recommended that a charitable trust not be used.
- (3) *A Charitable Not-For-Profit Corporation*: A charitable not-for-profit corporation without share capital can be incorporated federally under the *Canada Corporations Act*¹⁷ or under provincial incorporating legislation in each province, e.g., the *Ontario Corporations Act*.¹⁸ The advantage of using a not-for-profit corporation to carry on charitable operations in Canada is the permanency of the corporate vehicle as well as the limited liability protection that it affords to its members. As a result, most organizations that carry on active charitable operations in Canada are organized as charitable not-for-profit corporations. Generally speaking, it is preferable to incorporate federally under the *Canada Corporations Act* because it permits the charity to more readily carry on operations across Canada by being able to obtain extra provincial registrations in each province without having to have the corporate name of the charity approved on a province-by-province basis.

What is the Process of Becoming a Registered Charity In Canada?

The process of becoming a registered charity in Canada normally takes between eight and 12 months to complete, although that time frame can vary considerably and involves the following steps:

- (1) Assuming that the organization is being structured as a charitable not-for-profit corporation, an application for letters patent would be made to either the Federal Government, through Industry Canada, or provincially through one of the provincial ministries of corporate affairs, such as the Ministry of Consumer and Commercial Relations in Ontario. If the application is made to the Federal Government, then Industry Canada will normally grant letters patent of incorporation within two weeks of receiving the application, with the effective date for the letters patent being the date that the application is received. On the other hand, if the application for incorporation is made to a provincial government, then the time involved can vary considerably. In the case of the Province of Ontario, an application for incorporation must first be approved by the Attorney General through the Office of the Public Guardian and Trustee. This additional step can add a month or more to the application process. This delay and resulting additional scrutiny of the application that occurs if an application for incorporation proceeds in Ontario means that most applications for incorporation of not-for-profit charitable corporations located in Ontario will bypass the problem by applying for incorporation federally under the *Canada Corporations Act*.
- (2) Once letters patent are issued, then an application to have the corporation become a registered charity is made to the Charities Division. This would involve submitting the following documentation to Revenue Canada:
 - a T2050 application for Income Tax registration for Canadian charities;
 - a certified copy of the letters patent for the corporation as well as a certified copy of its general operating bylaw;
 - a statement of activities explaining how the corporation intends to fulfil its charitable purposes;
 - a certified copy of the names of the directors of the corporation and its officers; and
 - a proposed financial statement for the first year of the corporation's operations.
- (3) An alternative process would be to submit draft incorporation documentation to the Charities Division of CCRA along with draft copies of documents required to apply for charitable status and request that the Charities Division grant pre-approval before proceeding with formal incorporation. This procedure would avoid having to amend the charitable purposes in the letters patent if they were found to be deficient by the Charities Division. An amendment of the charitable purposes would otherwise require an application for supplementary letters patent, which can be a time-consuming delay. However, the

pre-approval process can involve a significant time factor itself, since the draft documentation must be approved twice: once during the draft approval process and a second time in its final form after the incorporation has been granted. Since most charitable clients are interested in obtaining status as a registered charity as quickly as possible, they will normally prefer to incorporate first and then apply for charitable status effective as of the date of incorporation notwithstanding the risk of possibly having to apply for supplementary letters patent to modify the charitable purposes of the organization if this is determined to be necessary by the Charities Division.

- (4) From the time that the Charities Division receives the application to become a registered charity until the application is finally approved, normally takes seven to 10 months to complete. However, this time frame can be expedited if there is an emergency. Alternatively, the application could be delayed for a considerable period of time if the application was found to be deficient because the Charities Division was not in agreement that both the purposes and the activities of the applicant were exclusively charitable at law.
- (5) Assuming that charitable status is granted by CCRA, then the effective date for charitable status will normally be back-dated to the date that the applicant was created. For a charitable not-for-profit corporation, that date will be the date of the issuance of letters patent or, in the event of a charitable trust, it will be the date of the trust agreement. A registered charity will only be able to issue charitable receipts for donations received as of, or after, the effective date of its grant of charitable status by the Charities Division.
- (6) In the process of granting charitable status, the Charities Division will designate the applicant as a charitable organization, a public foundation or a private foundation, depending upon what designation the applicant has requested and the opinion of the Charities Division concerning whether the applicant meets the statutory definition of the requested designation.
- (7) While the application for charitable status is being reviewed by CCRA, the solicitor for the applicant, assuming that the applicant has been organized as a not-for-profit charitable corporation, will arrange to have the initial organizing resolutions for the corporation prepared and an appropriate report forwarded to its board of directors explaining their responsibilities, duties and liabilities in operating a charitable corporation in Canada.
- (8) Once an applicant becomes a Canadian registered charity, then in accordance with section 230 (2) of the *Income Tax Act*, the charity will be required to keep its records and books of account at an address in

Canada. Paragraph 25 of *Information Circular 80-10R*¹⁹ states that all registered charities must have available for inspection sufficient records to allow verification of the donation receipts issued, income received, and any disbursements made.²⁰ The *Information Circular* explains what records are to be kept, the required location of the records, the method of record keeping, (including electronic records), and the retention period for such records.

- (9) Within six months of the charity's fiscal year end, it must file a Registered Charity Information Return on a prescribed form, currently T3010. The information that is required in the Registered Charity Information Return is very detailed and includes questions about the affiliation of a registered charity with organizations located outside of Canada, as well as details of any funds that are transferred outside of Canada.

What are Acceptable Charitable Activities?

Once an organization has been designated as a Canadian registered charity, it must ensure that all expenditures of its funds and resources are used for charitable activities in fulfilment of its charitable purposes. This involves the registered charity carrying out such activities itself or, alternatively, transferring money or property to a qualified donee as defined in the *Income Tax Act*.²¹ This definition includes other registered charities, but even then such payments generally may not exceed 50 per cent of the receipted income from the previous year. CCRA will generally consider any of the following activities to be those carried out by the charity itself:²²

- activities undertaken by employees of the charity;
- activities undertaken by volunteers of the charity;
- activities undertaken by agents of the charity;
- activities undertaken pursuant to a charitable joint venture in which the charity and a foreign charity participate; and
- activities undertaken by a charitable partnership in which the charity and the foreign charity participate as partners.

Based upon what is acceptable to CCRA, it is not possible for a Canadian registered charity to make payments to its counterpart in the United States though a gift of funds or resources. This is because a U.S. tax-exempt organization is not a qualified donee unless it has been included in the list of prescribed universities under the *Income Tax Act*. As a result, payments to a U.S. tax-exempt organization by a Canadian registered charity will only be possible if such payment or transfer constitutes a charitable activity that is carried out by the charity itself.

What Constitutes Acceptable Payments by a Canadian Registered Charity to its U.S. Counterpart?

Until the Draft Publication *Registered Charities: Operating Outside of Canada*²³ was released by the Charities Division in June of 1998, there was considerable uncertainty concerning what would be acceptable in relation to payments made by a Canadian registered charity to organizations located outside of Canada that were not qualified donees. Although the Draft Publication has not yet been formally adopted by CCRA, it is considered to be a relatively accurate statement of the current position of the Charities Division. It sets out general guidelines concerning how a Canadian registered charity can make payments outside of Canada, whether to a U.S. tax-exempt organization or to another non-Canadian charity. A summary of those guidelines is as follows:

- (1) A Canadian registered charity can generally make a payment outside of Canada to its U.S. counterpart if the payment is made in accordance with one of the following methods:
 - the payment is made pursuant to a contract to acquire goods or services, such as the purchase by the Canadian charity of books published by a U.S. organization;
 - the payment is made pursuant to an agency agreement as discussed below;
 - the payment is made pursuant to a joint-venture agreement as discussed below;
 - the payment is made pursuant to a co-operative partnership agreement as discussed below; or
 - the payment is made in accordance with a permitted expenditure for international membership fees as discussed below.
- (2) When a payment by a Canadian registered charity is made to a U.S. organization pursuant to an agency agreement, a joint venture agreement or a co-operative partnership agreement, the Charities Division requires that there be certain basic provisions contained within such agreement. Those requirements are summarized as follows:
 - the agreement must be in writing and must be for the primary purpose of furthering the charitable purposes of the Canadian charity;
 - the agreement must provide that the Canadian charity is to provide periodic and specific instructions concerning the application of its funds;
 - the Canadian charity must regularly monitor the payments made with respect to a project or program being undertaken pursuant to the agreement;

- the agreement must require that there be regular written progress reports given to the Canadian charity;
 - the Canadian charity must have the right to inspect the applicable project or program being undertaken; and
 - adequate records must be maintained at the address of the Canadian charity in Canada.
- (3) An agency agreement would be appropriate in situations where monies from a Canadian registered charity are transferred to a U.S. tax-exempt organization for a specific program or project. Under an agency agreement, the U.S. organization would be formally appointed as the agent of the Canadian charity to disburse certain designated monies on behalf of the Canadian charity. In addition to the general requirements already outlined above, CCRA also requires that the following additional provisions be included in an agency agreement:
- the agent, i.e., the U.S. organization, would be required to hold the monies that it receives from the Canadian charity segregated from its own funds; and
 - the U.S. organization, as agent, would need to keep separate books and records concerning the receipt and expenditure of agency funds that are received and disbursed.
- (4) A joint venture agreement would be appropriate in situations where the Canadian charity is transferring monies to a U.S. organization to carry on programs or projects on a continuing basis where both the Canadian charity and the U.S. organization are participating, even where the level of contribution from each organization is unequal. An example where a joint venture agreement is often used is where a Canadian missionary organization participates in funding continuing foreign missionary activities with a U.S. organization. When a joint venture agreement is employed, CCRA requires that there be continuing control exercised by the Canadian charity in relation to its contribution to the joint venture. Acceptable evidence of such control includes the following:
- the presence of Canadians on the governing body of the joint venture in numbers proportionate to the monetary contributions made by the Canadian charity;
 - the physical presence of Canadians at the project or in running the joint venture program;
 - the input of Canadians into the hiring and firing of personnel involved with the joint venture;
 - the input of Canadians into the initiation and follow-through of the project or the joint venture program;

- the requirement for Canadian signatures on contracts and agreements involved with the joint venture;
 - the ongoing review by the Canadian charity of the budget and financial statements of the joint venture;
 - Canadian authorship of manuals, standards, guidelines and materials used in operating the joint venture; and
 - the identification of the project or program as a joint venture involving the Canadian charity.
- (5) A co-operative partnership agreement would be appropriate in situations where the Canadian charity is entering into a partnership arrangement with a U.S. organization with each party carrying out a particular aspect of an international charitable project or program or contributing specific resources, equipment or other property for such project or program.
- (6) Revenue Canada will permit payments to a U.S. organization or other non-qualified donees as royalty payments, licence fees or international membership fees, provided that such payments are the lesser of five per cent of the total expenditures of the Canadian charity in that year and a maximum of \$5,000 (in Canadian funds). If the amount that is paid exceeds the permitted amount, the Canadian charity will be required to produce written documentation that the excess fees paid were no more than the fair market value of the goods and services that were received by the U.S. organization.

Establishing an International Structure in Conjunction with Canadian Charitable Operations

In establishing a Canadian registered charity to work in conjunction with a U.S. tax-exempt organization, it is essential to recognize that the Canadian charity is an independent and autonomous legal entity that cannot be “owned” as a subsidiary of the U.S. organization, or for that matter by any other foreign organization. This autonomy and the inability of a nonshare capital corporation to be owned through a parent/subsidiary arrangement mean that the establishment of an international structure in which the Canadian charity is a part must be carefully planned and implemented. This is often accomplished by means of a contractual arrangement between the Canadian charity and the U.S. organization, requiring that the internal structure for the Canadian charity reflect a particular pre-approved general form.

Frequently, though, a U.S. tax-exempt organization that operates in more than one country will not have developed a clear organizational structure to carry on its operations on a worldwide basis. This omission often occurs because the founding U.S. organization operates as both a domestic organization in the United States and as the overseeing body for international charitable operations. This dichotomy in roles can cause confusion, misunderstanding and even

mistrust by domestic charities in other countries such as Canada, because of a perception, real or imagined, that the founding U.S. organization is acting as a "benevolent dictator" over international operations. Such perception can cause resentment and tension, not only in the establishment of charitable operations in Canada, but also with domestic charities in other countries in which the U.S. organization carries on international operations.

Before commencing charitable operations in Canada, it is therefore important to understand how the Canadian registered charity fits into an international charitable structure and what is the applicable international structure.²⁴ In this regard, there are generally three types of international charitable structures that are commonly utilized. For the purpose of this article, they have been identified as the international co-operative model, the international subsidiary model, and the international umbrella model, each of which is briefly described below.

(1) *International Co-operative Model:* With this model, each country establishes a separate domestic charitable corporation. Each domestic charity has full control over ownership of its corporate name and associated trademarks in its own country. All domestic charities work in conjunction with each other on a consensual basis in accordance with a loose international association which may or may not be reduced to writing but, even if it is, it is normally not intended to be in the form of an enforceable arrangement. The difficulty with this model is that if one domestic charity no longer complies with the agreed on international standards, then there is little if anything that the other domestic charities, including the founding U.S. organization, can do to stop the renegade domestic charity from breaking ranks in its own country.

(2) *International Subsidiary Model:* With this model, the U.S. organization, as the founding charity, would function not only as a domestic organization in the United States but would also take on the role of the international parent organization in co-ordinating charitable activities of member domestic charities, including those of the Canadian charity. In acting in this dual role, the U.S. organization would tend to dominate, although not necessarily intentionally, international operations and to a certain extent the internal operations of each domestic charity, including those of the Canadian charity. This control is often manifested by a board of directors of the Canadian charity being dominated by board members who are either U.S. board members or are nominees of the U.S. organization. Even if there were participation by Canadian board members on the board of the U.S. parent organization, that participation would frequently be limited to a nominal or token participation. The lack of reciprocity in board membership often leads to frustration and resentment by members of the board of directors of the Canadian charity.

(3) *International Umbrella Model:* With this model, each country (including the United States) would have its own domestic charity, notwithstanding that the U.S. organization was the founding charity. A separate charitable corporation is then incorporated in one country, normally the United States, to act as

the international umbrella organization to establish, co-ordinate and enforce international standards for charitable operations for all the domestic charities, including the U.S. domestic charity. The international charity will normally own the applicable trademarks in each country and then license those trademarks to each domestic charity pursuant to a licence or other contractual arrangements. The international charity will be controlled by a board of directors elected on a proportionate basis by all participating domestic charities, including the U.S. domestic charity. However, the international charity would not control the activities of domestic charities in their own countries other than to ensure that the international standards that have been agreed upon by all the domestic charities are met.

Establishing a Franchise Control Model for Canadian Operations

No matter which international charitable structure is adopted, it is essential that careful consideration be given to establishing and implementing effective control provisions by the U.S. organization concerning certain fundamental aspects of Canadian operations. In this regard, failure properly to document the relationship between the U.S. organization and the Canadian charity could result in a disagreement arising between the two organizations, with the Canadian charity asserting that it is the owner of its name, trademarks and associated goodwill in Canada. Although a dispute of such issues would likely be resolved through negotiation or mediation, the potential for costly legal action with the resulting damage to the reputation of both organizations could be significant and must therefore be avoided at all costs. This requires, though, that the relationship and expectations between both organizations be clearly stated at the time that Canadian operations are being initiated and that such understanding be documented in writing.

An effective relationship model to consider would be that of the business franchise model. The relationship between a business franchisor and a franchisee has a close parallel to the relationship between an international parent charity and a member domestic charity. Just as an international charity cannot control the operations of a domestic charity by owning the shares of a domestic charity (because there are no shares to own), a franchisor in a business franchise will not normally own the shares of a franchisee corporation even though the franchisee corporation has shares that could be owned. Since the franchisee is not a subsidiary of the parent franchisor, the franchisor needs to exercise control over the franchisee by establishing a contractual relationship with the franchisee by means of a franchise agreement. Similarly a franchise arrangement could be implemented in dealing with international charitable operations by having the domestic charity enter into a franchise control model with the parent international charity.

The means by which a franchise control model could be established between the U.S. organization as a type of franchisor and the Canadian charity as a type of franchisee would include:

(1) *Association Agreement*: An association agreement, often referred to as a charter or affiliation agreement, would set out the basic expectations of the U.S. organization with regard to the Canadian charity. Such an agreement would reflect the similarity of charitable purposes of both organizations, a licensing of the trademarks and copyrights to the Canadian Charity, the contractual requirements of the Canadian charity in carrying out operations in Canada, the corresponding requirements of the U.S. organization, the consequences for failing to comply with those requirements, including the loss by the Canadian charity of its right to use the licensed trademarks and copyrights, as well as the establishment of a dispute resolution mechanism to avoid litigation in the event of a disagreement.

(2) *Incorporating Documents of the Canadian Registered Charity*: Part of an association agreement would include a description of the basic terms required for the incorporating documents of the Canadian registered charity. While recognizing that the Canadian charity is an autonomous legal entity that must comply with applicable Canadian laws, there is nothing to preclude the Canadian charity from entering into a contractual arrangement whereby it would agree that its incorporating documents, i.e., its letters patent and bylaws, would need to reflect certain basic requirements, provided that such requirements were not contrary to applicable Canadian law and did not overly diminish the autonomy of the Canadian charity.

The requirements in this regard would include a description of the charitable purposes that would need to be included, the general nature of the organizational corporate structure for the Canadian charity, the reservation by the U.S. organization of a right to exercise a veto over certain fundamental changes in the corporate documents of the Canadian charity, as well as the entitlement of the U.S. organization to nominate a certain number of U.S. board members as members of the board of the Canadian charity. (However, such board participation could not result in the U.S. organization exercising majority control over the Canadian board of directors, either directly by requiring more than 50 per cent membership on the board of directors, or indirectly by increasing the percentage vote required for board resolutions or the quorum to hold a board meeting beyond 50 per cent of all board members.)

(3) *Trademark Licence Considerations*: While it is beyond the scope of this article to outline the steps required effectively to protect trademarks for charities in Canada,²⁵ or to draft an effective international trademark licence agreement, there are a number of key considerations that U.S. organizations should be aware of in establishing charitable operations in Canada or in other foreign countries. Those considerations would include the following:

- The U.S. organization should identify whether its names and logos constitute trademarks that are worth protecting. If so, then such trademarks should be protected by applying for trademark registration in the United States, in Canada, and in every country that the U.S. organization

is either operating in now or is intending to operate in in the foreseeable future.

- The trademark application in Canada should be applied for in name of the U.S. organization, where possible, instead of the Canadian charity becoming the registered owner of the applicable trademarks in that country.
- A trademark licence agreement should be entered into between the U.S. organization and the Canadian charity to identify which trademarks are owned by the U.S. organization, the manner in which the trademarks can be used in Canada, as well as appropriate default provisions, including losing the right to use the trademarks in Canada in the event of a breach of the licence agreement by the Canadian charity.
- The U.S. organization should take steps to register as many internet domain names as possible that include the name and/or trademarks of the organization in conjunction with as many top level domain names as are still available, i.e., *.org*, *.com*, *.net*, as well as *.ca* in Canada. Separate trademark registration should then be secured for every domain name that is used on the internet. Even if not all of the internet domain names that are reserved become activated, the process of reserving additional domain names that otherwise could cause confusion with the primary domain name of the U.S. organization would preclude other organizations from being able to adopt potentially confusing domain names. The trademark licence agreement would include a grant of a licence from the U.S. organization to the Canadian charity of the right to use one or more specified domain names.
- In both Canada and the United States, trademark applications can be filed based upon proposed use or “intent to use” a trademark as opposed to waiting for actual usage to occur. The availability of a proposed use trademark application in Canada would allow the U.S. organization to protect key trademarks in Canada even before operations are commenced in that country. In addition, if a Canadian trademark is applied for within six months of the filing date of a trademark application in the United States, then the earlier filing date in the United States can become the effective filing date in Canada as well.
- If the Canadian charity is already operating in Canada without a licence agreement, the Canadian charity should be approached about the possibility of signing a trademark license agreement to acknowledge that the trademarks used in Canada by the Canadian charity have been used in its capacity as a licensee of the U.S. organization. However, before a Canadian charity could be expected to voluntarily give up its trademark rights, it would need to be satisfied that in return for relinquishing those rights, there would be an effective international umbrella organization

established through which the Canadian charity would have the right of proportionate input into overseeing international charitable operations, including those in Canada.

(4) *Copyright Considerations:* One aspect of establishing an effective franchise control model over operations in Canada that is often overlooked involves the licensing of applicable copyrights. This omission is in part due to complications in dealing with different copyright laws in each country as well as the impact of international copyright conventions²⁶ dealing with copyright issues in multiple jurisdictions.

Two key factors that should be considered in relation to copyright matters when creating an international structure involving charitable operations in Canada are:

- The U.S. organization should determine which of its works are subject to copyright protection and whether copyright registration is necessary. In Canada, as in the United States, copyright registration is not necessary but can be a helpful precaution in some circumstances, particularly when it involves music and other recorded works.
- The U.S. organization would also need to ensure that it had effectively licensed the copyrights in question to the Canadian charity, either as part of an international association agreement or pursuant to a separate copyright licence agreement.

(5) *Enforcing Control Provisions:* There is little point in establishing a franchise control model in relation to charitable operations in Canada unless the U.S. organization is prepared to enforce the control provisions that are set out in its association agreement or in a trademark or copyright licence agreement, if applicable. Failure to take consistent action to enforce the available default provisions could result in the Canadian charity being able to assert the doctrine of *estoppel* to preclude the U.S. organization from being able to rely upon the terms of such agreements. This is a very real concern in relation to intellectual property issues involving trademarks and copyrights. The adage of “use it or lose it” would have apt application to the perishable nature of enforcement provisions involving the licensing of trademarks and other intellectual property.²⁷

Conclusion

Although it has not been possible in this article to deal with all of the issues involved in a U.S. tax-exempt organization commencing charitable operations in Canada, the article has identified some of the key issues that would need to be addressed in creating a Canadian registered charity as well as establishing an effective international charitable structure. Although there are many similarities between the law in the United States dealing with tax-exempt organizations and the law in Canada dealing with registered charities, there are also considerable differences that require careful planning and analysis. By becom-

ing aware of the applicable issues and potential pitfalls that may be encountered, as well as the benefits from establishing an effective international structure before undertaking charitable operations in Canada, there is a better chance that the relationship between the Canadian charity and the U.S. tax-exempt organization will produce a constructive long-term relationship between the two entities, fulfilling what is ultimately the goal of both organizations: to accomplish similar charitable purposes in their respective countries and to act in concert internationally.

FOOTNOTES

1. The author would like to acknowledge the assistance of Adam Parachin, a student at Osgoode Hall Law School, York University, Toronto in reviewing and editing this article.
2. See par. 1, of Article XXI of the *Canada-United States Income Tax Convention, 1980*, as enacted in Canada by S.C. 1984, c. 20, as amended.
3. *Income Tax Act*, R.S.C. 1985, c.1 (5th Supp.), as amended (hereinafter "*Income Tax Act*" or the "*Act*"), section 118.1 (a).
4. *Excise Tax Act*, R.S.C. 1985, c.E-15.
5. *Revenue Canada Information Circular 80-10R*, "Registered Charities: Operating a Registered Charity", Charities Division, Canada Customs and Revenue Agency (CCRA), Ottawa, Ontario. (see website, www.rc.gc.ca).
6. Revenue Canada Draft Publication *RC4106E-Registered Charities: Operating Outside Of Canada*, Revenue Canada: Charities Division, Ottawa, Ontario. [Readers should note that Revenue Canada is now Canada Customs and Revenue Agency (CCRA)].
7. *Supra*, footnote 4 at 2.
8. *Ibid.*
9. *Ibid.*, at 4.
10. Revenue Canada (CCRA) Draft Publication *RC4108 Registered Charities and the Income Tax Act*, CCRA: Charities Division, Ottawa, Ontario.
11. See *Information Circular IC78-10R3*, October 5th, 1998, CCRA: Charities Division, Ottawa, Ontario.
12. See *Commissioners for Special Purposes of Income Tax v. Pemsel*, [1891] A.C. 531. See also the recent Supreme Court of Canada decision in *Vancouver Society of Immigrant and Visible Minority Women v. M.N.R.*, [1999] 1 S.C.R. 10.
13. See section 149.1 subsections (1.1), 149.1 (6.1), and 149.1 (6.2) of the *Income Tax Act*, *supra*, footnote 3. See also *Information Circular 87-1, Registered Charities - Ancillary and Incidental Political Activities*, CCRA, Ottawa, Ontario. See also the recent Federal Court of Appeal decision in *Human Life International in Canada Inc. v. M.N.R.*, [1998] 3 F.C.202, [1998] 3 C.T.C.126, 98 D.T.C. 6196 [F.C.A.]. Leave to appeal to the Supreme Court of Canada was denied on January 21, 1999.
14. See section 149.1(1) of the *Income Tax Act*, *supra*, footnote 3 which defines a "related business" to include a "business that is unrelated to the objects of the charity if substantially all persons employed by the charity in the carrying on of that business are not remunerated for that employment". This definition in effect provides permission for a registered charity to operate an unrelated business provided that it is substantially operated by volunteers.

15. *Astgen v. Smith*, [1970] 1 O.R. 129 (C.A.).
16. *Religious Organization Lands Act*, R.S.O. 1990, c.R-23.
17. *Canada Corporations Act*, R.S.C. 1970, c.C-32.
18. *Corporations Act*, R.S.O. 1990, c. C-38.
19. *Supra*, footnote 5.
20. *Supra*, footnote 10.
21. A qualified donee is defined under section 110.1, subsection (1) (a) and (b) of the *Income Tax Act* as:
 - a registered charity;
 - a registered Canadian amateur athletic association;
 - a not-for-profit housing corporation resident in Canada;
 - a municipality in Canada;
 - the United Nations or an agency thereof;
 - a university located outside of Canada that is prescribed to be a university which ordinarily includes students from Canada;
 - a charitable organization located outside of Canada to which the Government of Canada has made a gift during the taxation year or in the 12-month period preceding the year; and
 - the Government of Canada or a province in Canada.
22. *Supra*, footnote 5.
23. *Supra*, footnote 6.
24. For a more complete discussion of the issues involving the establishment of an effective international charitable structure, reference can be made to a paper by the author, entitled "National and International Charitable Structures: Achieving Protection and Control" in *Fit to be Tithed 2: Reducing Risks for Charities and Not-for-Profits*, (Toronto: Department of Continuing Legal Education, Law Society of Upper Canada, November 26, 1999, also available on the internet at www.wardlaw.on.ca).
25. For a more detailed discussion of the importance of trademark protection for charities in Canada and how to avoid trademarks becoming wasting assets, reference can be made to an article by the author entitled "Avoiding Wasting Assets: Trade-Mark Protection for Charities", in *Charity and Not-for-profit Law: The Emerging Specialty*, (Toronto: Canadian Bar Association of Ontario, Continuing Legal Education Program, May 15, 1998, also available on the internet at www.wardlaw.on.ca).
26. See, for example, the *Universal Copyright Convention* of 1952, the *Revised Convention of Berne*, signed November 13, 1908, and the *Additional Protocol Thereto* signed March 20, 1916, as well as the *International Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organizations* concluded at Rome on October 26, 1961.
27. For a more detailed discussion of enforcement provisions involving international charitable structures, see "National and International Charitable Structures: Achieving Protection and Control", *supra*, footnote 24.