

Overview of CRA's Guidance on Expenditures for Fundraising Activities

This is a Charity Central podcast. Charity Central provides information and resource material to registered charities in Canada to enhance their compliance with the *Income Tax Act*. For more information about Charity Central and to access resource materials, visit our website at www.charitycentral.ca

Introduction

Hello and thanks for joining us today. My name is Lesley Conley and I am the Coordinator of Information Services for Charity Central. I'd like to welcome you to the first in our series of podcasts on the newly released fundraising guidance for registered charities.

We are here today with Peter Broder. Peter is a lawyer and policy analyst with the Muttart Foundation in Edmonton, Alberta. He has written and spoken extensively on topics related to charity and not-for-profit law and regulation, and has a particular interest in fundraising issues.

Peter is here to discuss with us today, the direction offered in the guidance on different issues, and more generally to discuss fundraising by charities.

Welcome Peter and thank you for agreeing to speak with us today on a topic that is very relevant and timely for registered charities.

Peter: Thank you for inviting me

CRA recently published its guidance on fundraising for registered charities. What would be considered fundraising under the *Income Tax Act*?

The *Income Tax Act* itself does not define fundraising. The guidance released by CRA describes fundraising as including external activities, such as soliciting donations through telemarketing, direct mail, door-to-door canvassing, as well as putting on events, or distributing information through the media or thru a charity's own publications. Under the guidance, fundraising can also include internal activities, such as prospect research or hiring fundraisers. It does not matter whether such activities are carried on under contract, by staff, or by volunteers.

How should a charity treat the costs related to their fundraising activities?

Generally costs associated with a solicitation, or incurred in preparation for a solicitation, must be reported as fundraising expenditures.

How does the guidance define solicitation?

A solicitation is a request for financial or in-kind contributions, but does not include efforts to recruit volunteers or efforts asking for support from government or another charity. It also does not include requests for fees that may be charged by the charity to defray the costs of its services.

Such as...?

Such as tuition fees or membership dues.

What further information does the guidance provide?

CRA's guidance sets out some exceptions to when an expense associated with a solicitation must be counted as a fundraising expenditure and explains how to apportion costs related to activities with multiple purposes.

What key points should a charity be aware of?

There are a couple of key rules a charity should know. If 90% of the content of an activity is devoted to a purpose other than fundraising (or, in the jargon of the *Income Tax Act*, substantially all the resources used in the activity advance an objective other than fundraising) you do not need to count the cost as a fundraising expenditure. If you meet this criteria, you don't have to do any further analysis, since it has been determined that 100% of the expenditure should be allocated to whatever the main purpose the activity is. If you don't meet the substantially all criteria. There is a second rule.

Generally, a charity's fundraising efforts must meet a four-part test before it can allocate costs proportionally between the fundraising and other objectives of the activity. This four-part test looks at the purpose of the activity, the nature of the activity, the audience for the activity and the remuneration associated with the activity. If any of these four elements display traits of fundraising, the charity may be required to allocate all costs related to the activity as fundraising expenditures.

Are there any exceptions to the key rules?

There is an exception to the four-part test allocation rule. Where fundraising is clearly integrated with a charity's core programming — CRA may allow allocation to objectives other than fundraising.

How does CRA define core programming?

Core programming is defined as efforts to prompt an action or change a behaviour other than the giving of a donation or other support, efforts that reach an audience primarily composed of people other than prospective donors and efforts that are designed more to assist beneficiaries than to get financial or in-kind contributions.

Is raising awareness included in the exception?

The exception does not apply where the programming is merely raising awareness of the charity's work in conjunction with fundraising. Rather only where the charity is providing substantive programming along with their fundraising, will it be allowed to allocate part of the activity costs to expenditures other than fundraising expenditures. The fundraising guidance provides detailed information and examples for these rules.

What do registered charities need to know about fundraising to meet CRA's requirements?

There is no set percentage of costs in relation to fundraising revenues or overall revenues that CRA automatically considers acceptable or unacceptable. The guidance does give examples of ratios of a charity's fundraising expenses to its fundraising revenues. These ratios provide a very rough tool for gauging the acceptability of a charity's fundraising. But this is only an initial step, and CRA will also look at numerous other factors in evaluating the charity's fundraising program.

Does CRA have other concerns with fundraising activity?

CRA will be especially concerned where fundraising activity is illegal or contrary to public policy, where it has become a main, prevailing or independent purpose of the charity's operations, where it results in excessive or disproportionate private gain to individuals or corporations, or where the harm resulting from the fundraising activity can be said to outweigh the public benefit of the charity's work.

What does CRA mean by illegal or contrary to public policy fundraising activities?

Briefly, fundraising that is illegal or contrary to public policy would include: fundraising that breaches federal or provincial law, fundraising that is in support of an illicit tax shelter or fundraising that breaches stated government policy, such as CRTC telemarketing regulations.

What does it mean for fundraising to be the "main purpose" of a registered charity?

The best way to understand this concept is to think of situations where fundraising activity becomes an end-in-itself, rather than a means to support a group's charitable work.

The guidance uses the term "private gain". What does this mean?

Fundraising resulting in excessive or disproportionate private gain to individuals or corporations occurs where payments to the individuals or corporations are more than what is necessary or reasonable to generate the fundraising revenue that will be used to support the charitable work.

We hear the terms harm and public benefit used in conjunction with the fundraising guidance. Can you give us an example of when harm would be considered to outweigh public benefit?

Sometimes fundraising that results in harm outweighing the public benefit supported by the fundraising, this would include, for example, systematically misleading donors or prospective donors about how their donation will be used or how much of their donation will be paid to the fundraiser.

So what's the bottom line here?

Well, CRA wants to be satisfied that a charity is appropriately devoting resources to its charitable work. It wants to be satisfied that any fundraising expenses that have been incurred are reasonable in light of the charity's overall circumstances, and that the charity has acted prudently in procuring and managing fundraising activities. Charities that can show that they have paid fair market value when they entered into fundraising contracts, acquired fundraising services or hired fundraising staff are generally considered to have incurred reasonable costs and acted prudently.

What can a charity do to minimize the risk of facing sanctions by CRA?

While there is no guarantee that CRA will not take issue with your fundraising activity, charities that exercise good risk management in how they fundraise and take steps to lower their fundraising costs when their expenditures on fundraising are large, relative to the amounts raised through the effort, or to the charity's overall budget, are less likely to face sanctions or other enforcement measures.

A charity can argue that it's practicing good risk management by, among other things, being aware of, and following any provincial and municipal laws, complying with its fundraising activity; as well it may wish to show that it knows about and adheres to industry standards, such as Imagine Canada Ethical Fundraising Code.

In Alberta, there is a *Charitable Fundraising Act*. Does this mean that in Alberta there are two sets of rules to follow?

Yes, that is correct. Under the Canadian constitution, authority for the regulation of the day to day operations of registered charities falls to the provinces. However the *Income Tax Act* also imposes some requirements on registered charities that fundraise.

What happens in other provinces?

Other provinces may have their own provincial legislation. You should check your provincial legislation as to its fundraising requirements. In Manitoba and P.E.I. for instance, there are registration requirements for charities doing fundraising. In Saskatchewan, for-profit fundraising companies are subject to regulation. And, in Ontario, the Office of the Public Guardian and Trustee has certain powers to act against fundraising abuses that put charitable assets at risk.

Is there any difference between hiring in-house staff for fundraising and contracting with an external fundraising company?

Fundraising costs can become an issue whether they are incurred internally or paid to a third party. CRA can challenge excessive or unreasonable costs in either situation, but they may use different bases for questioning the expenditure, or to act against the charity, depending on the nature of the fundraising program. Regardless of how you do your fundraising, CRA expects you to exercise appropriate risk management over fundraising activities and be prudent about use of the charity's resources.

Contracting out your fundraising does not relieve you of the obligation to exercise proper control over it, and in particular to ensure that it is carried out in a way consistent with the requirements of being a registered charity. You should note however, that there are specific rules under the *Income Tax Act* that apply to parties that receive unreasonable compensation or other payments and are not arms length from the charity.

Can you explain the special rules around “non-arms length transactions”?

Whether a party is arms length or not is a question of fact, and is based on consideration of any contractual or familial ties that may exist between the charity and the party it is dealing with. There are specific rules under the *Income Tax Act* which apply to parties which receive unreasonable compensation or other payments and are not at arms length from the charity. The *Income Tax Act* provides for a monetary penalty for abusive non-arms length transactions that can apply either to an internal payment or to a payment to a fundraising company controlled by someone associated with the charity.

How does the fundraising guidance relate to the disbursement quota?

The *Income Tax Act* includes a requirement known as the disbursement quota that requires a charity to spend a certain percentage of their resources on their charitable work. This is a separate requirement from the fundraising guidance.

Satisfying your disbursement quota obligations does not necessarily mean that you are complying with the fundraising guidance and adhering to the fundraising guidance does not necessarily mean you will meet your disbursement quota obligations.

Charities should be aware of the need for complying with both of these obligations.

Thank you very much for being with us today Peter, and taking the time and talking with us today about this very important topic. We appreciate it.

Peter: Thank you for having me.

Peter Broder is Policy Analyst and General Counsel at The Muttart Foundation in Edmonton, Alberta. The views expressed do not necessarily reflect those of the Foundation.