Canadian Charities and Foreign Activities

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Canadian charities that operate abroad are in the forefront of dealing with many of the most difficult global problems, including HIV/AIDS, human rights, access to education, and clean water and sanitation, to name a few. Many donors have lived abroad and have a substantial attachment to causes and communities outside of Canada, and many consider themselves "global citizens" and are motivated by the enormity of global problems. Other philanthropists are impressed with the huge effect that their donations can have in a developing country—often many times greater than the same funds used at home. With the increasing value of the Canadian dollar, the impact of spending Canadian dollars abroad has dramatically increased.

A large number of Canadian charities operate to some degree outside of Canada. The latest statistics[2] from the 2006 T3010s indicate that of the 83,223 registered charities that filed that year, 12,319 charities identified themselves as carrying on programs directly or indirectly outside of Canada. This number represents over 15 percent of Canadian registered charities. The amount spent by these charities outside of Canada has risen from $1.4 billion in 2002 and $1.8 billion in 2004 to $2.3 billion in 2006.

This article will attempt to assist Canadian charities that are conducting or are interested in conducting programs outside of Canada with some of the legal issues that they may face. It will discuss the statutory and regulatory framework for Canadian charities operating abroad, describe the permissible structured relationships and agreements, review a number of cases dealing with Canadian charities operating abroad, and highlight some of the challenges facing Canadian charities that have foreign activities.

The Charities Directorate of the Canada Revenue Agency (CRA), the federal government department tasked with approving and regulating registered charities in Canada, is very concerned with the low level of compliance with CRA's rules on foreign operations by Canadian charities operating abroad. Recently, CRA as part of its Charities Partnership and Outreach Program, identified "conducting foreign activities in compliance with a charity's obligations under the *Income Tax Act*" as a major CRA concern. A number of articles have been written over the years on the subject of foreign activities by Canadian charities.[3] (Foreign charities wishing to operate in Canada, as opposed to Canadian charities wishing to operate abroad, may wish to review my article entitled "Foreign Charities Operating in and from Canada."[4])

Good Work Outside the Registered Charity Realm

Before giving a detailed review of the legal issues facing Canadian charities that operate abroad, I would be remiss in not mentioning that there are many ways to perform good work abroad that are outside the charitable sector and the scope of this article. For example, you could:

1. make personal donations of cash or in-kind items to foreign charities, with no tax receipt from a Canadian charity;
2. have your business make a donation to a foreign charity or cause with no tax receipt received, provide sponsorship to a foreign charity, or advertise in the publication of a foreign charity;
3. invest in developing countries or set up a branch of your business in a developing country;
4. establish a for-profit "nonprofit," which is a for-profit corporation set up with the intention of helping people rather than making a profit (examples include Google.org and many for-profits involved with micro-loans);
5. establish and utilize a Canadian nonprofit corporation without charitable status—this is particularly useful if your donor, such as the Canadian government, does not need a tax receipt;[5] or
6. volunteer at home or abroad.

In addition, many Canadians remit funds to their families, friends, or former employees in other countries, but they do not receive any tax benefit from it.[6]

It is always important to keep in mind that there are alternatives to being a registered Canadian charity. If a group wishes to avoid being constrained by the rules for Canadian charities conducting foreign operations, then they should consider operating as a for-profit or nonprofit entity, not as a registered charity.

CRA Publications

CRA has prepared two useful publications on Canadian charities operating abroad: "Registered Charities: Operating Outside Canada (RC4106)"[7] and "Registered Charities Newsletter No. 20." In addition, CRA has developed Policy Statements, Consultations on Proposed Policy, a paper,[8] and Information Letters[9] that provide additional information on CRA views relating to charities operating abroad, all of which are available on the CRA website.

CRA is at the time of writing this article reviewing its policies on Canadian charities operating outside of Canada. While no one knows what the review will yield, it will probably incorporate some of the case law discussed in this article and provide greater assistance to charities in complying with their obligations under the *Income Tax Act*.

General Restrictions Similar to Other Registered Charities

Some of the requirements imposed on Canadian charities operating abroad are similar to those imposed on Canadian charities operating in Canada, such as

the following: a prohibition on partisan political activities; a limitation on non-partisan political activities; a prohibition on violating Canadian public policy; a requirement to operate within the objects of the charity; a requirement to undertake charitable activities only; an obligation to avoid any support for terrorism; a requirement to accurately prepare and file the T3010 Registered Charity Information Return within six months after the charity's year-end; and a requirement to comply with disbursement quota obligations. Registered Canadian charities that conduct foreign operations not only have to comply with the same rules that apply to Canadian charities that only operate in Canada but also have additional obligations, as discussed below.

Corporate Objects and Trust Agreement

If a charity is a corporation, it should ensure that its objects allow for activities outside of Canada before embarking on such activities abroad. The Letters Patent/Articles of Incorporation contain the objects of the corporation. A charity wants to avoid operating outside the scope of its objects; otherwise, such actions would be outside the charity's legal authority (*ultra vires*). The consequences of acting *ultra vires* can result in the actions undertaken or decisions made being null and void, the revocation of charitable status, and, potentially, personal liability for the directors of such a charity.

Examples of appropriate object clauses can be found in the *Ontario Not-For-Profit Incorporator's Handbook* at the Ontario Public Guardian and Trustee website. As well, CRA has recently released some model objects on its website.[10]

Some pre-approved clauses are: "To relieve poverty in developing nations by providing food and other basic supplies to persons in need"; "To improve the quality of drinking water in developing nations by constructing wells and water treatment, irrigation and sewage treatment systems"; or "To advance and teach the religious tenets, doctrines, observances and culture associated with the (specify faith or religion) faith." An example of an object clause that would require modification in order to allow foreign operations is "To establish and maintain a hospital in Mississauga, Ontario."

A 'standard' foundation clause might have the following wording: "To receive and maintain a fund or funds and to apply all or part of the principal and income therefrom, from time to time, to charitable organizations that are also registered charities under the *Income Tax Act* (Canada)." This clause allows for the transfer of funds to Canadian registered charities but would not allow a foundation to carry out directly work abroad or have an agreement with a non-qualified donee to transfer funds.

The type of objects that are defined as charitable fall into one of four categories accepted by CRA and by the courts, namely to relieve poverty, advance education, advance religion, or benefit the community as a whole. In addition to fitting under one or more of the four categories, the charity must also be established for

the benefit of the public or a sufficiently large segment of the public, also known as the "public benefit test." CRA will expect that the public benefit is tangible; the beneficiaries are either the public-at-large or a sufficiently large segment of the public; benefits will not accrue to private individuals or members except under certain limited circumstances; the organization cannot restrict delivery of benefits to a certain group without adequate justification; and the organization cannot charge fees which have the effect of unduly excluding members of the public.

If the objects of the corporation are too broad and could include non-charitable activities or could have significant private benefit, then the corporation may not be successful in obtaining registered charity status, as discussed below in the *Travel Just* case. On the other hand, if the objects are too narrow, the charity will have trouble effectively conducting its activities.

If the charity is set up as a trust, then the charity should ensure that the Trust Agreement does not preclude operations outside of Canada. As well, if there are specific restrictions attached to a donation, the restrictions could preclude the funds from being spent outside of Canada, and they need to be observed. Other restrictions may be imposed on the activities of a charity either in the Notification of Registration received from CRA when the charity first received registered status or if the charity before or after registration provided to CRA an undertaking or entered into a compliance agreement. These restrictions, undertakings, or agreements can affect what operations are carried on by the charity and how they are carried on.

What Are Charitable Foreign Activities Under Canadian Law?

Although what is considered charitable under Canadian law for operations in Canada is very similar to what is considered charitable for operations outside of Canada, it is not identical. Canadian charities operating in Canada are allowed to undertake certain activities that Canadian charities operating abroad may not be allowed to do. The example given in RC4106 is that while it may be charitable for a Canadian charity in Canada to help the Canadian government reduce its debt, it is neither charitable nor permissible under Canadian law for a Canadian charity to reduce a foreign country's debt. As well, it may be considered charitable in certain circumstances for a Canadian charity to offer technical assistance to other registered Canadian charities, but it may not be considered charitable for a Canadian charity to offer technical assistance to foreign charities.

General Rule for Foreign Activities by Canadian Charities

The *Income Tax Act* (Canada) allows charities to conduct their charitable purposes by: 1) giving money or assets to another "qualified donee" (as defined below); or 2) conducting their "own activities" (at home or abroad). There is no 'third option'. A Canadian charity cannot just transfer or grant money to a foreign NGO or charity. In general, the same notion applies to operations within Canada.

A Canadian charity cannot just give or transfer funds to another Canadian organization that is not a qualified donee (e.g., a registered charity).

Transfers to Another Qualified Donee

Qualified donees are organizations that can, under the *Income Tax Act* (Canada), issue official donation receipts for gifts that individuals or corporations make to them.

Qualified donees include:

- registered charities;
- registered Canadian amateur athletic associations;[11]
- registered national arts service organizations;
- housing corporations in Canada set up exclusively to provide low-cost housing for the aged;
- a municipality;
- a municipal or public body performing a function of government in Canada;
- the United Nations and its agencies;[12]
- universities outside Canada with a student body that ordinarily includes students from Canada (these universities are listed in Schedule VIII of the *Income Tax Regulations*);[13]
- charitable organizations outside Canada to which the Government of Canada has made a gift during the donor's taxation year, or in the 12 months immediately before that period;[14] and
- the Government of Canada, a province, or a territory.

A Canadian charity can transfer funds or assets to another qualified donee. For example, a Canadian charitable organization with no experience in foreign operations that wishes to aid people in Darfur may decide to support Doctors Without Borders Canada, a Canadian qualified donee. There is no need from a CRA point of view to have an agreement between the donor charity and Doctors Without Borders Canada. If the donor charity wishes to restrict the gift to Darfur, then it may wish to have a direction or agreement to that effect. Similarly, if a donor requested that his or her donation to a community foundation (qualified donee) should be applied toward dealing with the issue of AIDS in sub-Saharan Africa, the foundation could transfer the funds to the Stephen Lewis Foundation or Canadian Crossroads International, both qualified donees, without the need for an agreement or monitoring. For many Canadian charities that do not have experience in direct charitable activities outside of Canada, a donation to another qualified donee is the simplest and safest way to have a global impact.

"Own Activities" and Intermediaries

Foreign charities and NGOs are rarely qualified donees. Therefore, as a general rule, a Canadian charity cannot transfer funds or assets to them except in further-

ance of the Canadian charity's "own activities" in a structured arrangement, as discussed below.

There are a number of different structured arrangements through which a Canadian charity can operate abroad, including: 1) Canadian employees or volunteers of the Canadian charity directly working abroad; 2) agency agreements with an agent; 3) contractor agreements; 4) joint venture agreements/joint Ministry agreements; and 5) cooperative partnership agreements.

1) Canadian Employees or Volunteers

Some Canadian charities send their own employees or volunteers abroad in order to conduct the Canadian charity's activities. For example, a medical relief organization in Canada may send a Canadian doctor to a developing country to provide medical help to those who cannot afford it or to assist with a natural disaster. A Canadian church may send a missionary abroad to conduct religious activities. There are many advantages of sending your own employees abroad, including using the skill and knowledge of Canadians, using your employees' understanding of your organization and its belief/philosophy, having control over the employee, and having the ability to harness employees' experience on their return to Canada.

However, many Canadian charities operating abroad find that it is not always possible to send Canadian employees abroad. Sometimes, because of logistical reasons, costs, language, culture, security, or other reasons, Canadian charities prefer to contract with foreign intermediaries to conduct the activities. Although CRA does not require a written employment agreement, charities should always have an employment agreement with employees, whether or not they are working in Canada.

2) Agency Agreement

The most commonly used method of operating abroad is through an agency agreement. The Canadian charity appoints an agent to conduct the Canadian charity's activities on behalf of the Canadian charity. The Canadian charity provides all of the funding and is in control of the relationship pursuant to a written agency agreement. This is one of the most popular methods of Canadian charities operating abroad.

An example would be a Canadian development organization entering into an agency agreement with an organization in Bolivia to provide food to needy children. The activities carried out by the Bolivian agent would be on behalf of the Canadian charity. The project would be a project of the Canadian charity. Either the Bolivian agent, who is on the ground and knows more about local conditions, or the Canadian charity, could suggest projects. However, all projects and budgets need to be approved by the Canadian charity's board of directors. The Bolivian agent must report, pursuant to the requirements of the agency agreement, to the Canadian charity on the project.

The concern with agency agreements is that the Canadian charity, as principal, is liable for the actions of the agent. As well, there is sometimes legitimate resentment by the agent, especially in the international development context, that the Canadian charity is controlling the project and relationship and the foreign charity is the "agent" of the Canadian charity. The relationship does not seem equal or fair. After all, it is not a partnership or joint venture (those models are discussed below). Another concern with agency agreements is that the funds are considered to have been used by the Canadian charity for financial statement/accounting and disbursement quota purposes only after they have been expended by the foreign agent.

Another concern with the agency agreement structure is the requirement for the agent to segregate the agent's Canadian funds from its other funds. CRA has noted in an information letter (CIL-1997-003):

> In general, the segregation of principal and agent funds should be respected. Where commingling takes place, we would require a complete and detailed accounting for every expenditure out of the mixed fund. The invoicing procedure you describe, if applied to all expenditures involving the Canadian charity's funds, would seem to satisfy this requirement. … We would point out that where the funds of several organizations are commingled, this will not necessarily be legitimized by the adoption of a joint ministry agreement.

Many organizations view segregation of funds as cumbersome. However, if one decides to use the agency model, then one may realize that there are advantages to having a separate bank account, including the reduced likelihood that co-mingled funds will be deliberately or unintentionally spent on unauthorized activities. If you are monitoring the activities of your agent, would it be easier to review 100 transactions related to your project or 10,000 transactions related to all the projects of the agent? Additionally, if CRA audits the Canadian charity, it is doubtful that the foreign charity will be excited about providing complete information on all its banking transactions. Sometimes it would be a lot simpler if the Canadian funds were in a separate bank account and were dealt with separately.

3) Contractor Agreement

A Canadian charity can also retain a foreign contractor to conduct certain work. For example, a Canadian charity that is interested in providing clean drinking water could, by written agreement, employ a contractor in a developing country to dig a well. This type of agreement would have many similar features to an agreement between a Canadian charity and a for-profit company in Canada. The contractor could be either a for-profit entity or a nonprofit. Contractor agreements are becoming more popular in relationships between Canadian charities and foreign charities. The advantage of this type of independent contractor relationship is that of limited liability. The contractor is an independent entity responsible for its own actions. This is not to say that the Canadian charity could

not be dragged into litigation if there were a problem, but it is less likely to be held responsible for the actions or inactions of the contractor. Foreign contractors do not need to segregate the funds of the Canadian charity, as agents do. Also, once funds are transferred from the Canadian charity to the foreign contractor, the funds have been spent and are no longer on the books of the charity and can be used to meet the charity's disbursement quota obligations. A very clear written agreement as to exactly what the contractor's obligations are, remuneration, ownership of work, etc., is required.

4) Joint Venture/Joint Ministry Agreement

A Canadian charity can work jointly with a foreign person or entity pursuant to a joint venture agreement, and they can pool their resources to carry out certain charitable work. The Canadian charity would need to have control of the charitable work at least in proportion to the funds that the Canadian charity is contributing. This type of agreement is popular because it can be used when two or more entities are pooling their resources with respect to a particular project—in many cases with international charities there could be ten or twenty parties to the joint venture, which can also make the agreement cumbersome.

An example of a joint venture is a Canadian charity and a U.S. charity working together on an educational project in India. The Canadian charity contributes 15% to the cost and the U.S. charity contributes 85%. The Canadian charity will have at least 15% representation on the management committee of the joint venture and must have input on all of the decisions of the joint venture. Therefore, the Canadian charity will have control over the project that is proportionate to the amount it contributed. Some joint venture agreements are for a particular project and others relate to a number of projects. Some joint ventures have a mechanism for adjusting the amounts that each party contributes, with a consequential adjustment in representation on the management committee.

Additional Joint Venture Requirements

CRA also has identified in RC4106 additional guidelines relevant to joint ventures to ensure proportionate ongoing control. These are:

- the presence of members of the Canadian charity on the governing body of the joint venture;
- the presence in the field of members of the Canadian charity;
- joint control by the Canadian charity over the hiring and firing of personnel involved in the venture;
- joint ownership by the Canadian charity of foreign assets and property;
- input by the Canadian charity into the venture's initiation and follow-through, including the charity's ability to direct or modify the venture and to establish deadlines or other performance benchmarks;
- the signature of the Canadian charity on loans, contracts, and other agreements arising from the venture;

- review and approval of the venture's budget by the Canadian charity, availability of an independent audit of the venture, and the option to discontinue funding;
- authorship of procedures manuals, training guides, standards of conduct, etc., by the Canadian charity; and
- on-site identification of the venture as being the work, at least in part, of the Canadian charity.

The concern with a joint venture agreement is the liability that the Canadian charity may face from the actions of its joint venture partners. It is possible to reduce the risk by separately incorporating the joint venture and by actively managing the joint venture risk by being very involved with the management of the joint venture.

5) Cooperative Partnership Agreement

In the cooperative partnership model, a Canadian charity works with a foreign entity and each contributes different resources and undertakes a different part of the project. This arrangement is different from a joint venture in which the parties pool their resources together.

An example of a cooperative partnership would be a Canadian group providing an x-ray machine to a clinic in Malawi. The clinic provides the space and the technicians to use the equipment. Both parties are working together to achieve a charitable end; however, they are each contributing something different to the partnership.

The concern with a partnership is the liability that the Canadian charity may face for the actions of its partner(s).

Summary of Structured Arrangements

The simple way to conceive of the five structured arrangements is as follows:

- If a Canadian charity is sending employees or volunteers outside of Canada and no funds are being transferred to any foreign organization, then a *volunteer* agreement or *employment* agreement would probably be used between the Canadian charity and the employee/volunteer.
- If a Canadian charity is contributing 100% of the money to a charitable project being carried out abroad by a foreign NGO that is not a qualified donee, then the agreement traditionally was an *agency* agreement. Increasingly, *contractor* agreements are being used.
- If a Canadian charity and a foreign organization that is not a qualified donee are contributing money to a project and putting that money together in a joint account ("pooling resources"), then it will probably be a *joint venture* agreement.
- If a Canadian charity and a foreign organization that is not a qualified donee are contributing different resources to the project, i.e., money, ma-

terial, staff, etc., then it will probably be a *cooperative partnership* agreement.

Elements of "Own Activities"

The Canada Revenue Agency has identified in RC4106 certain elements that are required in order for the foreign activities of a Canadian charity to be considered the "own activities" of the Canadian charity:

1) *The charity has obtained reasonable assurance before entering into agreements with individuals or other organizations that they are able to deliver the services required by the charity (by virtue of their reputation, expertise, years of experience, etc.).* I would compare this to due diligence in the purchase of a business—if you are going to transfer large amounts of money to an agent to undertake your charity's work, you need to satisfy yourself that they have the capacity, skills, interest, honesty, etc., to carry out the work. This step is vital—without the right intermediary (i.e., individual or organization), a Canadian charity can cause more harm than good. Have you or other trusted charities ever worked before with this organization? Have you met the intermediary in person? Have you visited the site of their activities? Can the intermediary carry out all the Canadian charity's work or will some have to be subcontracted out? Are there conflicts of interests? Has the intermediary or any of its principals ever been involved with illegal or nefarious activities? Have you received a number of positive references?
2) *All expenditures will further the Canadian charity's objects and constitute charitable activities that the Canadian charity carries on itself.* The objects or formal purposes of the charity are found in the Letters Patent of the charity. Charities are restricted to carrying out activities that are within their objects. What is 'charitable' under Canadian law is an evolving area but, as discussed above, what is charitable in Canada is broader than what is charitable abroad.
3) *An adequate agreement is in place.* CRA requires that any agreement must be in writing and must contain the minimum elements outlined below. While CRA considers having a written agreement essential to showing "own activities," many charities have had problems because having such written agreements, while necessary, is only a small part of demonstrating direction and control. CRA has for a while also been requiring that new applications for charity registration that involve foreign activities using intermediaries include a draft agreement.
4) *The charity provides periodic, specific instructions to individuals or organizations when appropriate.* In Registered Charity Newsletter #20, CRA advises that "The charity must maintain sufficient control to ensure that its resources are devoted to charitable purposes. The amount of control will vary by the nature of the resources being used and the characteristics of the foreign organization." After the charity and the intermediary

agree on a clear description of the activity, there will be monitoring and reports. As a result of receiving interim monitoring and reports, the charity may provide additional instructions or directions to the intermediary to act upon.

5) *The charity regularly monitors the progress of the project or program and can provide satisfactory evidence of this to the Canada Revenue Agency.* The two elements are regular monitoring and satisfactory evidence. With respect to regular monitoring, although required by CRA, I would argue that no donor should contribute to a charity that does not regularly monitor its activities. The monitoring could take place on the ground by the Canadian charity, or by a third party, or by the foreign NGO reporting on the progress with the Canadian charity by reviewing the reports and requesting further information or clarifications when necessary. Satisfactory evidence will depend on the circumstances. Having a site visit by a director or employee of the Canadian charity is good, especially with larger projects; however, if no detailed written report is provided by the director or employee to the Canadian charity, then the visit is of little use in showing 'satisfactory evidence'. As well, although it may be useful to have a Canadian representative on the board of the intermediary, or an intermediary representative on the board of the charity, one needs to manage potential conflicts of interest, and board representation alone is far from adequate in showing direction and control. (See the section on books and records below.)
6) *Where appropriate, the charity makes periodic payments on the basis of this monitoring (as opposed to a single lump sum payment) and maintains the right to discontinue payments at any time if it is not satisfied.* "Where appropriate" probably means that if you have a $10,000 budget, you may not need periodic payments, especially if it is a long-term relationship. However, foreign entities frequently balk, in my opinion unreasonably, at this requirement. In the event that a Canadian charity is funding the building of twenty schools, each costing $50,000 for a total budget of $1 million, I see nothing wrong with sending funds for five schools at a time, and when those schools are satisfactorily completed sending along the next payment. The periodic payments need to be based on monitoring and on demonstrated performance by the intermediary; otherwise, the periodic payments serve little use in ensuring that there is direction and control. I think it would be generally not prudent for the Canadian charity to wire transfer $1 million in the example above and hope for a detailed report at the end. Many charities also retain a hold back, which will be sent once reporting is completed.

Written Agreement

CRA has identified certain minimum requirements with respect to the written agreements between a Canadian charity and a foreign entity in RC4106, which provides:

Written agreements should typically include at least the following information:

1) names and addresses of all parties;
2) the duration of the agreement or the deadline by which the project must be completed;
3) a description of the specific activities for which funds or other resources have been transferred, in sufficient detail to outline clearly the limits of the authority given to the recipient to act for the Canadian charity or on its behalf;[15]
4) provision for written progress reports from the recipient of the Canadian charity's funds or other resources, or provision for the charity's right to inspect the project on reasonably short notice, or both;
5) provision that the Canadian charity will make payments by installments based on confirmation of reasonable progress and that the resources provided to date have been applied to the specific activities outlined in the agreement;
6) provision for withdrawing or withholding funds or other resources at the Canadian charity's discretion;
7) provision for maintaining adequate records at the charity's address in Canada;
8) in the case of agency agreements, provision for the Canadian charity's funds and property to be segregated from those of the agent and for the agent to keep separate books and records; and
9) the signature of all parties, along with the date.

CRA is not just looking for the existence of an agreement and the form of agreement but also the actual implementation. In CIL-1994-001, CRA noted:

> Once the agreement is in place, the Canadian charity must in fact show a reasonable degree of on-going interest and control in the project carried out by the agent, to such an extent that it might, for example, be able to withhold funds if at any stage in the project the agent's work is not satisfactory, or to the extent that it might require the agent to account for the project's progress so far. Vouchers, if any, or other documentation related to the carrying out of the project by the agent should be part of the charity's records, available in Canada. The charity's continuing eligibility for charitable registration will depend on whether or not it is in fact maintaining sufficient degree of ongoing control as required by the Act and provided for in the agreement.[16]

In information letter CIL-1998-027, CRA noted that a predecessor draft of RC4106 "… essentially describes the minimum elements Revenue Canada requires for arrangements that charities may use to show that they retain direction and control of their resources." In this increasingly competitive area of international philanthropy, few charities are going to excel by following only the minimum standards.

I have seen Canadian charities try to use what they claim to be CRA 'requirements' to try to take advantage of foreign organizations by imposing additional onerous conditions and restrictions in their agreements beyond those required by CRA.[17]

The relationship between a Canadian charity and an intermediary should be balanced. On the one extreme, there are some Canadian charities that are completely deferential for religious, ideological, or other reasons to the foreign organization,

and they have no interest in controlling or questioning any of the activities. On the other hand, there are Canadian charities, in many cases who know little about implementing a program in a foreign country, that are prepared to micromanage every aspect of the program, want to completely dominate the relationship, and end up causing more harm than good. There is an appropriate middle ground in the relationships between Canadian charities and foreign intermediaries. When and if the relationship involves the transfers of assets and funds, then the RC4106 rules need to be followed.

Transfer of Assets to Foreign NGOs and Charities and Others

Canadian charities operating abroad should maintain ownership and control over all of their assets. In general, the Canadian charity can only sell these assets at fair market value or transfer them to another Canadian qualified donee. Except as provided below, a Canadian charity cannot just transfer assets to a foreign charity or NGO that is not a qualified donee.

Charitable Goods Policy

CRA has a charitable goods policy, which allows certain limited types of goods to be transferred to a foreign organization or given away, in some cases without the need for a written agreement. Frequently cited examples include food in a famine situation or prayer books. However, there are limits to CRA's charitable goods policy, and CRA is very concerned that the charitable goods may be used for non-charitable or private purposes. In those cases, it is important that the charity impose controls on the use of the goods.

The basis of the 'charitable goods policy' is a CRA Staff Memo produced in 1985 and cited in the *Canadian Magen David Adom* case (hereafter "*CMDA*"), which provides:

> Equally acceptable are transfers of goods and services that are directed to a particular use by the very nature of the goods and services so transferred. Examples of such transfers include:
>
> - transfers, by a research organization, of books and scientific reports to anyone interested (including foreign governments, libraries, schools, etc.),
> - transfers of books,
> - on a subject of particular interest to an educational charity,
> - to public libraries in major cities all over the world,
> - transfers of medical supplies to a refugee camp,
> - transfers of food, blankets, etc., to a charity coping with a natural disaster,
> - transfers of drugs, medical equipment, etc., to poorly equipped hospitals,
> - transfers of personnel to schools or hospitals (on loan).

The CRA Staff Memo also provides that:

> Transfers of goods or services can more easily be viewed as charitable activities per se. The transfer of a piece of equipment that is meant to be used *only* for charitable

purposes to an organization that will *clearly* use it for such purposes is *likely* to be a charitable activity. [emphasis added]

In Registered Charities Newsletter #20, CRA advises:

> …the Charities Directorate will consider a transfer of property reasonable where the *nature of the property* means that it can *only* be used for a charitable purpose. For example, it is generally reasonable to assume that a copy of the Bible will be used for religious activities, that medical equipment will aid the sick, and that student books will be used for educational purposes in a school. In some cases, where the property could be used for something other than charitable purposes, it may none-the-less be unreasonable to expect the charity to maintain control of assets. The Charities Directorate will consider such situations on a *case-by-case basis when requests are received in writing*. [emphasis added]

As can be seen from the italicized parts of the above two quotes, the charitable goods policy in the *CMDA* case or Newsletter #20 is anything but a foundation upon which to base charitable operations abroad, unless you have requested in writing consent from CRA and CRA has agreed in writing to that request.

When could the charitable goods policy be useful? Perhaps it may be appropriate in the provision of a small amount of a clearly charitable product such as food in a country experiencing a famine, where it is an emergency, and the charity involved is dealing with a reputable agency that is non-political, non-sectarian, and the agency is acting as the charity's representative in distributing the food.

Prohibition on Foreign Ownership

CRA has accepted that in certain countries there are prohibitions on a Canadian/outside charity owning real estate, and it may be necessary for a local charity or government institution (which would not be a qualified donee) to hold the real estate. The local charity or government institution would have to give written assurances to the Canadian charity that the building or land will be used for charitable purposes.

In Registered Charities Newsletter #20, CRA advised that:

> …if there are legal impediments to the Canadian charity constructing or holding title to real property in a foreign country, the Canadian charity should get a letter from the country's embassy or consulate to confirm the law in this matter. In such circumstances, the Charities Directorate will accept that title to the facility vests in a body other than the Canadian charity, if:
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> - it can be demonstrated that the facility is being built and will be used indefinitely for exclusively charitable purposes; and
> - title to the facility vests either:
>   - in a locally recognized charity (proven by a letter from the appropriate authority that regulates charities in the foreign country); or
>   - in a government body.

The written agreement implementing such a project should include a clause stipulating the title-holding arrangements for each capital property undertaking.

Development Work

The third exception deals with the transfer of assets as part of development work. A Canadian charity can turn over to local control bridges, roads, wells, etc., that are part of a development initiative as long as the charity receives written assurances that the structures or equipment will continue to benefit the community.

Repayment of Actual Debt

CRA noted in CIL-1999-009 that "…a registered charity, in particular a charitable organization, can repay a loan to a creditor regardless of whether or not the creditor is resident in Canada and a Canadian registered charity. However, the books and records of the Canadian charity must evidence that such a debt exists."

Tithes, Membership, or Other Fees to Related Foreign NGO

In RC4106, CRA acknowledged that many charities are affiliated or associated with foreign NGOs that are typically not qualified donees and that those organizations may confer goods and services on the Canadian charity in return for the payment of tithes, royalties, membership fees, or other payments. The goods or services may include intellectual property rights such as a license to use a trademark or copyrighted literature and materials. The services may also include consulting services or professional training.

CRA takes the position in RC4106 that "We are generally willing to accept that a Canadian charity is receiving value for its payments when only a small amount is involved. For these purposes, we will probably consider a small amount to be the lesser of 5% of the charity's total expenditures in the year and $5000." Alternatively, if the amount is greater, CRA advises that the "Payments to related organizations are only acceptable where the amount paid by the charity can reasonably be regarded as proportional to the benefit it receives."[18]

CRA cautions: "If the fees are excessive, we may regard the payment as a gift by the Canadian charity to a non-qualified donee." CRA continues: "Payments made to related organizations outside the country should be clearly identified as such in the charity's books. Where the payments exceed a small amount, as described above, the charity should be able to document the actual goods and services it is receiving in exchange for the payments, or demonstrate that they were made under a properly structured arrangement."

Canadian charities are sometimes confused as Canadian qualified donees affiliated with other qualified donees can transfer large amounts of funds because of tithes, membership fees, royalties, and other fees from one to the other. However, once the transfer is to a foreign entity and above the lesser of the de minimis percentage

or amount discussed above, then the Canadian charity needs to demonstrate that it received goods or services or have a structured arrangement in place.

Books and Records

Books and records for Canadian charities operating abroad should generally be in either English or French[19] and kept in Canada. From the CRA point of view, books and records are required to be able to substantiate the qualification of the Canadian charity for registration and to permit verification of donations. As well, in terms of foreign activities, the books and records show how the charity's funds and resources are used, show that the charity is actively involved with the activity, and assist in the accurate completion of the T3010.

RC4106 requires charities to keep records of the regular direction that the charity provides to the foreign intermediary, to monitor the structured arrangements, and to obtain "reasonable reports on the progress of its projects and programs." What is reasonable in one circumstance may be different in another. These reports should be supported by backup evidence such as copies of written agreements, deeds, financial statements, invoices, photos, minutes of meetings, and any other materials that reflect the charity's ongoing participation and that show how the charity's funds are used. The frequency of reporting will depend on the agreement, but CRA suggests that progress reports should be received before sending payments by installment and that many charities have these reports filed quarterly.[20] In RC4106, CRA makes specific suggestions for recordkeeping with respect to Agents,[21] Contractors,[22] Joint Ventures,[23] Cooperative Partnerships,[24] and CIDA projects.[25] CRA's publication IC78-10R4 also has further details. If a charity needs to request books and records prior to an audit instead of receiving information on a regular basis, then it will be more difficult to demonstrate to CRA that the charity is monitoring its own activities.

In terms of records retention, charities are required to keep duplicates of receipts for at least two (2) years from the end of the calendar year in which the donations were made. Most other documents need to be kept for six (6) years from the end of a fiscal year. Some other records must be retained in perpetuity or until two (2) years after the charity is no longer a charity, such as "ten-year gifts," minutes of meetings, and all governing documents, such as letters patent.

Failure to keep adequate books and records is a ground for revocation. As well, without adequate books and records, a charity will have a difficult time monitoring the intermediaries' activities and convincing a sophisticated or observant donor that the funds donated to the charity were properly spent. If in doubt, it is better to keep more information rather than less.

Case Law on Canadian Charities Operating Abroad

Recent Canadian cases such the *Tel-Aviv Foundation* case, the *Canadian Magen David Adom* case, the *Bayit Leplitot* case, and the *Travel Just* case, all decided

in the last few years, should be of particular interest to Canadian charities that operate outside of Canada.[26] I deal with the four cases below.

The Canadian Committee for the Tel Aviv Foundation v. Canada (2002 FCA 72)

The *Tel Aviv Foundation* case deals with a Canadian charity set up to promote education and the relief of poverty in Tel-Aviv, Israel. The Canadian charity had an agency agreement with the Tel Aviv Foundation. In 1990, CRA conducted an audit in which it noted its concern that the Tel Aviv Foundation's overseas expenditures were not properly documented. In 1993, there was another audit in which it was revealed that, apparently, the new Israeli management of the Tel Aviv Foundation was not aware of the agency agreement. In 1996, the Tel-Aviv Foundation made undertakings to CRA to "conform strictly to the requirements of Revenue Canada, including the specific provisions of the Agency Agreement."

In 1997, there was a further CRA audit in which CRA expressed concern with the following:

- violation of the agency agreement—there was little control over funds disbursed to the agent (the Canadian charity is acting as a 'conduit' and is not controlling the funds and activities),
- the Canadian charity could not show reporting of transactions,
- the funds of the Foundation were not kept separate from the agent,
- receipting and T3010 and T4 irregularities,
- the Canadian charity did not authorize projects,
- no evidence of alleged oral arrangements that superseded the agency agreement,
- a $20,000 grant to an Air Force Museum in Beersheva, another city in Israel, which was outside of the objects of the Tel Aviv Foundation and therefore *ultra vires*.

In 2000, CRA advised the Tel-Aviv Foundation of its intention to revoke its charitable status. In 2002, the Canadian Federal Court of Appeal found in favour of CRA and against the Tel-Aviv Foundation and revoked the Foundation's charitable registration.

This case illustrates not only the importance of having the correct agreement with a foreign nonprofit or charity but also the importance of complying with the agreement. In order to follow the agreement, both the Canadian charity and the foreign agent must be aware of the agreement, understand it, and be committed to implementing it.

Furthermore, if there are going to be changes in the manner in which an operation or relationship is going to be carried out, then the changes to the agreement must be documented in writing. One of the greatest challenges that charities face in operating abroad is in direction, control, and supervision of agents abroad.

The case also reminds Canadian registered charities of the importance of operating within the charity's objects.

A final point: as illustrated in the *Tel-Aviv Foundation* case and the *Canadian Magen David Adom* case discussed below, CRA provided warnings about concerns with operations abroad. It was only after those warnings were not heeded over a protracted period of time that CRA went to the extraordinary step of deregistering a charity. As we will discuss later, CRA is less patient today with charities that are non-compliant with their obligations when operating abroad compared to 5–10 years ago. As well, when a charity gives a written undertaking that it will 'clean up its act', presumably to avoid deregistration, then that charity will be held by the Courts to a higher standard than another charity who has not been warned and has not provided such undertaking.

Canadian Magen David Adom for Israel v. MNR (2002 FCA 323)

The Canadian Magen David Adom (hereafter "CMDA") was set up to donate emergency medical supplies and ambulances to the people of Israel. CMDA appointed a Canadian representative in Israel to implement the program. In 1986, there was a CRA audit of CMDA. In that audit, CRA raised two concerns: first, CMDA was giving funds to the U.S. MDA for purchasing ambulances and that CMDA was not directly using the funds to purchase the ambulances from General Motors; and, second, there was no written agency agreement between the CMDA and a similarly named Israeli organization (Magen David Adom) and no control over how the ambulances were used once they were sent to Israel.

CMDA was arguing that the transfer of the ambulances and equipment to Israel fell within the charitable goods policy, discussed previously in this article. CRA was concerned that some of the expenditures, such as purchasing bullet proof vests, were more remote and therefore subject to being used for non-charitable purposes.

CMDA acknowledged at one point that there was probably a need for an agency agreement, but it did not enter into one with its agent in Israel, as the agent was not interested.

CRA undertook further audits for the 1993, 1995, and 1996 years, and again raised concerns about the lack of any agency agreement, persistent disbursement quota problems, and potentially non-charitable expenditures, like bulletproof vests and telecom equipment. In fact, in one instance a CMDA-purchased ambulance was transferred over to the Israel Defence Forces for their use.

CRA also later raised a public policy concern. As the ambulances were being used in Israel and the West Bank, CRA was of the view that to some extent they were being used to support the permanence of Israeli settlements in West Bank. CRA argued that such actions were contrary to Canadian foreign policy that opposed settlement activity as an impediment to creating peace in the region.

In 2001, CRA issued a notice of revocation to CMDA. The Federal Court of Appeal ultimately dismissed the CMDA appeal and CMDA lost its status as a registered charity in Canada.

The Federal Court of Appeal agreed with the charity with respect to the public policy argument. The FCA found that there is no "definite and somehow officially declared and implemented policy" with respect to Israeli organizations operating in the West Bank and Gaza Strip.

However, the Federal Court of Appeal found that:

1. the agent in Israel was "not effectively authorized, controlled and monitored by the charity"; and
2. equipment was not used only for charitable purposes and the court was concerned about the involvement by the agent with Israeli military operations.

CMDA's charitable registration was revoked in 2003. CMDA and CRA worked out an agreement whereby CMDA would need to have greater controls and CMDA would regain its charitable status! What lessons can be drawn from this case, which reads more like a saga from 1986 to 2003? What was the financial and emotional cost and distraction caused by the decision by CMDA to operate as it did? Could the CMDA not have just agreed in 1986 to buy the ambulances from GM directly and to have a proper written agreement and follow through with the agreement?

The lessons we can learn from the CMDA case are that:

1. it is important to have a written agreement that authorizes, controls, and monitors the agent;
2. transfers of equipment to a foreign military are not charitable;
3. there are limitations on the charitable goods policy; and
4. even high-profile charities such as CMDA can be targets for deregistration.

Bayit Lepletot v. MNR **(2006 FCA 128)**

This case deals with a Canadian charity that had an agency relationship with a Rabbi in Israel who "presumably" exercised some control over an Israeli charity with a similar name to the Canadian charity. The Israeli charity ran three orphanages. But, according to the Federal Court of Appeal, there was no evidence of the Rabbi's control over the charitable works of the Israeli charity, and the status of the Canadian charity was revoked.

This case demonstrates the importance of having a written agreement with the correct party. An agent can carry on charitable work, but it must be shown that the agent is actually carrying out the work. It is not sufficient for an agent to be part of another organization that does the actual charitable work. Although it is possible for an agent in certain circumstances to sub-delegate their authority,

in this case the Court found that there was no factual basis for arguing that the Rabbi had delegated his authority.

Travel Just v. Canada Revenue Agency (2006 FCA 343)

This recent Federal Court of Appeal case demonstrates the importance of properly drafted object clauses in the letters patent of a non-share capital corporation that will apply to become a registered Canadian charity.

The company "Travel Just" is a federal non-share capital corporation that applied for charitable status and was deemed to be refused by CRA as CRA did not dispose of the application within the time period that at that time was required under the *Income Tax Act* (Canada).

The objects of Travel Just are:

a. to work with key governmental authorities and grassroots communities of various tourism destination markets to create and develop model tourism development projects that contribute to the realization of international human rights and environmental norms and that achieve social and conservation aims that are in harmony with economic development aims for the particular region; and
b. to develop, fund, administer, operate, and carry on activities, programs and facilities to produce and disseminate materials on a regular basis that will provide travelers and tourists with information on socially and environmentally responsible tourism in order to establish normative discourse around traveling with a social conscience.

Legal counsel for Travel Just argued that Travel Just should be registered as a charity because the objects fall within the fourth leg of the test in *Pemsel v. Special Commissioners of Income Tax* [1891] A.C. 531 (Eng. H.L.) in that it has "other purposes beneficial to the community."

The court was sympathetic to the idea of "ethical tourism"; however, the court was concerned with two very important elements, namely: (1) the "vague and subjective" object provisions; and (2) what the court described as the "strong flavour of private benefit" that could flow from model tourist projects, such as luxury resorts in the developing world.

The objects in this case were quite broad. In some people's minds, a "model tourism development project" could be one in which the owners are running an ultra luxury resort available only to the very affluent that makes a very large profit for its owners and has occasional workshops on "international human rights and environmental norms" and will provide travelers and tourists with information on socially and environmentally responsible tourism, such as little signs in the bathroom encouraging reuse of towels and conservation of water.

While "economic development aims for the particular region" could be charitable, they could also be anything but charitable, depending on the region and what its economic development aims are.

The FCA decided in favour of CRA, and in May 2007 the Supreme Court of Canada refused leave to appeal of the case.

The case illustrates the importance of properly drafting object clauses to ensure that the objects are completely charitable. This decision also highlights the Federal Court of Appeal's concern that registered charities can be used as vehicles for private benefit more than actually conducting charitable activities outside of Canada.

Interaction Between Canadian Charities and CRA—"Education-First" Approach

CRA tries to assist charities with their compliance requirements for operating abroad by publishing materials and answering calls. A charity can always provide its proposed agreement and description of the project to CRA and request approval of the agreement and project. However, my experience is that many charities are reluctant to interact with CRA in such a fashion unless required, for example, as part of an audit. Many charities operating abroad are concerned about dealing with CRA because of its oversight responsibility. Furthermore, some charities from certain groups within society have the erroneous view that CRA will not 'support' their organization, activity, or ethnic group, and they are afraid to deal with CRA. The long waiting times for written responses to questions posed to CRA, often from six to eight months, makes it less likely that Canadian charities or professional advisors will obtain advice from CRA, which reduces the likelihood of the Canadian charity being compliant with Canadian laws and rules relating to operations abroad. As well, CRA provides advice with respect to the *Income Tax Act*. CRA is not, and should not be expected to always be, focused on or knowledgeable about many other legal and liability issues for charities.[27]

If CRA is auditing a charity, it uses what it calls an "education-first" approach. Depending on the seriousness of the issue and the response of the charity, CRA tries first to use education letters, then compliance agreements, and, only if necessary, sanctions or the revocation of a charity's registration.

We can see from the *Canadian Magen David Adom* case and the *Tel Aviv Foundation* case that in the past, typically numerous warnings have been given and only after many years of non-compliance will CRA move to deregister a charity for cause unless the charity has been very uncooperative. In the past, I have written about how infrequently CRA deregistered charities for anything other than non-filing of the T3010. In the last few years, there has been greater audit focus on Canadian charities that operate abroad and a larger number of deregistrations.

CRA is very concerned about three distinct issues: first, simple schemes in which fraudulent tax receipts are issued when no donation has been made, sometimes encouraged by some tax preparers; second, sophisticated, but ridiculous, tax evasion schemes, some of which are carried out under the umbrella of helping the poor globally, which involve a large number of taxpayers and a large amount of money (this issue has been covered by the *Toronto Star* over the last few years and one major law firm has just been sued as part of a class action lawsuit for a legal opinion it provided in connection with one of these schemes); and, third, legitimate and well-meaning charities that are not directing and monitoring their operations and are thus not able to show that their funds spent abroad are being spent on charitable activities, as opposed to private benefit, terrorism, fraud, or other non-charitable matters.

Some commentators complain about the 'increased burden' placed by CRA on Canadian charities operating abroad or the 'increasingly complicated' administrative rules. I then scratch my head and wonder what increased burden and what increased rules? CRA has not modified RC4106 since 2000 (almost eight years) and, since the publication of that document, CRA has in fact provided greater leeway to registered Canadian charities in operating abroad (for example, charities that are umbrella organizations). CRA has also provided clarifications in newsletters on various issues about which it has been asked. CRA has also made far greater efforts to educate charities about compliance issues for Canadian charities operating abroad, including through a recent educational partnership with certain charities.

The rules are not increasingly complicated or burdensome, but there is increasing enforcement of the rules. In addition to the increasing educational efforts made by CRA, there has also been a dramatic increase in the number of audits of Canadian charities operating abroad. To the extent that one can argue that it is increasingly complicated to operate abroad, it is my view it has less to do with CRA and more to do with the complexity of the world and the increasing demands of donors.

The world has become more complicated because of terrorism, money laundering, fraud, a desire to prevent corruption and bribery, sensitivity to human rights concerns, and a number of other challenges. Funders are no longer just writing out cheques and hoping that their money will save millions of lives. Increasingly they are looking not only for accountability but also for results that are measurable and programs that are effective, which is more than CRA is requiring in RC4106.

Other Concerns and Traps for Canadian Charities Conducting Foreign Activities

When dealing with Canadian charities operating abroad, the requirements of RC4106 are only part of the legal picture. Some of the other issues[28] of legal concern to charities that operate abroad include:[29]

- terrorism and money laundering;
- bribery and corruption;
- fraud;
- private benefits;
- protecting valuable intellectual property (IP) such as trademarks, copyrights, patents, and trade secrets when much of the protection is national in scope and protections put in place in Canada may not afford protection in another country;
- legal constraints on individuals and charities under laws of other countries, including but not limited to registration requirements, criminal law, restrictions on certain occupations/professionals practicing, foreign currency restrictions, restrictions on ownership of land, and restrictions on activities such as financial services (microfinances);
- donor restrictions and Canadian International Development Agency (CIDA) constraints that must be observed in addition to CRA requirements and the fact that not all activities funded by CIDA are necessarily charitable under Canadian law;
- ethical issues;[30]
- security of staff abroad;
- employment issues;
- insurance;
- foreign currency fluctuations;
- sanctions; and
- import tariffs and duties.

Risk management for Canadian charities operating abroad is imperative. Although CRA refers in Newsletter #20 to having indemnification provisions in agreements and various types of insurance, there is much more that Canadian charities can do and are doing, including setting up separately incorporated nonprofit or charitable affiliates, having detailed contingency and evacuation plans to deal with deteriorating conditions, and extensive training of employees and volunteers before they go into the field. The best way to avoid problems is to be vigilant in monitoring your activities, whether conducted by employees/volunteers or pursuant to structured arrangements.

Canadian charities need to carefully consider these and other issues before operating abroad in order to minimize problems and avoid subsequent legal liabilities.

Conclusion

The rules governing Canadian charities operating abroad, while somewhat complicated, are not too onerous, and it is important that Canadian charities understand these rules and comply with them.

Although some commentators have criticized CRA's requirements for charities operating abroad as silly or artificial, it appears that the totality of what the CRA

requires is not unreasonable in light of the importance of the funds transferred abroad being used for appropriate charitable activities and the substantial contribution of the Canadian government by way of tax credits. When monies are transferred abroad, a large part of every dollar is actually coming from the Canadian taxpayers. Many "major donors" who put in only a small percentage of a project would require far greater controls than those required by CRA.

From a corporate governance perspective, many of the CRA requirements are simply good corporate governance. Directors and officers of charities have an obligation to ensure that the funds of the charity are well spent. Charities should always receive reports on activities they are undertaking whether in Canada or abroad. When an organization is conducting a large or ongoing project, it makes sense to have progress payments. Keeping Canadian charities' funds separate simplifies the accounting and auditing process. Canadian charities that receive donations from the public or other sources need to ensure that their funds are being spent wisely or the consequence to the charity's reputation could be severe.

In my experience, charities are often more concerned with a local newspaper writing an unflattering article that will undermine the charity's fundraising or goodwill than they are with CRA audits and deregistration. As well, the charity may be concerned that a faction may publicly complain or go to court over non-compliance or illegal conduct by others in the charity. Furthermore, the chair or chief executive officer may be concerned that they will end up being replaced or fired or have their reputations ruined. As many charities have discovered, it may be easier to ask for forgiveness from CRA than to deal with disgruntled donors and the public.

As Canadian charities increasingly operate outside of Canada, it is important for them to realize that there are restrictions with respect to Canadian registered charities conducting foreign activities and the transfer of funds to foreign NGOs and charities. While failure to comply with the rules can result in deregistration and other penalties, I would hope that this article will encourage compliance with the rules which will not only protect the reputation of the charity but also that of the whole sector. Unfortunately, charities that conduct international development work have the lowest level of trust of any part of the charitable sector.[31] It is in the interest of all Canadian charities working abroad to raise the level of trust for all charities. Certainly complying with the CRA requirements is a significant step in the right direction. Avoiding many of the other common legal and ethical pitfalls discussed in this article is another.

It is perfectly reasonable for donors to be concerned with how their money is spent. When 40–60 cents of every dollar donated to a registered Canadian charity results in forgone tax revenue, CRA and taxpayers have a legitimate interest in how those funds are spent. Canadians realize that charities perform very important work in our country and beyond, but they also understand that when a person donates to a charity and then deducts the amount of such donation, the burden of paying the taxes shifts to another taxpayer. As long as the funds do-

nated to the charitable sector are well spent, Canadians are prepared to subsidize the charitable system. Without rules and an active regulator, there would be no limits on how the funds could be spent and no way of knowing if the funds are being appropriately spent. I do not think in this age of terrorism, money laundering, and expectations of greater accountability that most Canadians would be comfortable with about $2.3 billion being spent by charities outside of Canada per year without necessary controls and reporting.

NOTES

1. Mark Blumberg is a partner at the law firm of Blumberg Segal LLP in Toronto and works primarily in the areas of nonprofit and charity law, and estate planning. Mark has a B.A. in Political Science from the University of Toronto, an LL.B. degree from the University of British Columbia, and a LL.M. from Osgoode Hall Law School in Tax Law. The author would like to thank a number of people who have provided support, namely his law partners Henry Blumberg and Ronald Segal, and assisted with this article, including Lize-Mari Swanepoel and Julie Waldman and his very supportive spouse Lisa Singer. This paper is based in part on his 2006 article "Canadian Charities Operating Outside Canada and Agency Agreements" at <http://www.blumbergs.ca/articles_more.php?id=103_0_2_0> and his 2007 article "Canadian Charities and Foreign Activities" at <http://www.globalphilanthropy.ca/images/uploads/Canadian_Charities_and_Foreign_Activities_by_Mark_Blumberg_October_2007.pdf>.

2. See *Canadian Charities Spent More Abroad in 2006 Compared to Previous Years* at <http://www.globalphilanthropy.ca/index.php/articles/canadian_charities_spent_more_abroad_in_2006_compared_to_previous_year/>.

3. Terrance Carter's paper "National and International Charitable Structures: Achieving Protection and Control" in the Law Society of Upper Canada's CLE program Fit to be Tithed 2, November 26, 1998. David Amy wrote an article in The Philanthropist in 2000 entitled "Foreign Activities by Canadian Charities." Robert Hayhoe wrote "Cross-Border Operations by Canadian Registered Charities," (2004) 52 Can. Tax Journal, pages 941–967 among other articles. Robert Hayhoe also wrote "International Charitable Activities" (Chapter 12) in the loose-leaf "Charities Taxation, Policy and Practice" by Arthur Drache, Robert Hayhoe, and David Stevens. See also "Charities Operating Outside of Canada: Controls, Practices and Policies," by Carole M. Chouinard, October 2004; Terrance Carter and Jacqueline M. Demczur's 2006 article "Documenting Transfers of Funds Outside of Canada"; and "Carrying on Charitable Activities Outside of Canada Through the Use of Agents and Contractors for Service," by Jacqueline M. Demczur and Terrance S. Carter, 2008.

4. This article is available at <http://www.globalphilanthropy.ca/index.php/articles/foreign_charities_operating_in_and_from_canada/>.

5. Although pursuant to s. 149.1(1) and s. 149(1)(l) of the *Income Tax Act* you cannot qualify as a nonprofit if you meet the definition of charity in s. 149.1. However, CRA rarely deems a nonprofit to be a charity. It is relatively easy for a nonprofit to ensure that it will not be considered a charity by having any object that is not charitable (such as a political object), by having the nonprofit carry on prohibited activities such as partisan political activities, or by having the nonprofit gift assets to a non-qualified done. All three of those activities would disqualify such organization under s.149.1 from being a charity.

6. In fact, remittances account for more than three times the transfer of funds outside of Canada compared to all the Canadian registered charities operating abroad. You can see my article comparing remittances from Canada to global philanthropy from Canada at <http://www.globalphilanthropy.ca/index.php/articles/global_philanthropy_is_growing_in_canada_but_remittances_and_investment_rul/>.

7. You can read the Canada Revenue Agency publication "Registered Charities: Operating Outside Canada (RC4106)" as well as other resources at the CRA website (<http://www.cra-arc.gc.ca>).

8. In 2006 CRA released a paper entitled "Charities in the International Context" at <http://www.cra-arc.gc.ca/tax/charities/international-e.html>, which focuses mainly on the issue of violence and terrorism abroad as well as money laundering.

9. I have compiled some of the Charity Directorate's Information Letters that deal with Canadian charities operating abroad and have placed them in one PDF file at <http://www.globalphilanthropy.ca/images/uploads/CRA_Information_Letters_on_Operating_Abroad_in_PDF.pdf>.

10. <http://www.attorneygeneral.jus.gov.on.ca/english/family/pgt/nfpinc/> or <http://www.cra-arc.gc.ca/tax/charities/becoming/mod-intro-e.html>.

11. James M. Parks wrote an interesting article entitled "RCAAA's and Other Qualified Donees" for the 2008 National Charity Law Symposium which discusses in detail each of the lesser known categories of qualified donees.

12. It is not clear exactly what UN agencies would be acceptable to CRA; a donor should probably call CRA and verify whether a particular UN agency would be considered by CRA to be a qualified donee.

13. See Blumbergs article on Schedule VIII Universities at <http://www.globalphilanthropy.ca/images/uploads/Foreign_Universities_Fundraising_In_Canada.pdf>. As well, see CRA the bulletins "Donations by Canadians to Prescribed Universities Outside Canada" (RC191-07) and "Information for Educational Institutions Outside Canada" (RC190-07).

14. Only about four organizations currently are on the list and have received such a donation from the Canadian government withinin the time required. Probably the only organization that has widespread recognition is the Aga Khan Foundation.

15. The agreement should set out a clear and complete description of the activity, which will depend on the nature of the activity, the complexity and duration of the activity, and the type and quantum of resources allocated. It may include the purpose; who will benefit; in some cases, the precise location; a budget, including if there is other income generated by the activity; a schedule with beginning and end dates; a description of deliverables or targets; details on monitoring; mechanism by which the agreement can be modified or discontinued; and what other organizations will be contributing to the activity.

16. I have had the opportunity to work with foreign intermediaries who have agreements with Canadian charities to explain the requirements and rationale of those agreements. It is much easier to have compliance if the foreign party understands the meaning of a particular clause and, just as importantly, why particular clauses are in the agreement. The executive director of one large Canadian foundation once mentioned to me that she was blessed by the fact that the agents understood exactly what was needed by the CRA and why.

17. The most egregious term I recently reviewed was a Canadian charity requiring the foreign charity to agree that, upon signing the agreement, the foreign charity would be required to transfer a certain portion of all of its capital property built up over decades to the Canadian charity, even though the Canadian charity could stop providing the partial funding to the foreign charity at any point in time and still own the capital property.

18. Some commentators have used this last sentence to imply that if a start up Canadian charity is using a well-regarded foreign charity's goodwill, including name and logo, then such goodwill would be extremely valuable and the Canadian charity would be able to justify, especially during the first few years of its existence, large payments on account of royalties. This argument is problematic and can result in unwelcome attention from CRA. CRA has stated in Newsletter #20 that "In all cases, the charity must be able to establish that the Canadian charity is receiving a benefit that is proportional to the amount it pays." If the Canadian charity cannot establish that the benefit is proportional, then it risks losing its charitable status. As a Canadian charity would need to have a structured arrangement for all other payments to the foreign charity, a more cautious and simpler approach may be to have a structured arrangement covering all funds that are sent to the foreign charity above the lesser of the $5000.00 or 5% de minimis royalty amount.

19. CRA has suggested in Newsletter #20 that "we recognize that for some small charities this becomes a significant burden. We are willing to consider such situations on a case-by-case basis."

20. Newsletter #20.

21. RC4106 suggests for agency relationships: "Copies of these books and records should be forwarded regularly to the charity, and the originals should be available for inspection at the place where they are being kept by the agent." With fax, scanning, and e-mail, it is ever easier for agents to provide copies of all necessary documents.

22. RC4106 suggests for contractors: "As with agency agreements, a Canadian charity that employs contractors should obtain regular progress reports. The charity should also obtain a final complete report on the work that has been done on behalf of the charity, along with documentary evidence, such as invoices, receipts, and photographs, that the project has been completed. The reports should also show the amounts received from the charity and the expenses incurred."

23. RC4106 provides: "In the case of joint ventures, the Canadian charity should ensure it regularly receives a copy of the full and complete financial information relating to the entire venture or program, along with other documentation that will enable the charity to demonstrate that it has devoted its resources to its own charitable activity."

24. RC4106 provides: "A Canadian charity involved in co-operative partnerships should maintain adequate records relating to its particular share of the program. It should also have available sufficient documentation to establish that the program as a whole is charitable and to show how the charity's contribution fits into the overall undertaking."

25. No part of the RC4106 is more frequently misunderstood than the part relating to CIDA. It states that "CIDA has a number of requirements calling for the active involvement of an organization in the projects it funds. Thus, provided the CIDA-funded project is charitable at law, we *may* consider a charity to be carrying on its own activities with regard to that particular project. …Also, although CIDA's *current* funding criteria *may* be sufficient to secure the charity's active involvement in a project, the charity still must ensure that it is indeed exercising a sufficient degree of direction and control." Some charities and professional advisors have mistakenly taken this quote to mean that CRA

exempts CIDA projects from the RC4106 rule and this is not correct. CIDA projects are required to have the same directions and control, although in some cases CIDA requires the Canadian charity to have extensive direction, control and reporting and this may then be adequate.

26. If you wish to read the full text of the above four Federal Court of Appeal cases dealing with Canadian charities conducting foreign activities, then you can access them at <http://www.globalphilanthropy.ca> As well, you may want to review the CRA Information Letters on Canadian charities operating abroad or conducting foreign activities at <http://www.globalphilanthropy.ca>.

27. CRA is not responsible for enforcement of environmental statutes, corporate law, criminal law, labour and employment law, human rights legislation, etc.

28. For a more detailed discussion of these other legal issues see "Canadian Charities and Foreign Activities" at <http://www.globalphilanthropy.ca/images/uploads/Canadian_Charities_and_Foreign_Activities_by_Mark_Blumberg_October_2007.pdf>

29. See my article "16 Steps for Canadian charities and non-profits to avoid involvement with Terrorism" at <http://www.globalphilanthropy.ca/images/uploads/Terrorism_and_Canadian_charities_and_Non_Profit_organizations.pdf>.

30. There are many ethical issues affecting Canadian charities operating abroad, including but not limited to:

    - concerns about cooperation versus control by Canadian charities, especially when the Canadian charity is trying to empower foreign partners;
    - carrying out long-term commitments in foreign countries versus, in some situations, withdrawing over concern for the security of a charity's employees or sustainability of the projects when there is conflict or political uncertainty;
    - operating in countries that do not treat women and minorities fairly;
    - sexual coercion by aid workers or recipients of aid;
    - the proliferation of development projects by military forces that, in some circumstances, create confusion about the role and impartiality of a charitable organization;
    - the truthfulness of fundraising solicitations and advertising in Canada; and
    - cultural sensitivity versus uncritical acceptance.

    An interesting resource is the Canadian Council for International Cooperation (CCIC) Code of Ethics at ccic.org. Also, you may wish to refer to CIDA's Questions About Culture, Gender Equality and Development Cooperation at <http://www.acdi-cida.gc.ca/>

31. See my article entitled "Why Canadian Donors Have Low Levels of Trust for Canadian International Development Charities?" at <http://www.globalphilanthropy.ca/index.php/articles/why_do_canadian_donors_not_trust_canadian_international_development_chariti/>.