



CRA: Major Non-Compliance Issues

Charity and Not-for-Profit Law
OBA February 2011



Canada Revenue
Agency

Agence du revenu
du Canada

Canada

Outline

1. Audit Plan
2. Audit Results
3. Common compliance issues
4. Serious non-compliance issues impacting the sector, the donor public and the tax system
 - Tax Shelters
 - False Receipts

Audit Plan

- Each year the Compliance Division develops an “audit plan”.
- The Audit Plan for 2010/2011 :
 - 53% - High Risk files (446 files)
 - 18% - Core Audit Program – Random (150 files)
 - 10% - Compliance Agreements Review (80 files)
 - 9% - Restricted Books/Records Review (80 files)
 - 5% - Exploratory Audits (40 files)
 - 5% - Projects (50 files)

AUDIT RESULTS – 2009/10

- Compliant 13%
- Education 52%
- Compliance Agreements 22%
- Revocations for cause 41 6%
- All Others 7%
- Note – The “All Others” category includes: Voluntary revocations, Annulments, Pre registration audits, Part V

Enforcing compliance

- Sanctions:
 - Monetary Penalties &/or Suspension of receiving privileges and qualified donee status
- Revocations
 - A revoked charity can no longer issue official donation receipts to acknowledge gifts made by donors
 - A revoked charity is subject to a revocation tax equivalent to 100% of its net assets
 - A revoked charity may become a taxable entity
- Where it is in the public's interest, compliance actions taken against a charity will be publicized (e.g., through a press release)

Discovering non-compliance

- Generally, cases of non-compliance are discovered through the course of an audit.
- They can also be discovered through external and internal referrals/leads
- The following list of issues are encountered all too frequently through the audit process.

Top 5 Audit Findings

- 1. Incorrect issuance of donation receipts
- 2. Books and Records are inadequate or deficient
- 3. Gifts to non-qualified donees
- 4. Failure to maintain direction and control
- 5. Failure to file T3010

Incorrect Issuance of Receipts

- Registered charities are often unaware of requirements for contents of receipts.
- Registered charities often make mistakes as to what type of property can be receipted
 - Receipts are often incorrectly issued for “gifts” of services.
- Establishing fair market value (FMV) also tends to be a hurdle for charities

Books & Records Deficiency

- Books & Records must be maintained in Canada
- The CRA must be able to verify:
 - Revenues, including all charitable donations received
 - That resources are spent on charitable programs;
 - and
 - That the charity's purposes and activities continue to be charitable
- Duplicates of all issued, cancelled and replaced receipts must be maintained

Gifts to Non-Qualified Donees

- Registered charities tend to be unaware of the restrictions surrounding “Qualified Donees”.
- Registered charities may use their resources in one of two ways:
 - In support of their own charitable programs;
 - Or
 - By gifts to Qualified Donees

Gifts to Non-Qualified Donees (cont'd)

- Gifting to organizations that are not qualified donees is a serious issue:
 - There are monetary penalties which apply (105% of amount gifted)
 - Also a common ground for revocation
- Confirming an organization's status as a registered charity is easily accessible through the CRA's website or by calling the Charities Directorate

Failure to Maintain Direction and Control

- Often registered charities operating in foreign jurisdictions carry out activities through an agent or other intermediary.
- Where a registered charity conducts activities through an intermediary, it must maintain **direction** and **control** over the use of its resources.
- A properly structured agreement (containing all the necessary elements) helps demonstrate direction and control
- Frequently, charities fail to properly implement and monitor the arrangement.

Failure to File T3010

- Continues to be the biggest compliance issue (largest number of revocations)
- Hundreds of charities file late each year or fail to file and are revoked as a consequence
- Financial statements must also be provided as a part of a charity's filing requirements for the annual information return

Fundraising

- While the CRA accepts that charities can have fundraising costs, our expectation is that these expenses be reasonable and proportionate to the charitable activity being conducted
- A charity which spends excessive amounts on fundraising to the detriment of its charitable programs is not considered to be devoting all of its resources to charitable activities.
- See Guidance CPS-028,
■ *Fundraising by Registered Charities*

Focus Shift

- Since 2007, the Charities Directorate has been focusing its audit and compliance resources on two major issues:
 - ❖ Addressing the participation by registered charities in facilitating tax shelter arrangements
 - and
 - ❖ Combating the issuance of fraudulent donation receipts .



TAX SHELTERS

Definition

- Under the Income Tax Act, a tax shelter includes any gifting arrangement:
 1. for which a promoter represents that an investor can claim deductions or credits which equal or exceed the cost of the property or
 2. for which a person will incur a limited recourse amount (debt).
- These arrangements are generally promoted promising participants tax receipts reflecting a value many times greater than what participants are out-of-pocket
- Tax Shelters have to obtain identification numbers in order for CRA to track these arrangements and identify their participants

TAX SHELTERS

- There are generally 3 types of tax shelter schemes involving charities:
 - Buy low, donate high, where an individual buys property for \$3,000, then donates the property at a “fair market value” of \$10,000, and receives a \$10,000 receipt
 - Gifting trust arrangements, where an individual donates \$3,000 cash to a charity, receives property with a purported fair market value of \$7,000 from a trust which is also donated to charity, and receives a donation receipt of \$10,000
 - Leveraged cash donations, where an individual borrows \$8,000 (from an organization involved in the scheme) to donate to a charity and donates \$2,000 out of pocket to the charity for a \$10,000 donation receipt

SCOPE OF THE PROBLEM

- Since 2003, despite the introduction of legislation to combat such arrangements, tax shelter schemes have continued to draw in investors. It is estimated that there are approximately:
 - 161,500 donors;
 - \$5.15 billion in donations;
 - 75 registered charities/RCAAA; and
 - 30 donation arrangements

SCOPE OF THE PROBLEM

■ Participation by Charities and RCAAAs:

- Charities and RCAAAs are happy to receive the 1%
 - tax receipts cost them very little
 - Don't give consideration to the effects of their activity on the tax base
- Believe the often incredible claims of the promoters as to what is done with the donated money and property
 - No accountability for the funds/property
- Believe it is a “loophole” or a matter of interpretation
 - Many schemes cross the line into gross misrepresentation or outright fraud.

CRA APPROACH

Promoters & Donors

- Aggressive Tax Planning Division is currently proceeding with the re-assessment of tens of thousands of participants for hundreds of Millions of dollars
- Third-party penalties will be considered against promoters of these arrangements and other third-parties
- Possibility of Criminal charges

CRA APPROACH

Registered Charities

- Charities Directorate auditing all charities and RCAAAs participating in tax shelter arrangements
 - Includes organizations seeking registration or re-registration whereby applicants appear to be seeking registration to participate in arrangements
- Revocation and/or financial penalties will be considered in all cases
 - 25 audits on-going
 - 63 audits completed with 39 charities/RCAAAs revoked & 6 applicants denied registration
- Publicizing compliance actions (e.g., through a press release)

CRA APPROACH Registered Charities

- Egregious Cases
- Revocation published within 30 days of Notice of Intent to Revoke issued
 - Charities required to obtain a Stay Application from Federal Court of Appeal to prevent CRA from publicizing revocation
- Taxpayer Alerts and Fact Sheets are posted on CRA's Web site
- Public information sessions

Promising Results

- 2008 statistics have shown a 58% reduction in number of donors involved in tax shelters as well as a reduction of 51% in the amounts donated through these arrangements

FALSE RECEIPTING



SCOPE OF THE PROBLEM

- The schemes generally involve a charitable tax receipt being sold for 10% of the receipts face value.
- In most cases the CRA finds that the charity is complicit in these arrangements, however, this fraud may or may not be carried on with the knowledge of the particular registered charity e.g., receipts being created sold entirely by a tax preparer.

SCOPE OF THE PROBLEM

- False Receipting:
- Over 135,000 donors have been involved since 2004
- Hundreds of Millions in donations.

Statistics

- Since 2004, the Charities Directorate has screened over 170 files for audit.
- 150 audits completed – 76 revoked
- Numerous cases referred to CRA Enforcement for the potential laying of Criminal charges.
 - Some prosecutions already completed.
- Charities Directorate is currently working with other areas of the CRA to potentially identify additional cases.

CanAfrica International Foundation

- Audit conducted for FPE 2002-2005
- Charity reported \$2,203,364 as receipts on 2004 T3010
- CRA seized records showing Charity issued \$21,555,427 in receipts to 3,700 donors in 2004
- Estimated \$38,127,696 in false receipts issued – (low)
- One of directors - Ambrose Danso-Dapaah issued receipts
- File referred to Enforcement
- Charity revoked September 8, 2007

Toronto tax preparer jailed for providing false charitable donation receipts to clients

- Toronto, Ontario, December 18, 2008 . . . Ambrose Danso Dapaah, formerly of Mississauga, pleaded guilty on December 15, 2008 to one count of fraud over \$5,000. He was sentenced to 51 months in jail in the Ontario Court of Justice in Toronto.
- “Canadians have to be confident that the administration of the tax system is fair,” said William V. Baker, Commissioner of the Canada Revenue Agency. “That’s why the Agency works to ensure that the vast majority of Canadians who pay their taxes are not penalized by those who don’t.”
- A Canada Revenue Agency (CRA) investigation revealed that Dapaah, owner and operator of ADD Accounting Services, as well as president of CanAfrica International Foundation (CIF), prepared and filed false personal income tax returns on behalf of his clients. His clients claimed fictitious or overstated charitable donation receipts from CIF and other charities on their income tax returns. During the 2002 to 2005 tax years, Dapaah falsified over \$21M in charitable donations, and in doing so, helped his clients claim over \$6M in non-refundable tax credits.
- On September 8, 2007, CRA revoked the charitable registration of CIF for its role in selling official donation receipts.

Appeals process

- Regular
 - 90 days to file a Notice of Objection
 - 30 days to file an Appeal to the Federal Court of Appeal
 - 30 days to file an Appeal to the Supreme Court of Canada
 - File is not revoked until all Appeals rights have been exhausted. Organization continues to issue receipts.

Appeals process (cont'd)

- Egregious cases (as of early 2008)
 - Although the organizations' rights of Objection and Appeals is intact, we revoke the organization within 30 days of our ITR letter unless the organization successfully obtains a stay of proceedings, from the Federal Court, within that time period.
 - The organizations lose their receipting privileges as soon as the revocation notice is published in the Canada Gazette

THANK YOU