



CANADA REVENUE
AGENCY

AGENCE DU REVENU
DU CANADA

REGISTERED MAIL

Living Waters Ministry Trust
123 Concord Crescent
London ON N6G 3H5

BN: 860719145 RR0001

Attention: Mr. Bernard McMillan

File #:3026946

June 8, 2009

**Subject: Revocation of Registration
 Living Waters Ministry Trust**

Dear Mr. McMillan:

The purpose of this letter is to inform you that a notice revoking the registration of Living Waters Ministry Trust (the Organization) was published in the *Canada Gazette* on June 6, 2009. Effective on that date, the Organization ceased to be a registered charity.

Consequences of Revocation:

- a) The Organization is no longer exempt from Part I Tax as a registered charity and is **no longer permitted to issue official donation receipts**. This means that gifts made to the Organization are no longer allowable as tax credits to individual donors or as allowable deductions to corporate donors under subsection 118.1(3), or paragraph 110.1(1)(a), of the *Income Tax Act* (the Act), respectively.
- b) By virtue of section 188 of the Act, the Organization will be required to pay a tax within one year from the date of the Notice of Intention to Revoke. This revocation tax is calculated on prescribed form T-2046 "*Tax Return Where Registration of a Charity is Revoked*" (the Return). The Return must be filed, and the tax paid, on or before the day that is one year from the date of the Notice of Intention to Revoke. A copy of the Return is enclosed. The related Guide RC-4424, "*Completing the Tax Return Where Registration of a Charity is Revoked*", is available on our website at www.cra-arc.gc.ca/E/pub/tg/rc4424.

Section 188(2) of the Act stipulates that a person (other than a qualified donee) who receives an amount from the Organization is jointly and severally liable with the Organization for the tax payable under section 188 of the Act by the Organization.

- c) The Organization no longer qualifies as a charity for purposes of subsection 123(1) of the *Excise Tax Act* (ETA). As a result, the Organization may be subject to obligations and entitlements under the ETA that apply to organizations other than charities. If you have any questions about your GST/HST obligations and entitlements, please call GST/HST Rulings at 1-888-830-7747 (Quebec) or 1-800-959-8287 (rest of Canada).

In accordance with *Income Tax Regulation* 5800, the Organization is required to retain its books and records, including duplicate official donation receipts, for a minimum of two years after the Organization's effective date of revocation.

Finally, we wish to advise that subsection 150(1) of the Act requires that every corporation (other than a corporation that was a registered charity throughout the year) file a *Return of Income* with the Minister of National Revenue (the Minister) in prescribed form, containing prescribed information, for each taxation year. The *Return of Income* must be filed without notice or demand.

If you have any questions or require further information or clarification, please do not hesitate to contact the undersigned at the numbers indicated below.

Yours sincerely,



Danie Huppé-Cranford
Director
Compliance Division
Charities Directorate
Telephone: 613-957-8682
Toll free: 1-800-267-2384

Enclosures

- Copy of the Return (form T-2046)
- Canada Gazette publication

Cc: Mr. Robert McMechan, LLB., LLM
28 Glengarry Road
Ottawa ON K1S 0L5



REGISTERED MAIL

Living Waters Ministry Trust
123 Concord Crescent
London ON N6G 3H5

APR 24 2009

BN: 860719 145 RR 0001
File No: 3026946

Attention: Mr. Bernard McMillan

**Subject: Notice of Intention to Revoke
Living Waters Ministry Trust**

Dear Mr. McMillan:

I am writing further to our letter dated July 28, 2008 (copy enclosed), in which you were invited to submit representations as to why the Minister of National Revenue (the Minister) should not revoke the registration of Living Waters Ministry Trust (the Charity) in accordance with subsection 168(1) of the *Income Tax Act* (the Act).

We have reviewed and considered the written response dated September 29, 2008 (copy enclosed without attachments) from your authorized representative Mr. Robert McMechan. However, notwithstanding your reply, our concerns with respect to the Charity's non-compliance with the requirements of the Act for registration as a charity have not been alleviated. Our position is fully described in Appendix "A" attached.

Conclusion:

Our audit has concluded that from August 11, 2004 to December 31, 2006, Living Waters Ministry Trust issued in excess of \$41.6 million in receipts for cash received through a tax shelter arrangement. The Charity, in turn, directed \$40.7 million of the cash to another registered charity also participating in this arrangement. Our audit revealed that the vast majority of the cash sent to the other participating charity was subsequently paid to the promoters of the tax shelter arrangement. Of the remainder, the Charity itself paid \$ 443,000 in fundraising fees to the tax shelter promoters and retained \$416,000 for use in their own activities.

It is our position that the Charity has operated for the non-charitable purpose of promoting a tax shelter arrangement and for the private benefit of the tax shelter promoters. The Charity has issued receipts for transactions that do not qualify as gifts, issued receipts otherwise than in accordance with the *Income Tax Act* and its Regulations, has failed to maintain sufficient books and records to support its activities and has used its income for the

personal benefit of its trustees. For all of these reasons, and for each of these reasons alone, it is the position of the CRA that the Charity's registration should be revoked.

Consequently, for each of the reasons mentioned in our letter dated July 28, 2008, I wish to advise you that, pursuant to the authority granted to the Minister in subsections 149.1(4) and 168(1) of the Act, which has been delegated to me, I propose to revoke the registration of the Charity. By virtue of subsection 168(2) of the Act, revocation will be effective on the date of publication of the following notice in the *Canada Gazette*:

Notice is hereby given, pursuant to paragraphs 168(1)(b) and 168(1)(d) of the Income Tax Act, that I propose to revoke the registration of the organization listed below under subsection 149.1(4), and paragraph 149.1(4)(b), of the Income Tax Act and that the revocation of registration is effective on the date of publication of this notice.

Business Number	Name
860719 145RR 0001	Living Waters Ministry Trust London ON

Should you wish to object to this Notice of Intention to Revoke the Charity's registration in accordance with subsection 168(4) of the Act, a written Notice of Objection, which includes the reasons for objection and all relevant facts, must be filed within **90 days** from the day this letter was mailed. The Notice of Objection should be sent to:

Tax and Charities Appeals Directorate
Appeals Branch
Canada Revenue Agency
250 Albert Street
Ottawa ON K1A 0L5

A copy of the revocation notice, described above, will be published in the *Canada Gazette* after the expiration of 30 days from the date this letter was mailed. The Charity's registration will be revoked on the date of publication, unless the Canada Revenue Agency receives an order, **within the next 30 days**, from the Federal Court of Appeal issued under paragraph 168(2)(b) of the Act extending that period.

Please note that the Charity must obtain a stay to suspend the revocation process, notwithstanding the fact that it may have filed a Notice of Objection.

Consequences of Revocation:

As of the effective date of revocation:

- a) the Charity will no longer be exempt from Part I Tax as a registered charity and **will no longer be permitted to issue official donation receipts**. This means that gifts made to the Charity would not be allowable as tax credits to individual donors or as

allowable deductions to corporate donors under subsection 118.1(3), or paragraph 110.1(1)(a), of the Act, respectively;

- b) by virtue of section 188 of the Act, the Charity will be required to pay a tax within one year from the date of the Notice of Intention to Revoke. This revocation tax is calculated on prescribed form T-2046 "*Tax Return Where Registration of a Charity is Revoked*" (the Return). The Return must be filed, and the tax paid, on or before the day that is one year from the date of the Notice of Intention to Revoke. A copy of the relevant provisions of the Act concerning revocation of registration, the tax applicable to revoked charities, and appeals against revocation, can be found in Appendix "B", attached. Form T-2046, and the related Guide RC-4424, "*Completing the Tax Return Where Registration of a Charity is Revoked*", are available on our website at www.cra-arc.gc.ca/charities;
- c) the Charity will no longer qualify as a charity for purposes of subsection 123(1) of the *Excise Tax Act* (ETA). As a result, the Charity may be subject to obligations and entitlements under the ETA that apply to organizations other than charities. If you have any questions about your GST/HST obligations and entitlements, please call GST/HST Rulings at 1-888-830-7747 (Quebec) or 1-800-959-8287 (rest of Canada).

Finally, I wish to advise that subsection 150(1) of the Act requires that every corporation (other than a corporation that was a registered charity throughout the year) file a *Return of Income* with the Minister in prescribed form, containing prescribed information, for each taxation year. The *Return of Income* must be filed without notice or demand thereof.

Yours sincerely,



Terry de March
Director General
Charities Directorate

Attachments:

- CRA letter dated July 28, 2008;
- Your letter dated September 29, 2008 (without attachments);
- Appendix "A", Comments on Representations; and
- Appendix "B", Relevant provisions of the Act

cc: Mr. Robert McMechan, LL.B., LL.M
28 Glengarry Road
Ottawa ON K1S 0L5

LIVING WATERS MINISTRY TRUST

COMMENTS ON REPRESENTATIONS OF SEPTEMBER 29, 2008

Failure to Devote Resources to Charitable Activities:

Based on the Canada Revenue Agency's (CRA) audit of Living Waters Ministry Trust (the Charity), the Charity primarily operates for the purpose of furthering the Canadian Humanitarian Trust (CHT) tax shelter by agreeing, for a fee, to act as a receipting agent in the tax shelter. *Per* our previous letter, it is CRA's position that the Charity is operating as a conduit for the tax shelter. In operating as such, the Charity has entered into agreements with persons associated with the tax shelter program to facilitate the Charity's acceptance, and subsequent receipting, of all cash contributions made by participating donors. The Charity also agreed to "immediately upon receipt" transfer approximately 98% of all cash contributions received from participating donors to another participating charity. For its role in the entire tax shelter, the Charity retains 1% of total tax-receipted cash contributions receipted and pays a 1% + GST fundraising fee.

The submissions of September 29, 2008 argue that "[t]here is no prohibition in the *Income Tax Act* (Canada) (the Act) against a charity participating in, that is receiving donations in the course of, a charitable donation program that is registered as a "tax shelter"... The participation by the [Charity] in the CHT Program, a registered "tax shelter", by receiving donations of cash from participants in the CHT Program, was part of the [Charity's] charitable activities." You are correct that there is no explicit prohibition in the Act against a charity participating in a tax shelter. However, at law, where an activity becomes so predominant it becomes an end in and of itself, it may cause an organization to cease to qualify as an organization operating for exclusively charitable purposes. As described in our letter of July 28, 2008, it is our position that the overwhelming majority of funds received by the Charity are devoted to its participation in this tax shelter and the manner in which the Charity has structured itself to accommodate the tax shelter, has become an end in itself. Operating for the purpose of promoting a tax shelter donation arrangement is not a charitable purpose at law and, for this reason alone, we are of the position that the Charity does not operate for exclusively charitable purposes as required by subsection 149.1(1) of the Act.

In support of this we note, that based on the Charity's annual information returns, the CHT tax shelter is the Charity's primary activity. The Charity issued official donation receipts for \$41.6¹ million that flowed through its account from participants in the CHT tax shelter and had at least \$416,000² contributed to its own programs in 2004, 2005 and 2006. During this same period, the Charity's only other source of income, \$15,600,

¹ Included is \$182,000 in interest income earned on the trust account deposits erroneously reported by the Charity as tax-receipted gifts at line 4500 of the Registered Charity Information Returns filed for 2004, 2005 and 2006.

² 1% of CHT tax-receipted gifts and interest income earned on trust account deposits in 2004, 2005 and 2006

was received from offerings, investment income and rental income. It remains our position that, rather than fundraising to pursue its own charitable activities, the Charity's involvement and promotion of the CHT tax shelter has become its primary purpose.

The representations find that statements made in our previous letter "manifestly distort the nature of the [Charity's] participation in the CHT Program, a registered tax shelter, and are wrong in fact and law." The Directors involvement in and promotion of the CHT Program as well as the Charity's relative inactivity until late 2006³, provide the facts supporting our statements that:

- "the Charity structures and conducts its activities to accommodate this tax shelter;
- a collateral purpose, if not primary purpose of the Charity is, in fact, to support and promote the tax shelter arrangement;
- enthusiastically lends its resources (not to mention tax receipting privileges) to support this tax shelter arrangement, with little regard for the mandate and best interests of the Charity itself; and
- [o]perating for the purpose of promoting tax shelters is not a charitable purpose at law."

Upon receiving its notification of registration, the first actions of the board of directors were to finalize its contracts for participation in the CHT tax shelter and to set-up meetings with community groups to have the CHT tax shelter presented. Findings such as these, in our opinion, do not distort the nature of the Charity's activities as they were occurring during the audit nor distort the fact that the Charity continues to participate in the CHT tax shelter.

The submissions further state, "[t]here is no prohibition in the Act against the [Charity] entering into such a services agreement with WHI (World Health Initiatives), nor against the [Charity] paying WHI the services fee, and the [Charity] paid the services fees in the course of its charitable activities. The disbursement by the [Charity] to CPAR (Canadian Physicians for Aid and Relief) of the proceeds of cash donations received by it was...properly part of the [Charity's] charitable activities." We do not disagree that the Act permits a charity to engage in fundraising contracts and to transfer funds to qualified donees. However, it is our conclusion that the Charity's primary purpose for making these transfers to CPAR was merely an orchestrated step in the overall CHT tax shelter arrangement and the cash contributions were not intended to be used for charitable purposes of the Charity or by CPAR. We also disagree that the transfers to CPAR were part of the Charity's own charitable activities. The transfer of cash by one participating charity to another CHT participating charity, such as CPAR, was established prior to the Charity's registration and involvement in the tax shelter, thereby making it difficult for the CRA to concur the Charity's actions were of their own design and in furtherance of their own charitable activities. The Charity's purposes "to preach and advance the teaching of Living Waters Ministry's faith and to establish, support and maintain a house of worship

³ Charity commenced religious services in December 2006 as the church building was acquired in March 2006.

with services conducted in accordance to the tenets and doctrines of the Living Waters Ministry's faith" fail to convince CRA that transfers of funds to CPAR, and participation in the CHT tax shelter, was part of its own charitable activities and done in furtherance of its own charitable purposes.

The Charity made distributions of funds to a predetermined registered Canadian charity pursuant to its participation in the CHT tax shelter. This is clear from the selection of CPAR, which is named in the tax shelter's promotional materials, as well as the pattern of transactions of donor "gifts" and subsequent transfers to this other registered and participating charity. In fact, it appears the Charity only made gifts to CPAR as directed to do so by the tax shelter promoter and in amounts predetermined by the tax shelter promoter. The Charity states it agreed to participate in the CHT Program "in support of the [CHT] Program's extraordinary charitable aims and accomplishments" which the Charity believes is advancing its Articles of Faith. The Charity may have been motivated to participate in a humanitarian endeavour, such as the one proposed by CHT; however it is our position an overwhelming majority of actual funds contributed by participating donors were subsequently paid to the promoters of the tax shelter arrangement, with the Charity and CPAR each retaining a 1% "fee" for its participation. Of the funds received by CPAR, the funds are used to discharge the lien attached to the pharmaceuticals received by CPAR and to pay fundraising and administrative fees to WHI. We have not been provided with evidence confirming the funds paid by the Charity and CPAR to WHI "were an essential part of the charities' activities, carried on in support of a program which distributed pharmaceuticals in the course of a massive international humanitarian aid program" in at least 42 countries as boldly emphasized by the Charity. The Charity has submitted, as evidence confirming the pharmaceuticals alleged distributions, copies of acknowledgement letters contained within the CHT promotional materials rather than copies of reports it was to receive from CPAR supporting the use of their funds and distribution of goods "for the purposes of humanitarian aid overseas".

Per our previous letter, the Charity received cash from participant donors as per its role in the tax shelter and simply received and transferred the cash, as per the arrangements entered into, to another participating registered charity, CPAR. It is further our position, as stated in our earlier letter, that CPAR paid substantially all of the "gifts" received from the Charity to the promoter of the tax shelter. The Charity states that "no cash "revert[ed] back" to WHI from either the [Charity] or from CPAR, as WHI was not the source of the funds the CHT participants donated to the [Charity]." The CRA does not dispute the Charity's statement that WHI was not the source of the participants' funds. It is the CRA's position that the funds made available by participating donors to the Charity were merely disguised as "donations" - flowing through the participating charities to WHI under the guise of fundraising, administration and lien payments. Again, we emphasize that in this arrangement substantially all, in fact 97.5% of the cash, donated to the participating charities, is eventually paid out in fees and other charges, or made available, to WHI. Aside from 1% of gross donations, the cash does not remain in the hands of the participating charities.

Also noted in our previous letter, the cash contributions “donated” to the Charity are not monies the Charity can use freely in its own charitable activities. At all times the monies are segregated in a trust account maintained solely for the purpose of facilitating the CHT tax shelter by Mr. Sommer and only the Charity's 1% earnings are distributed from the trust account to the Charity. The cash contributions received through the CHT tax shelter are tax-receipted on behalf of the Charity by WHI but are earmarked to be transferred to the CPAR and WHI, with “payments to CPAR and WHI made on the same day as initial deposit”. As noted in that letter and in your submission, the Charity consistently distributed 98% of the cash contributions received to CPAR and 1% plus GST to WHI.

In this regard, it is difficult to see how the Charity's participation can be characterized in any other way but as being paid to act as the receipt issuing entity in a tax shelter arrangement. The overwhelming financial activity of the Charity; lack of due diligence; and lack of continued control and monitoring of the activities undertaken by the Charity's third party agents (including WHI, Mr. Sommer and CPAR) demonstrate the Charity's willingness to lend its name and tax receipting privileges to the CHT tax shelter in exchange for monetary compensation. It is the CRA's position that the Charity has participated in a tax shelter designed to abuse the charitable gift incentive provisions of the Act and that the Charity's participation in this tax shelter has become an end in and of itself. Accordingly, it is our position that the Charity has operated for the non-charitable purpose of promoting and participating in tax shelter arrangement and, therefore cannot be considered to be a charitable foundation *operated exclusively for charitable purposes*.

Therefore under paragraph 168(1)(b) of the Act, the Minister may, by registered mail, give notice to the organization that the Minister proposes to revoke its registration because it ceases to comply with the requirements of the Act related to its registration as such. For this reason, there are grounds for revocation of the charitable status of Living Waters Ministry Trust.

Personal Benefit

The representations of September 29, 2008 maintain that Mr. McMillan loaned the Charity \$20,000 from his own personal resources to facilitate the purchase of the church building and advanced an additional \$24,000 to pay for renovations undertaken. The representations also confirm the Charity failed to maintain detailed records supporting the expenditures incurred on the Charity's behalf. The representations state “Regarding the lack of formal record-keeping concerning how the \$24,000 was spent on behalf of the [Charity], Pastor McMillan spent decades in the construction industry and dealt with payments on behalf of the [Charity] in the way to which he was accustomed. The part-time help he employed were individuals from the Men's Mission and others in need. It did not seem appropriate to him to issue any paperwork to these individuals.”

The Charity, in its representations, has provided sufficient documentation to substantiate that Mr. McMillan did advance \$20,000 from his personal bank account to Prime Capital

Realty Ltd. for the purchase of the church building. The representations also clarify previous statements made by Mr. McMillan as to who paid the \$20,000 down payment on the church building.⁴

Notwithstanding the above, CRA remains of the position that the Charity has failed to maintain adequate records and has failed to provide adequate records during the course of the audit to support Mr. McMillan's loaning of funds to the Charity; the Charity has failed to substantiate that Mr. McMillan loaned funds to the Charity, or made payments on the Charity's behalf, totaling \$24,000 for renovations. The representations do not provide evidence substantiating that the amounts estimated by Mr. McMillan in Appendix G of the representations are reasonable or that, where specific record of cost plus Mr. McMillan's labour are absent, third party documentation was sought to substantiate a portion of the amounts. The fact that Mr. McMillan did not consider it appropriate to issue paperwork to the individuals employed to undertake the renovation work and dealt with payments in a way to which he was accustomed does not preclude the Charity from complying with the Act. The Charity remains responsible for the maintenance of adequate records and issuing appropriate Statements of Remuneration Paid whether the payments are made to Mr. McMillan or to others. We find the representations misleading given that the Charity considered it appropriate to maintain, and provide copies of expense reimbursements from directors for items as minor as parking and kilometer reimbursement.⁵

The Charity has also failed to follow its own Constitution, of which Article 111(6) states "The executive or directing officers, leadership team member(s) or leader(s) shall not be paid a salary but are entitled to expenses provided they have been pre approved by the majority of the executive or directing officers". The Charity's records have not confirmed the \$50,000 was pre-approved and in this regard, it appears Mr. McMillan took advantage of his position in the organization to incur expenses he later demanded repayment for. This is further evidenced by the fact that the \$50,000 loan agreement between the Charity and Mr. McMillan was dated March 6, 2006 which was after the \$20,000 was loaned for the down payment but before the remaining \$24,000 was actually expended or required to be expended.

It is our position the Charity has transferred charitable assets for the private gain of a director and therefore has failed to demonstrate that it meets the test for continued registration under 149.1(1) as a charitable organization that "no part of the income of which is payable to, or is otherwise available for, the personal benefit of any proprietor, member, shareholder, trustee or settlor thereof". For this reason, it appears to us that there are grounds for revocation of the charitable status of Living Waters Ministry Trust under paragraph 168(1)(b) of the Act.

⁴ Per our July 28, 2008 letter, "Mr. McMillan also alleges to have given \$20,000 to a parish member for the sole purpose of having the parish member pay a \$20,000 down payment on the church." Per your September 29, 2008 letter at Appendix G, item (B), "The offer [to purchase the church building] was presented in a parish members name and gave a cheque with it for the \$20,000.00 and I was to provide the \$20,000.00 for the offer but instead I got a money order which was paid direct [to Prime Capital Realty Ltd] ..."

⁵ Reimbursements for parking of \$2 and kilometres travelled at \$0.25/kilometre were maintained with supporting documentation.

Failure to Accept and Issue Receipts for Valid Gifts:

Animus Donandi

Our position remains that the cash contributions received by the Charity from participant donors are not valid gifts under section 118.1 of the Act. Our position is based on the fact that the primary motivation of the participant donor was not to enrich the Charity, but through a series of artificial transactions and a minimal monetary investment, to enrich themselves from the aggregate tax credits so obtained. The representations are correct in stating that there are two conditions³ which must be satisfied in order for a transfer of property to be considered a gift. However, it is our position the representations erroneously consider the only benefit received by a participating donor in the CHT tax shelter to be the charitable tax credit.

We agree that the charitable tax credit available with respect to a donation is not usually an advantage or benefit that would affect whether a gift is made. However, it is our position that mass-marketed donation arrangements promising participant donors that they will be able to claim tax credits for charitable donations far in excess of the expenditures actually made (i.e. the actual cash outlay and subsequent reduction in the donor's net worth), lack the requisite *animus donandi* for the transactions to be considered gifts.

It remains our position that the participant donors entered into the CHT tax shelter arrangement as a result of the estimated income tax saving benefits and positive return on investment promoted. The income tax savings and return on investment are based on the participant donor's aggregate "gift" of cash and pharmaceuticals units which have been valued at amounts many times higher than the participant donor's cost to participate in the arrangement. The participant donors fully intend to recoup their out-of-pocket cash outlay and to profit from the tax shelter through the artificial manipulation of the charitable gifting provisions. The Charity's role in the donation arrangement was to facilitate this by accepting money and transferring it as instructed by the tax shelter's promoters. At no point is a donation received by the Charity that it is beneficially entitled to. Your representations also confirm that the participating donors were not making a gift to a charity of their choosing, but rather made their gift to any participating charity. Your representations state, "...some donors, who had already written their cheques for gifts to another charity, were subsequently informed that charity would not be participating in the CHT program. These donors then re-wrote their cheques⁴, payable to the [Charity], for the same dates as the original cheques were written."

³ The two conditions are: 1) a voluntary transfer of property by the donor, and 2) no benefit or consideration flowing in return to the donor.

⁴ Cash contributions of at least \$573,000 were re-designated by participating donors to the Charity upon notification another charity choose not to participate in the CHT Program in 2004. These gifts were also "received" by the Charity prior to its notification of registration as a registered Canadian charity.

Accordingly, it is our position the cash contributions lack *animus donandi*; participating donors did not necessarily enrich, or intend to enrich the Charity⁵ but rather enriched themselves through artificial transactions and the income tax saved. As such, it is our position the Charity was not entitled to issue an official donation receipt in these circumstances.

Benefit Received

Per our previous letter, the CHT donation program involves Canadian participant donors making a cash donation to the Charity then applying to become a capital beneficiary of the Canadian Humanitarian Trust(s) (the Trust). The participant indicates on the application form, the number of pharmaceutical units they wish to receive and acknowledges that each of the pharmaceutical units is subject to a limited recourse lien. Upon acceptance as a beneficiary, the participant receives a capital distribution from the Trust in satisfaction of his capital interest in the Trust. The capital distribution is in the form of pharmaceutical units, which the participant then "donates" to a second designated Canadian registered charity in transactions facilitated by the promoter acting as agent for the participant. The purported value of the pharmaceutical units, on average, is three to four times the value of the cash "gift".⁶

Your letter states that "At no time did participants in the CHT Program who applied to become beneficiaries of an as-yet-to-be-settled trust have any "entitlement", that is any enforceable right, to (1) require the settlement of the trust; (2) become a beneficiary of the trust; or (3) receive a distribution from the trust's property. The receipt by a taxpayer of a gift of property from an unrelated third party, in the participants' case a distribution without consideration of pharmaceuticals from a resident Canadian trust, after making a donation to the [Charity] does not, in and of itself, constitute a "benefit" or "consideration" in return for the prior cash gift that would render the prior cash gift invalid." We make no comment on whether participants had an "enforceable right" to receive pharmaceuticals but we disagree with the Charity's submission that the pharmaceuticals so received by the participating donors is not a "benefit" or "consideration" received as a result of the cash gift. It is clear that there is a direct link between the "donation" to the Charity and the participants' eligibility to receive some form of property from the Trust. This is clear both from the promotional materials and the pattern of transactions of the participants.

It should be noted that the common law does not require there to be a legally enforceable right to receive property, but rather that a payment be made in expectation of return.⁷ We note that the promotional materials describe, in detail, how the tax shelter works, including the requisite "donation" to the specified charities. We note that the distribution of pharmaceuticals from the trust is proportionate to the amount of cash "donated" to the specified charities and that all participant donors making the requisite

⁵ We do recognize the 1% retained by the Charity is an enrichment beyond what the Charity would have received otherwise however it is preposterous that the Charity is satisfied retaining a mere 1% of the \$41.6 million flowed through its bank accounts.

⁶ The proportion of cash to purported value of the pharmaceuticals fluctuates throughout the calendar year as donor's participating earlier in a calendar year is rewarded with "cash discounts". As a result, donors contribute less cash yet receive the same purported value of pharmaceuticals as a donor who participates in the latter part of the year.

⁷ See, for example, *McPherson v. the Queen* (2007) DTC 326

cash contribution to the Charity did receive, as a result of an application to a trust, distributions of pharmaceuticals in amounts equivalent to the formulas outlined in the CHT promotional materials. It is as a result of these findings, that the CRA considers the pharmaceutical units received by the participating donors to be the advantage, benefit or consideration received by a donor directly linked to the donors' cash contribution. As such, the Charity was not entitled to issue a receipt to participants given that the payment to the Charity was made in full expectation of receiving a distribution from a trust of pharmaceutical units.

Property Transferred

Your representations confirm that there is no provision in the Act or Regulations prohibiting charities from retaining third party fundraising and paying fees to these fundraisers, and that the Act considers gifts made to a qualified donee, as defined by the Act, to be a charitable activity. While your representations are technically correct, our position and findings remain that the transactions in question are abusive to the Canadian tax system. The Charity improperly issued \$41.6 million in official donation receipts for property it did not beneficially own and for property which was flowed through the Charity's trust account to be ultimately paid to, or for the benefit of WHI and not the qualified donee, CPAR. While the Charity only directly paid a 1% + GST fundraising fee to WHI, it indirectly paid far more.

The representations state the Charity is aware that CPAR paid certain fees to WHI for fundraising and administration but the representations fail to specify that the "certain fees" referred to represent approximately 97.5%⁸ of the gross funds CPAR received from the Charity. It is therefore irresponsible of the Charity to simply consider the amounts transferred to CPAR to be gifts to a qualified donee when the purpose of the transfer, as part of the donation arrangement, was to flow the cash contributions received to WHI. The Act provides that a charity may gift its resources to a qualified donee provided that the gift is valid; the Act does not deem all transfers of funds between qualified donees to be gifts.

The representations also state that the Charity "was at all times aware of what was being done with its funds, as it provided the instructions to its [trust] lawyer. The lawyer accounted to the [Charity], in the normal course, regarding the transactions in his trust account involving the [Charity's] funds." These representations differ from our findings and statements made by Mr. McMillan during the audit, whereby he stated he merely received copies of official donation receipts issued on the Charity's behalf from WHI at year-end, received cheques from Mr. Sommer's representing the Charity's 1% of deposited funds and received a "trust-account summary" at year-end. Trusting that the third parties contracted to conduct certain activities on the Charity's behalf also does not

⁸ Per audit findings, of the gross funds received, CPAR utilizes the funds as follows: 32.68% + GST paid to WHI for donor solicitation and administration fees, 1% + GST paid to WHI for fundraising fees, an amount equivalent to 1.507% of the unencumbered value of pharmaceutical goods received from another participating charity "gifted" to this participating charity, 1% retained by the CPAR for its own operations with the balance of funds held in the trust account of WHI to pay all costs associated with administration, marketing, distribution, shipping and all other costs associated with the CHT program including all payments necessary to retire any liens or encumbrances which may be attached to any of the pharmaceuticals.

preclude the Charity from exercising an appropriate level of due diligence to ensure the third parties are operating according to the agreements signed and that any reports, summaries, receipts, etc. provided are accurate. *Per* our previous letter, the Charity failed to maintain or failed to provide complete documentation supporting its involvement in the CHT tax shelter such as the periodic updates and/or trust account summaries from Mr. Sommer's⁹ and reconciliations of the trust account deposits to total official donation receipts issued. We acknowledge the Charity signed agreements in 2004 that provided directions to Mr. Sommer's on how the funds received were to be distributed. It is presumed these agreements are the Charity's sole source of evidence it was involved in and aware of the millions of dollars of cash contributions flowing into and from its trust account in accordance with the Charity's intentions.

Based on our audit findings, we remain of the position that cash contributions made are not gifts that have actually been made to the Charity, but rather it appears that the Charity is paid a 1% fee to issue receipts for monies it neither sees, cannot access nor is entitled to. *Per* the Charity's own records, "We have been assured that Living Waters Ministry Trust will receive 1% of the donations." For this reason, there are grounds for revocation of the charitable status of Living Waters Ministry Trust under paragraph 168(1)(d) of the Act.

Application of Proposed Subsections

Per our previous letter, proposed subsections 248(32), (35) and (38) of the Act apply to the transactions described in our July 28, 2008 letter. Regardless that the legislation remains proposed, once passed into law it will apply to all transactions covered by the audit period under review. The CRA's expectation of these provisions is that, once announced, donors and charities alike should have begun to follow this legislation as, when passed, would be applied retroactively and therefore provides grounds for the revocation of a registered charity.

The representations state "the Auditor is incorrect in suggesting that a distribution by a trust of pharmaceuticals to a participant in the CHT Program, who had previously donated cash to the [Charity], is an "advantage" to be deducted from the amount of cash gift for the purposes of determining the eligible amount of the cash gift under proposed subsec. 248(31) of the Act" and goes on to further conclude there must be an enforceable contract between the donor, Charity and third parties involved. The representations consider the cash contribution and distribution of pharmaceuticals as two distinct separate transactions.

With respect, it is simply not sufficient to state that there is no link between the cash payment and the distribution from the trust where the audit evidence has revealed a

⁹ In fact, in correspondence to the Charity dated February 29, 2008, Mr. Jonathon Sommer's wrote, "You have also asked me for copies of the bank statements for the account in which your funds were held. I must decline this request, as the bank account used was a segregated account which not only held your funds, but also those of several other third parties." This indicates that the Charity neither obtained, nor previously requested, copies of bank statements for its trust account established by Mr. Sommer's and that the trust account established was not a separate account solely for the benefit of the Charity's funds.

clear link. From the information provided, it is evident that the pharmaceuticals received by the participant donors were received as a result of the donor's cash contribution to the Charity. We refer you to the CHT promotional packages whereby the donor indicates the number of pharmaceutical units he wishes to receive at the same time he contributes a cash amount equivalent to one-third (or another portion) of the pharmaceuticals purported fair market value to a participating charity. Our audits have revealed participant donors do not become beneficiaries of the trust unless a cash contribution is made to a participating charity and, if they do make this contribution, receive a distribution from the trust proportionate to the amount of cash contributed. In our view, the distribution from the trust is clearly an advantage in "consideration"¹⁰, "gratitude"¹¹ or "in any other way related to the gift or monetary contribution"¹².

Our position remains that the Charity was required by the Act to reduce the value reflected on the official donation receipt by that of the advantage received regardless if the advantage was received directly from the Charity or from another third party.

As such, it remains our position that the Charity issued receipts for transactions that do not qualify as gifts at law. For this reason, there are grounds for revocation of the charitable status of Living Waters Ministry Trust under paragraph 168(1)(d) of the Act.

Failure to Meet its Disbursement Quota:

Per our previous letter, and per our discussion above, we remain of the position that the Charity failed to meet its annual disbursement quota. We do not consider the monies transferred to CPAR, pursuant to the agreements signed, to be valid gifts made to a qualified donee as substantially all monies were ultimately paid to, or made available to WHI. The representations state "The [Charity] is not aware that the CPAR used the cash for anything other than carrying on its charitable activities" but does not provide evidence that it inquired with CPAR, or obtained evidence to support this claim, following the receipt of our July 28, 2008 letter whereby we stated CRA audits to date have revealed that substantially all monies received by it were ultimately paid to, or available to WHI.

The representations reiterate "Again, there is no provision of the Act which prohibits a charity from paying fundraising and administrative fees to a third party. Payments of fees by the [Charity] and by CPAR to the promoter of the CHT Program were an essential part of the charities' activities, carried on in support of a program which distributed pharmaceuticals in the course of a massive international humanitarian aid program". Per above, we agree there is no provision in the Act prohibiting a charity from retaining and paying service fees of third party fundraisers but CRA is concerned by the Charity's assertion that the fees were used in support of distributing pharmaceuticals. CRA audits have not concluded funds directed to CPAR were used for its own charitable purposes or for the distribution of pharmaceuticals, but as we have stated, substantially all funds

¹⁰ Ss. 248(32)(a)(i)

¹¹ Ss. 248(32)(a)(ii)

¹² Ss. 248(32)(a)(iii)

received by CPAR were paid to, or made available to, WHI for purposes other than distribution of pharmaceuticals.

Accordingly, it remains our position that the Charity has not met its disbursement quota as per paragraph 149.1(2)(b) of the Act. Therefore under paragraph 168(1)(b), the Minister may, by registered mail, give notice to the Charity that the Minister proposes to revoke its registration because it ceases to comply with the requirements of the Act related to its registration as such. For this reason, there are grounds for revocation of the charitable status of The Living Waters Ministry Trust under paragraph 168(1)(d) of the Act.

Failure to Issue Receipts in Accordance with the Act:

The representations of September 29, 2008 do not alter our findings and our position that the official donation receipts issued by the Charity to acknowledge cash contributions received from participants in the Canadian Humanitarian Trust tax shelter are not valid gifts under section 118.1 of the Act. We have fully discussed our position on this subject above.

Your representations also do not change our findings that the Charity breached Regulation 3501(3) of the Act which requires receipts with facsimile (in this case, electronic) signatures to be maintained by the Charity at their address as recorded with the Minister until completed as an official receipt. Based on the representations, and our audit findings, WHI prepared official donation receipts for the Charity and maintained copies of unused receipts bearing Mr. McMillan's electronic signature at an address other than the Charity's. This in and of itself is grounds for the revocation of the Charity's status. The fact that the Charity retained the services of WHI to assist in preparing and issuing the receipts again does not preclude the Charity from complying with the Act and its Regulations, which also includes protecting its receipts from unauthorized use; safeguarding unused and duplicate donation receipts; and properly cancelling and issuing replacement receipts where warranted. The Charity remains responsible for each receipt issued and each unused receipt regardless of whether this service is performed on the Charity's behalf or is performed by the Charity itself.

We accept the Charity's submission that errors were made while learning the software system resulting in receipts issued out of sequential order. We would also note that the software system utilized has failed to include all receipts issued for gifts in kind. A reconciliation of the duplicate receipts provided to the receipt listings indicate the listing failed to include six receipts totalling \$5,037, or nearly one-third of total non-tax shelter related donations, in 2006 and 2007. The receipts bore a different receipt number than those of cash donations received and duplicated receipt numbers were also observed. We also acknowledge the Charity advised the donor who received an official receipt for services provided to the Charity, "not use the receipt and to destroy it".

Under paragraph 168(1)(d) of the Act, the Minister may, by registered mail, give notice to the registered charity that the Minister proposes to revoke its registration if it issues a

receipt otherwise than in accordance with the Act and the Regulations. It is the CRA's position that the Charity issued receipts for transactions that do not qualify as gifts at law and breached Regulation 3501(3). For these reasons alone there are grounds for revocation of the charitable status of The Living Waters Ministry Trust under paragraph 168(1)(d) of the Act.

Failure to Maintain Adequate Books and Records:

As discussed above, it remains the CRA's position that the Charity failed to maintain and failed to provide complete and adequate records during the course of our audit. The Charity was able to provide documentation for considerably all expenditures incurred for its operations including reimbursements to Mr. McMillan for his travel expenses and phone/fax lines. The Charity was unable to provide supporting documentation for the purported \$18,000 spent by Mr. McMillan on the Charity's behalf and records supporting its involvement in, issuance of official donation receipts for and distribution of funds for charitable purposes for, the Canadian Humanitarian Trust tax shelter. We acknowledge the Charity was eventually able to obtain documents supporting its involvement in the tax shelter from WHI and Mr. Sommer; actions which support our position that the Charity willingly lent its registered charity status and tax-receipting ability to WHI in exchange for a 1% fee as it was not concerned, nor took actions to obtain, review and maintain these records prior to our audit. The Charity was not able to provide, or failed to provide, its records supporting the charitable use of its funds transferred to CPAR, including its on-going direction and control over the application of these funds by CPAR. This, in and of itself, demonstrates a lack of due diligence on the part of the directors to take an active interest in the operations of the Charity and to operate in the best interests of the Charity.

Accordingly, the Minister may, by registered mail, give notice to the Charity that the Minister proposes to revoke its registration because it fails to comply with or contravenes section 230 of the Act dealing with books and records under paragraph 168(1)(e) of the Act. It is our position the Charity has contravened section 230 of the Act for failing to maintain complete records to verify the information contained within its Registered Charity Information Returns and financial statements. For this reason, there are grounds for revocation of the charitable status of Living Waters Ministry Trust.

Appropriateness of Revocation:

Finally, we note that Mr. McMechan argues in the representations of September 29, 2008 that, "There are contentious legal issues involved with respect to the Canada Revenue Agency's positions concerning the CHT program which will be resolved in the courts...It is submitted that it would be inappropriate for the [CRA] to issue a notice of intention to revoke the [Charity's] charitable registration on the basis of unresolved legal issues. This is particularly so, given that there is no doubt whatever that the [Charity's] goal was to act pursuant to its Articles of Faith, by way of providing humanitarian aid, in supplying medicines to needy individuals in third world countries." We disagree. As above, the Charity has not engaged in, or operated in a manner that is in furtherance of

its registered objects which are to “teach and inspire individuals to develop their innate spiritual abilities for increased spiritual awareness and enlightenment.” The Charity has merely operated as a conduit for the CHT tax shelter by issuing receipts in excess of \$41.6 million for transactions that do not qualify as gifts, has failed to demonstrate how it used \$40.7 million of these funds in its own charitable activities and has breached numerous other requirements of the Act. The Charity’s submission that it has consistently taken steps to improve upon what it deems to be administrative issues, fails to address the substantive issue that the Charity has failed to devote all its resources to its own charitable activities by failing to engage in, and to undertake activities that support its charitable purposes in a manner consistent with charitable law. It is the CRA’s position that these are serious contraventions of the *Income Tax Act* and warrant the revocation of the Charity’s registered status.



REGISTERED MAIL

Living Waters Ministry Trust
123 Concord Crescent
London, Ontario N6G 3H5

Attn: Bernard F. McMillan

BN: 860719 145RR0001
File # 3026946

July 28, 2008

Subject: Audit of Living Waters Ministry Trust

Dear Mr. McMillan:

This letter is further to the audit of the books and records of Living Waters Ministry Trust (the "Charity") by the Canada Revenue Agency (the "CRA"). The audit related to the operations of the registered charity for the period from January 1, 2004 to December 31, 2006.

At our meeting of May 2, 2008, you were advised that the CRA has identified specific areas of non-compliance with the provisions of the *Income Tax Act* (the "ITA") and/or its *Regulations*. The specific areas of non-compliance identified are:

AREAS OF NON-COMPLIANCE:		
	Issue	Reference
1.	Failure to Devote Resources to Charitable Activities	149.1(2), 168(1)(b)
2.	Failure to Accept Valid Gifts in Accordance with the ITA	118.1
3.	Failure to Meet its Disbursement Quota	149.1(2)
4.	Issuing Receipts Not in Accordance with the ITA	118.1, 149.1(2), 168(1)(d)
5.	Failure to Maintain Adequate Books and Records	149.1(2), 168(1)(e), 230(2)

The purpose of this letter is to describe the areas of non-compliance identified by the CRA during the course of our audit as they relate to the legislative provisions applicable to registered charities and to provide the Charity with the opportunity to address our concerns. In order for a registered charity to retain its registration, it is required to comply with the provisions of the ITA and Common Law applicable to registered charities. If these provisions are not complied with, the Minister of National Revenue may revoke the Charity's registration in the manner prescribed in section 168 of the ITA.

The balance of this letter describes the identified areas of non-compliance in further detail.

Canada

CO P # 12001

Identified Areas of Non-Compliance:

1. Failure to Devote Resources to Charitable Activities:

The Charity is registered as a charitable organization. In order to satisfy the definition of a "charitable organization" pursuant to subsection 149.1(1) of the ITA, "charitable organization" means an organization "...All the resources of which are devoted to charitable activities".

To qualify for registration as a charity under the ITA, an organization must be established for charitable purposes that oblige it to devote all its resources to its own charitable activities. This is a two-part test. First, the purposes it pursues must be wholly charitable and second, the activities that a charity undertakes on a day-to-day basis must support its charitable purposes in a manner consistent with charitable law. Charitable purposes are not defined in the ITA and it is therefore necessary to refer, in this respect, to the principles of the common law governing charity. An organization that has one or more non-charitable purposes or devotes resources to activities undertaken in support of non-charitable purposes cannot be registered as a charity.

It is our view, based on our review that the Charity does not operate for charitable purposes. In fact, the evidence on the file, as outlined below, demonstrates that the preponderance of the effort and resources of the Charity are devoted to participating in a tax planning donation arrangement. Operating for the purpose of promoting a tax planning donation arrangement is not a charitable purpose at law.

a) Non-Charitable Purpose

It is our view, based on our audit, the Charity is pursuing a non-charitable purpose and non-charitable activities in furtherance of this purpose. In our view, the Charity is primarily operating for the purpose of supporting, promoting and participating in an abusive tax shelter arrangement. As outlined below, by engaging in a tax shelter arrangement whereby the Charity receipting over \$41 million dollars in donations, the Charity has actually received and devoted a comparatively insignificant amount of resources to its own actual charitable activities.

The Charity was registered effective September 4, 2004, and its purpose at the time of registration was to *"preach and advance the teaching of Living Waters Ministry's faith and to establish, support and maintain a house of worship with services conducted in accordance to the tenets and doctrines of the Living Waters Ministry's faith."* Within weeks of receiving its registered status, the Charity entered into an agreement with Canadian Humanitarian Trust ("CHT") whereby the Charity *"wishes to increase their donor base and to increase the monies it receives from the general population in donations; and ...wishes to increase the level of their support for humanitarian relief in the third world; and ...specifically wishes to provide financial support to the third world medical relief program of the Canadian Physicians and Aid Relief ("CPAR").* The latter of which is not an activity the Charity was registered for nor contemplated at registration.

Within the Charity's first year of operations, the Charity was able to raise and issue official donation receipts for over \$16.6 million in "gifts". All "gifts" received were pursuant to the Charity's participation in the CHT tax shelter program. The Charity has continued to

From the Charity's participation in the CHT program, it is our position the Charity is merely operating as a conduit for the identified tax shelter. In the donation arrangement, the Charity enables itself to accept the donations being promoted and sign official donation receipts prepared by WHI for the amounts determined by the tax shelter scheme promoter. Per correspondence obtained, *"Living Waters Ministry Trust (LWM) agreed to prepare tax receipts with the help of World Health Initiatives Inc for the donations in a form acceptable to Canada Revenue Agency, in a timely manner, and not later than 7 days from the date of notification (from WHI) of the gift."* In fact, the Charity was not involved in the actual receipt of the cash "gifts" made to the Charity as all transactions were handled by a trust lawyer, Jonathan J. Sommer. Mr. Sommer maintained a trust account on behalf of the Charity and distributed the funds received as instructed, presumably by WHI, to the Charity, to WHI and to CPAR. Based on the information available, the Charity was so eager to participate in the CHT program that it accepted and receipted for donations received prior to its registration as a registered charity and prior to its official signing of the agreement with WHI. From the documentation presented to CRA, the Charity began preparing receipts to acknowledge deposits received by Mr. Sommer in early August 2004.

The Charity has not demonstrated the activities undertaken or resources it consulted as part of its due diligence undertaken to evaluate the authenticity of the CHT program in which it participated or how participation in the CHT program furthered its charitable activities aside from the relatively small portion of cash "earned". Mr. McMillan attended a CHT seminar in London, Ontario in and around September/October 2004 and approached Mr. Stephen Rosen, Director of CHT, about the Charity's interest and potential involvement in the CHT program. Mr. Rosen contacted the Charity in October 2004 and the Charity signed its contract with WHI on October 19, 2004. The Charity did not seek to obtain an independent review of the donation arrangement at that time. We would also note the Charity has not shown that it has sought professional advice from its own legal or accounting representatives or reviewed the professional opinions presented by CHT in any of the years in which it has participated.

Given the manner in which the Charity structures and conducts its activities to accommodate this tax shelter, and the proportional levels of involvement in this arrangement, it is our view that a collateral purpose, if not primary purpose of the Charity is, in fact, to support and promote the tax shelter arrangement. In this regard, it appears the Charity enthusiastically lends its resources (not to mention tax receipting privileges) to support this tax shelter arrangement, with little regard for the mandate and best interests of the Charity itself. Operating for the purpose of promoting tax shelters is not a charitable purpose at law.

It is our view, therefore, that by pursuing this non-charitable purpose, the Charity has failed to demonstrate that it meets the test for continued registration under 149.1(1) as a charitable organization "all the resources of which are devoted to charitable activities". For this reason, it appears to us that there are grounds for revocation of the charitable status of Living Waters Ministry Trust.

participate in the CHT tax shelter program, promoted by World Health Initiatives Inc. ("WHI"), in fiscal periods ending 2005, 2006 and 2007 by agreeing to accept cash from taxpayers who were also participants in the tax shelter and by agreeing to forward a certain percentage of the cash received to a designated registered charity, also participating in the tax shelter arrangement.

Generally, the CHT donation program involves Canadian individual participants (the "donors") making a cash donation to a designated registered charity such as the Charity. The donor then makes application to become a capital beneficiary of the Canadian Humanitarian Trust(s) (the "Trust"). The donor indicates on the application the number of pharmaceutical units they wish to receive. The donor also acknowledges on the application that each of the pharmaceutical units is subject to a limited recourse lien. Upon acceptance as a beneficiary, the donor receives a capital distribution from the Trust in satisfaction of his capital interest in the Trust. The capital distribution is in the form of pharmaceutical units, which the donor then "donates" to a second designated Canadian registered charity in transactions facilitated by the Promoter acting as agent for the donor. The donor receives two official donation receipts for the "gifts" made to both charities: one receipt for the cash "gift" and one receipt for the value of the pharmaceutical units less the lien amount.

The CHT donation program also involves the participation of a third designated Canadian registered charity. This designated charity receives "donations" of pharmaceutical units from the second designated charity and also receives "donations" of cash from the first designated charity. The third charity is represented as being a distributor of the pharmaceutical units and as such, has purportedly "distributed" the pharmaceutical units to needy individuals in third world countries.

As noted above, the Charity's role in this donation arrangement is to accept and issue receipts for the participant donor's cash contribution and to "gift" a certain percentage of the participant donor's cash contribution to the third designated Canadian registered charity. The Charity earns, for its participation, tax-receipting ability and registered charity status, 1% of the gross value of official donation receipts issued. The Charity is also required to pay 1% + GST of the gross value of the official donation receipts issued to WHI as fundraising fees with the remainder of the funds "gifted" to the designated third participating charity, Canadian Physicians for Aid and Relief ("CPAR").

For the years audited, the Charity has issued official donation receipts for "gifts" received from participant donors of over \$41.6 million per its annual information returns filed and has accordingly "earned" over \$416,000 as a result of its participation in the CHT program. During this same period, the Charity earned negligible income, approximately \$15,600, from offerings, investment income and rental income. The Charity also paid fundraising fees to WHI in excess of \$445,000 less any GST/HST rebate the Charity applied for, and "gifted" over \$40.7 million to CPAR. We note the Charity has reported the "gifts" made to CPAR as expenditures on its own charitable programming as per its annual information returns filed however the Charity has failed to show how the funds transferred to CPAR were in furtherance of the Charity's registered objects.¹ Of the funds transferred to CPAR, CRA audits have revealed substantially all of the funds revert back to the tax shelter promoter, namely WHI, as fundraising costs and were therefore not used for charitable programming.

¹ We note that the mandate of this CPAR has little, if anything, in common with the stated purposes of the Charity.

b) Personal Benefit:

Paragraph 149.1(1)(b) of the ITA stipulates that no part of a charity's income is payable or otherwise available for, the personal benefit of any proprietor, member, shareholder, trustee or settler thereof. The CRA considers the meaning of the term "trustee", for registered charity purposes, to include those persons who stand in a fiduciary relationship to the charity, having general control and management of the administration of a charity, including directors of corporations established for charitable purposes. This is, essentially, a rule against self-dealing, reflecting the general rule of equity that a trustee must not profit out of his position of trust, nor must he place himself in a position where his duties as a trustee conflict with his own interests. It is also a statutory embodiment of the common law test that individuals with ties to a charity should not profit from their association with the charity. The Charity's Constitution, Article 111(6) also state *"The executive or directing officers, leadership team member(s) or leader(s) shall not be paid a salary but are entitled to expenses provided they have been pre approved by the majority of the executive or directing officers."*

The audit has discovered the Charity repaid a loan purportedly made by a director of the Charity, Bernard McMillan. Mr. McMillan claims to have loaned the Charity \$50,000 in 2006 for the purposes of renovating the place of worship acquired in March 2006. Mr. McMillan did not advance the funds to the Charity directly but alleges to have paid for certain expenses, such as casual labour and renovation expenses, on behalf of the Charity. Mr. McMillan has represented to us that he performed most of the renovation work himself except for landscaping contract payments made. Mr. McMillan also alleges to have given \$20,000 to a parish member for the sole purpose of having the parish member pay a \$20,000 down payment on the church.

The Charity was able to provide minimal documentation to support Mr. McMillan's claim he loaned funds to the Charity. The Charity and Mr. McMillan were able to substantiate \$6,000 of the \$50,000 recorded as loaned by Mr. McMillan. The Charity also provided documentation supporting \$20,000 was received from the parish member and that \$20,000 was paid to Prime Capital Reality Ltd as a down payment on the acquisition of the church. Mr. McMillan has not provided sufficient evidence to support his assertion the funds were originally loaned by him to the parish member nor has either party provided source documents to support the alleged \$24,000 incurred for labour and renovation costs regardless whether the costs were performed by Mr. McMillan or by other parties.

The loan, plus \$1,500 for Mr. McMillan's part time help, was repaid in December 2006 and January 2007 after the Charity received its 1% "earnings" distribution from WHI. In April 2008, the Charity has decided to write-off \$24,000 in expenses as the supporting documentation is not available to support these expenses however Mr. McMillan has indicated he will not be repaying the Charity personally for the \$24,000 he received simply because *"They [the Board] all know that I spent the money"*. In this regard, it is our view that the director has financially, and improperly, benefited from his position as a director of the Charity.

It is our view, that by transferring charitable assets for the private gain of a director, the Charity has failed to demonstrate that it meets the test for continued registration under 149.1(1) as a charitable organization that "no part of the income of which is payable to, or is otherwise available for, the personal benefit of any proprietor, member, shareholder, trustee or settlor

thereof". For this reason, it appears to us that there are grounds for revocation of the charitable status of Living Waters Ministry Trust.

2. Failure to Accept Valid Gifts in Accordance with the ITA:

It is our position that the Charity has contravened the *Income Tax Act* by accepting and issuing receipts for transactions that do not qualify as gifts. We offer the following explanations to support our position.

a) No *Animus Donandi*

Under the common law, a gift is a voluntary transfer of property without consideration. However, an additional essential element of a gift is *animus donandi* - that the donor must be motivated by an intention to give. It must be clear that the donor intends to enrich the donee, by giving away property, and to generally grow poorer as a result of making the gift.

It is our view that the vast majority of the transactions involving the Charity fail to meet this latter element. The common theme, found throughout all of these transactions, is that through an artificial series of transactions and a minimal monetary investment, "donors" profit through the tax credits so obtained. It is clear that the primary motivation of the donors is intent to profit, and, as such, these transactions fail to qualify as gifts at law.

In support of this position, we note the promotion materials primarily focus on the substantial return on investment as a result of the donor's participation with greater returns on investment offered to participants "donating" early within the calendar year. Minimal investment is required on the donors. Donors give money to the Charity and, in return, receive a distribution of "valuable" medicine units from a trust. These goods are "gifted" by participants to another participant charity without using or seeing the property. The goods are typically transferred from the donors to the Charity within a few days of purchase or trust distribution. Minimal information is provided to the prospective investors as to how the "donations" will benefit the charity, or to the activities of the charity they are supporting. Transactions are pre-arranged and handled entirely by promoters or other pre-arranged third parties. Participants in these arrangements are merely expected to put forward a minimal investment to receive generous tax receipts in return.

As such, it is our position that there is no intention to make a "gift" within the meaning assigned at 118.1 of the ITA. Participants in these donation arrangements are primarily motivated by the desire to profit from the artificial manipulation of the tax incentives available from donations rather than a desire to enrich the participating charity. In our view, these transactions, given the combination of the tax credits and other benefits received, lack the requisite *animus donandi* to be considered gifts.

b) Transfers not gifts - Benefit received

Additionally, we are of the opinion that the transactions themselves lack the necessary elements to be considered gifts at law. The "donors" received some form of consideration or benefit that was directly linked to their cash donations. It is clear, based upon our audit and the promotional materials of CHT that there was a clear expectation of return with respect to the

donation made to the Charity. "Donors" received the benefit of becoming owners of medicine units and having the options to distribute them, without cost, from the trust. The donor's entitlement to receiving the units from the trust was clearly linked to and proportionate to the amount of cash "donated".

In our view, it is clear that the cash transferred to the Charity were not gifts in the sense understood at law. The Charity was, therefore, not entitled to issue official donation receipts for the amounts that it received. In our findings, the Charity has issued in excess of \$41.6 million in donation receipts for transactions that did not qualify as gifts. It is clear from our audit and the promotional materials of CHT and WHI, which the Charity engaged as fundraisers that the Charity knew, or ought to have known, that there was a clear link between what was "donated" to it and the distribution of goods the donors purportedly would receive from the trust. The Charity knew, or ought to have known, that it was not entitled to issue donation receipt for these transactions.

It is clear that the amount paid by investors is, in effect, not a donation but both the price of participation levied by the tax shelter/donation arrangement and a payment to receive a distribution from the trust. While the payment was transferred to the Charity, this amount was not a voluntary transfer of property, without expectation of return, within the sense contemplated by the term "gift" at law as all participants expected to receive "medicine units" in return for their payments. Indeed, and as above, it is all the more disturbing that the Charity freely lent its tax receipting privileges not only for transactions that do not qualify as gifts, but for monies it was not even entitled to retain, beyond its 1% commission, substantially all of which flowed into the hands of the promoters. In our view, given that the Charity is responsible for the issuance of \$41.6 million in improper tax receipts, this represents an extremely serious abuse of the Charity's tax receipting privileges.

c) Property Transferred

We are greatly concerned that the property for which the Charity has issued receipts was at no time beneficially owned by the Charity. The Charity at no time had discretion to retain, beyond 1% of the gross amount for which it issued tax receipts, the property which was donated to it. The funds were, as part of its paid participation in the arrangement, earmarked to be transferred to another participating registered charity. As above, our audit has revealed that the overwhelming majority of these funds were, in fact, paid to the promoters of the arrangements. In fact, the funds were at no time under the control and direction of the Charity as these were controlled and paid out by a trust lawyer, Mr. Sommer, retained by WHI. The Charity was merely a recipient of the disbursements permitted from the trust account maintained in their name and it was only these funds, the 1% of the gross official donation receipts issued, the Charity had unfettered discretion to use.

Based on this we are unconvinced that gifts have actually been made to the Charity, but rather it appears that the Charity is paid a 1% fee to issue receipts for monies it neither sees, cannot access, nor is entitled to. For this reason, it appears to us that there are grounds for revocation of the charitable status of Living Waters Ministry Trust under paragraph 168(1)(d) of the ITA.

d) Application of the Proposed Legislation

Even without reference to the common law definition of a gift, it is clear that proposed section 248(32) of the ITA applies to these transactions as well. While this legislation is still proposed, once passed into law, it applies to all transactions covered by the audit period under review. In our view, the distribution from the trust is an advantage which is in consideration for the gift² or is otherwise related to the gift.³ The Charity was therefore required by the ITA to reduce the value reflected on the receipt by that of the advantage. There is no indication whatsoever that the Charity took these provisions into account when issuing receipts on behalf of the tax shelter arrangement.

It is also our view that the purpose of the Charity's participation in this arrangement is to facilitate the tax shelter arrangement by enabling it to avoid the application of proposed subsection 248(35). Subsection 248(35) applies to limit a taxpayer who receives property from a tax shelter arrangement to the cost of the property to the taxpayer. It is our view that the purpose of the "gift" to the Charity is to avoid the application of 248(35) by characterizing what is, in fact, a payment to receive medicine units as instead a gift to the Charity. As it is clear, in our view, that one of the purposes of this transaction is to avoid the application of 248(35) to a gift of property, that proposed subsection 248(38) also applies. As such, the value of the gift is deemed, according to the ITA, to be nil and the Charity was not entitled to issue tax receipts for any of the payments made to it.

3. Failure to Meet its Disbursement Quota:

In this arrangement, all the money donated to the Charity for the CHT program is received by the Trust lawyer. Then, the Charity must, as a mandatory condition of its participation transfer approximately 98% of the cash received in its name to CPAR. In our view, these cash "gifts" made by the Charity are, in fact not gifts. First, these fail to meet the definition of a gift as they lack an element of voluntariness. Second, these funds are not in fact given, free and clear, for the use of CPAR, but as a part of the same overall arrangement are earmarked to be paid to the promoter as fundraising fees. In our view these transactions fail to qualify either as gifts to a qualified donee for income tax purposes, nor are they expenditures by the Charity on activities carried on by the organization itself. It is our view, therefore, that the Charity is not spending sufficient funds towards its disbursement quota.

4. Issuing Receipts not in Accordance with the ITA:

The law provides various requirements with respect to the issuing of official donation receipts by registered charities. These requirements are contained in Regulations 3500 and 3501 of the Act and are described in some detail in Interpretation Bulletin IT-110R3 *Gifts and Official Donation Receipts*.

The audit reveals that the donation receipts issued by the Charity do not comply with the requirements of Regulation 3501 of the ITA and IT-110R3 as follows:

² See proposed sub-paragraph 248(32)(a)(i)

³ See proposed sub-paragraph 248(32)(a)(iii)

- Receipts issued to acknowledge cash "gifts" received as a result of the Charity's participation in the CHT tax shelter were not valid gifts under section 118.1 of the ITA. Under the *Income Tax Act*, a registered charity can issue official donation receipts for income tax purposes for donations that legally qualify as gifts.
- Receipts were missing serial numbers and were not issued in sequential order (Regulation 3501(1)(c)).
- Receipts were issued for gifts of services (IT-110R3 Paragraph 15(d)).
- Receipts were issued to individuals despite the cash donation being made by a corporation (Regulation 3501(1)(g)).

Additionally, the Charity was unable to provide details concerning any cancellation and/or issuance of replacement receipts or safeguarding of unused and duplicate official donation receipts issued as all receipting functions were performed on the Charity's behalf by WHI. As above, the Charity signed an agreement with WHI in October 2004 whereby WHI would assist the Charity in its preparation of official donation receipts *"in a form acceptable to Canada Revenue Agency, in a timely manner, and not later than 7 days from the date of notification (from WHI) of the gift"*. The Charity has indicated the receipts were prepared by WHI using Mr. McMillan's electronic signature and Mr. McMillan has never verified any of the receipts issued. It is our position the Charity has failed to exercise any control over or demonstrate its on-going due diligence to ensure receipts issued on the Charity's behalf complied with the ITA and as such, were issued for valid gifts.

We note that the Charity's complete abdication of its responsibility for the issuance of receipts, in addition to being extremely concerning in the circumstances, is in breach of regulation 3501(3) of the ITA which requires receipts with facsimile (in this case, electronic) signatures to be maintained by the Charity at their address until complete. This in and of itself is grounds for the revocation of the Charity's status. The fact that Charity was unaware of the transactions as they occurred, and only informed post-fact of what had been "donated" to it, and to an account that the Charity cannot access, only adds to the seriousness of this non-compliance.

Additionally, we would like to inform you that certain amendments to the ITA were introduced as part of Bill C-33 tabled in Parliament on March 23, 2004, that came into force May 13, 2005. As part of the amendments, a registered charity that issues an official donation receipt that includes incorrect information is liable to a penalty equal to 5% of the eligible amount stated on the receipt. This penalty increases to 10% for a repeat infraction within 5 years.

A registered charity that issues an official donation receipt that includes false information is liable to a penalty equal to 125% of the eligible amount stated on the receipt, where the total does not exceed \$25,000. Where the total exceeds \$25,000, the charity is liable to a penalty equal to 125% and the suspension of tax-receipting privileges. We do not believe that this is an appropriate alternative, given the serious nature of the matter of non-compliance.

Under paragraphs 168(1)(d) of the ITA, the Minister may, by registered mail, give notice to the registered charity that the Minister proposes to revoke its registration if it issues a receipt otherwise than in accordance with the ITA and the Regulations. It is our position the Charity

issued receipts for transactions that do not qualify as gifts at law. For this reason alone there are grounds for revocation of the charitable status of The Living Waters Ministry Trust under paragraph 168(1)(d) of the ITA.

5. Failure to Maintain Adequate Books and Records:

The ITA, per subsection 230(2), requires that every registered charity shall keep records and books of account at an address in Canada recorded with the Minister or designated by the Minister containing:

- Information in such form as will enable the Minister to determine whether there are any grounds for the revocation of its registration under the Act;
- A duplicate of each receipt containing prescribed information for a donation received by it; and

Other information in such form as will enable the Minister to verify the donations to it for which a deduction or tax credit is available under the ITA.

In addition, subsection 230(4) also states "every person required by this section to keep books of account shall retain:

- a) The records and books of account referred to in this section in respect of which a period is prescribed, together with every account and voucher necessary to verify the information contained therein, for such period as is prescribed; and
- b) All other records and books of account referred to in this section, together with every account and voucher necessary to verify the information contained therein, until the expiration of six years from the date of the last taxation year to which the records and books relate".

The audit indicated the books and records kept by the Charity were inadequate for the purposes of the ITA. In the course of the audit, the following deficiencies were noted:

- The Charity was unable to provide adequate supporting documents regarding its involvement in the CHT program. Particularly, the Charity does not have nor did it obtain a copy of the agreement it signed with WHI or statements for the trust account maintained by Mr. Sommer on behalf of the Charity.
- The Charity was unable to provide complete details of and supporting documentation for all recorded expenditures. Details and support for payments to casual workers and contractors for the renovation of the church building were not maintained and/or not provided.
- The Charity was unable to substantiate the loan purportedly received from Mr. McMillan and repaid by the Charity in 2006 and 2007.
- T4A statements of remuneration slips and summaries were not prepared and filed for the payments to casual workers and individual contractors.

Under paragraph 168(1)(e) of the ITA, the Minister may, by registered mail, give notice to the charity that the Minister proposes to revoke its registration because it fails to comply with or contravenes section 230 of the ITA dealing with books and records. It is our position Living Waters Ministry Trust has failed to comply with and has contravened section 230 of the ITA. For this reason alone there are grounds to revoke the registered status of Living Waters Ministry Trust.

The Charity's Options:

a) No Response

You may choose not to respond. In that case, the Director General of the Charities Directorate may give notice of its intention to revoke the registration of the Charity by issuing a Notice of Intention to Revoke the registration of the Charity in the manner described in subsection 168(1) of the ITA.

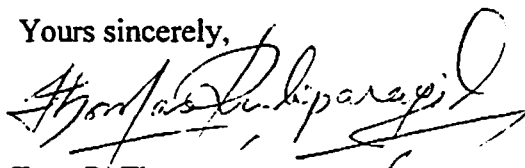
b) Response

Should you choose to respond, please provide your written representations and any additional information regarding the findings outlined above ~~within 30 days~~ from the date of this letter. After considering the representations submitted by the Charity, the Director General of the Charities Directorate will decide on the appropriate course of action, which may include the issuance of a Notice of Intention to Revoke the registration of the Charity in the manner described in subsection 168(1) of the ITA.

If you appoint a third party to represent you in this matter, please send us a written authorization naming the individual and explicitly authorizing that individual to discuss your file with us.

If you have any questions or require further information or clarification, please do not hesitate to contact the undersigned at the number indicated below.

Yours sincerely,



Tony P. Thomas
Verification and Enforcement Division
Kitchener Tax Services Office

Telephone: 519 - 896-3706
Facsimile: 519 - 585-2803

Address: 166 Frederick Street
Kitchener, ON N2G 4N1