



Canada Revenue
Agency

Agence du revenu
du Canada

JAN 05 2011

REGISTERED MAIL

Pediatric AIDS Canada/USA
10 Downie Street, Suite 302
Stratford ON N5A 7K4

BN: 13506 3097 RR0001
File #: 0941385

Attention: Adrienne Clements

**Subject: Notice of Intention to Revoke
 Pediatric AIDS Canada/USA**

Dear Ms. Clements:

I am writing further to our letter dated February 4, 2010 (copy enclosed), in which you were invited to submit representations as to why the registration of Pediatric AIDS Canada/USA (the Organization) should not be revoked in accordance with subsection 168(1) of the *Income Tax Act*.

We have reviewed and considered the Organization's written response dated May 7, 2010 (copy enclosed) from your authorized representative, Ms. Karen Cooper of Carters Professional Corporation, wherein the Organization has stated that while it does not concur with the Canada Revenue Agency's (CRA) findings, it does not intend to oppose the revocation of its charitable registration. Notwithstanding your reply, our concerns with respect to the Organization'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:

The audit of Pediatric AIDS Canada/USA (the Organization) has revealed serious issues of non-compliance. In particular, the Canada Revenue Agency (CRA) found that the Organization devoted the majority of its resources to fundraising and administrative expenses rather than on charitable activities. Further, the Organization has participated in an international donation arrangement designed to disguise this lack of activity by artificially inflating the ratio of funds spent on charitable activities.

The Organization received \$5.06 million in cash donations. Of this amount \$3.26 million was directed to fundraising and administrative fees while only \$1.8 million was spent on its own charitable activities.

Further, as part of the international donation arrangement, the Organization paid \$877,000 to allegedly acquire property with a purported value of \$15.5 million. The Organization then reported distributing this property as part of its own activities. However, the Organization's records fail to substantiate the value of the property purportedly received,

Canada

Place de Ville, Tower A
320 Queen Street, 13th Floor, 250 E (08)
Ottawa ON K1A 0L5

whether it was ever in its possession, or whether the property was ever distributed. As above, it is our view that the purpose of participating in this international donation arrangement was to artificially inflate its expenditures on charitable activities.

As such, it is our view that the Organization has failed to demonstrate that it meets the definition of a charitable organization "all the resources of which are devoted to charitable activities carried on by the Organization itself".

Our audit also found that the Organization failed to file an accurate information return, issued official donation receipts otherwise than in accordance with the Act and gifted funds to a non-qualified donee. For all of these reasons, and for each of these reasons alone, it is the position of the CRA that the Organization's registration should be revoked.

Consequently, for each of the reasons mentioned in our letter dated February 4, 2010, I wish to advise you that, pursuant to subsection 168(1) and 149.1(2) of the Act, I propose to revoke the registration of the Organization. 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), 168(1)(c), 168(1)(d), 168(1)(e), and paragraph 149.1(2)(b) of the Income Tax Act, that I propose to revoke the registration of the organization listed below and that the revocation of registration is effective on the date of publication of this notice.

Business Number	Name
13506 3097RR0001	Pediatric AIDS Canada/USA Stratford ON

Should you wish to object to this notice of intention to revoke the Organization'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 Organization's registration will be revoked on the date of publication, unless the CRA 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 Organization must obtain a stay to suspend the revocation process, notwithstanding the fact that it may have filed a Notice of Objection.

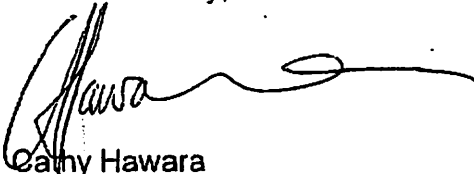
Consequences of Revocation

As of the effective date of revocation:

- a) the Organization 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 Organization 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 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 relevant provisions of the Act concerning revocation of registration, the tax applicable to revoked charities, and appeals against revocation, can be found in Appendix "A", 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 Organization will no longer qualify 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).

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 the prescribed form, containing prescribed information, for each taxation year. The *Return of Income* must be filed without notice or demand.

Yours sincerely,



Cathy Hawara
Director General
Charities Directorate

Attachments:

- CRA letter dated February 4, 2010;
- Your letter dated May 7, 2010;
- Appendix "A", Comments on Representations; and
- Appendix "B", Relevant provisions of the Act

c.c.: Karen J. Cooper, Carters Professional Corporation
70 Gloucester Street
Ottawa ON K2P 0A2



CANADA REVENUE
AGENCY

AGENCE DU REVENU
DU CANADA

February 4, 2010

HAND DELIVERED & REGISTERED MAIL

Pediatric AIDS Canada
10 Downie Street, Suite 302
Stratford, On N5A 7K4

BN: 135063097 RR0001
File #: 094138

Attention: Adrienne Clements

Re: Audit of Pediatric AIDS Canada

Dear Ms. Clements:

This letter is further to the audit of the books and records of Pediatric Aids Canada (the Organization) conducted by the Canada Revenue Agency (the CRA). The audit related to the operations of the Organization for the period of July 1, 2005 to December 31, 2007. The audit is a follow-up to our audit of the Organization's 1995 to 1999 fiscal period ends.

As per our discussions, the Organization was advised that the CRA has identified specific areas of non-compliance with the provisions of the *Income Tax Act* (the Act) and/or its *Regulations* in the following areas:

AREAS OF NON-COMPLIANCE:		
	Issue	Reference
1.	Failure to Devote All of Its Resources to its Charitable Purposes	149.1(1), 168(1)(b)
2.	Failure to Maintain Adequate Books and Records	168(1)(e)
3.	Failure to File an Information Return as Required by the Act	149.1(14), 168(1)(c)
4.	Failure to Issue Donation Receipts in Accordance with the Act	Regulations 3501
5.	Failure to Satisfy the Disbursement Quota Requirement	149.1(1); 149.1(2); 168(1)(b)

The purpose of this letter is to describe the areas of non-compliance identified by the CRA during the course of the audit as they relate to the legislative and common law requirements applicable to registered charities, and to provide the Organization with the opportunity to make additional representations or present additional information. In order for a registered charity to retain its registration, legislative and common law compliance is mandatory, absent which the Minister of National Revenue (the Minister) may revoke the Organization's registration in the manner described in section 168 of the Act.

Below we provide an overview of the requirements for registration and identify the areas of non-compliance. Attached to this letter, at Appendix "A", we provide details of our findings and elaborate on the non-compliance matters.

Identified Areas of Non-Compliance:

1. Failure to Devote all of its Resources to its Charitable Purposes:

The Organization is registered as a charitable organization. Under subsection 149.1(1) of the Act, a "charitable organization" is defined as "an organization...all the resources of which are devoted to charitable activities carried on by the organization itself..."

In order for an organization to be recognized as a charity, it must be constituted exclusively for charitable purposes, and devote its resources to charitable activities in furtherance thereof.¹ In the Supreme Court decision of *Vancouver Society of Immigrant and Visible Minority Women v. M.N.R.* [1999] 1 S.C.R. 10, Iacobucci J. speaking for the majority, summarized the requirements for charitable registration at paragraph 159, as follows:

"In conclusion, on the basis of the Canadian jurisprudence, the requirements for registration under s. 248(1) come down to two:

- (1) the purposes of the organization must be charitable, and must define the scope of the activities engaged in by the organization; and*
- (2) all of the organization's resources must be devoted to these activities."*

The term "charitable" is not defined in the Act therefore it is necessary to rely on the jurisprudence in the common law. The courts have recognized four general categories of charitable purposes: (1) the relief of poverty; (2) the advancement of religion; (3) the advancement of education; and (4) other purposes beneficial to the community as a whole (or a sufficient section thereof) in a way that the law regards as charitable. This last category identifies an additional group of purposes that have been held charitable at law rather than qualifying any and all purposes that provide a public benefit as charitable.

In order to accomplish its charitable purposes, a registered charity may only use its resources (funds, personnel and/or property) in two ways, both inside and outside of Canada: for charitable activities undertaken by the charity itself under its continued supervision, direction and control; and for gifting to "qualified donees" as defined in the Act.

The objects of the Organization are:

- support research concerning pediatric AIDS in Canada through fund raising and other initiatives;
- to establish an interactive AIDS database;
- to assist developing countries in attaining the technology to access the database; and

¹ *Vancouver Society of Immigrant & Visible Minority Women v. Minister of National Revenue*, [1999] 1 S.C.R. 10, at page 110 (paragraph 152, 154, 156)

- to create and maintain a current listing of all AIDS related community services and resources

We do not dispute that the wording of these objects could possibly be seen in a charitable vein; however, our audit has revealed little of these activities being conducted. Our audit has revealed a preponderance of effort and resources devoted to non-charitable activities. The Organization has devoted a substantial portion of its efforts and resources to fundraising and to participating in an international donation arrangement with a comparatively minor portion of its resources devoted to its registered purpose.

Turning to the "devotion of resources", a registered charity may only use its resources (funds, personnel and/or property) in two ways, both inside and outside Canada – for charitable activities undertaken by the charity itself, under its continued supervision, direction and control; and for gifting to "qualified donees" as defined in the Act.

Fundraising Activities

Fundraising is not a charitable activity. A registered charity can raise funds to support its charitable purposes, but:

- If the fundraising activity becomes the primary emphasis of the charity, then it is not operating for exclusively charitable purposes; and
- If a substantial portion of the charity's revenues is devoted to the fundraising activity, it is not considered to be devoting its resources to charitable activities.

A registered charity that engages in fundraising as a primary activity, or that devotes a substantial portion of its revenue to fundraising activities, is putting its registered status in jeopardy.

Our audit findings reveal that the Organization devotes a substantial portion of its actual cash contributions to fundraising activities as discussed in Appendix "A". It is our view that by pursuing these non-charitable purposes, the Organization 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".

Activities Outside Canada

The CRA acknowledges that it is not always practical for a registered charity to become directly involved in charitable activities because of limited financial resources, the size of the project or because the charity lacks the necessary expertise to operate effectively in a particular area of interest. Accordingly, CRA will consider that a registered charity is involved in its own charitable activities if the charity demonstrates that it maintains the same degree of control and responsibility over the use of its resources by another entity as it would if its activities were conducted by the charity itself.

Where a registered charity chooses to operate through an appointed agent or representative ("intermediary"), it must be able to substantiate, generally through documentary evidence, that it has arranged for the conduct of certain specific activities on its

behalf, and has not simply made a transfer of resources to a non-qualified donee. A charitable organization is not at liberty to transfer funds or resources to other individuals or entities unless the recipient is an employee of the charity, an agent of the charity under contract, or a qualified donee. To this end, the charity must be able to demonstrate to the CRA's satisfaction that it maintains control over, and is fully accountable for, the use of resources provided to the intermediary, at all times.

The existence of an arrangement that demonstrates sufficient and continuing direction and control over, and full accountability for, all resources and related activities, is critical. The arrangement must establish that the activities in question are, in fact, those of the Organization.

We refer to the comments of the court in *The Canadian Committee for the Tel Aviv Foundation vs. Her Majesty the Queen*²:

"Pursuant to subsection 149.1 (1) of the [Income Tax Act], a charity must devote all its resources to charitable activities carried on by the organization itself. While a charity may carry on its charitable activities through an agent, the charity must be prepared to satisfy the Minister that it is at all times both in control of the agent, and in a position to report on the agent's activities..."

And

"Under the scheme of the Act, it is open to a charity to conduct its overseas activities either using its own personnel or through an agent. However, it cannot merely be a conduit to funnel donations overseas".

As re-iterated by the Federal Court of Appeal, it is not enough for a charity to fund an agent that carries on certain activities. The Act requires that the agent actually conduct those activities *on the organization's behalf*³:

"A charity that chooses to carry out its activities in a foreign country through an agent or otherwise must be in a position to establish that any acts that purport to be those of the charity are effectively authorized, controlled and monitored by the charity."⁴

In this respect, the Organization has not shown that through its programs and arrangements for the undertaking of activities, it devotes all of its resources to its own charitable activities. The Organization has not shown that the activities are charitable and that it has continued supervision, direction and control over the programs.

In addition, over the period being audited, the Organization made financial contributions to organizations that are not considered to be "qualified donees" under the Act.

² *The Canadian Committee for the Tel Aviv Foundation vs. Her Majesty the Queen*, 2002 FCA 72 at paragraphs (FCA) at paragraphs 40 and 30

³ *Baylt Lepletot v. Minister of National Revenue*, [2006] FCA 128

⁴ *Canadian Magen David Adom for Israel v. Minister of National Revenue*, [2002] FCA 323 at paragraph 66

2. Failure to Maintain Adequate Books and Records:

Subsection 230(2) of the Act requires that every registered charity maintain adequate books and records, and books of account, at an address in Canada recorded with the Minister.

"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 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."*

It is our view the Organization has failed to maintain adequate books and records to support that it devoted all of its resources to its charitable programs. The Organization's books and records and the internal accounting controls supporting them are considered to be inadequate. As a result, the auditor was unable to confirm revenue (including receipted donations) and expenditures as recorded; the accounting of receipts; and the charitable nature of expenditures reported on the Registered Charity Information Return (T3010). As a result, the Organization appears to have failed to meet the requirements of subsection 230(2) of the Act.

3. Failure to File an Information Return As Required by the Act:

Pursuant to subsection 149.1(14) of the Act, every registered charity must, within six months from the end of the charity's fiscal period (taxation year), without notice or demand, file a Registered Charity Information Return with the applicable schedules.

It is the responsibility of the charity to ensure that the information that is provided in its Return, schedules and statements, is factual and complete in every respect. A charity is not meeting its requirement to file an Information Return if it fails to exercise due care with respect to ensuring the accuracy thereof.

The Organization has improperly completed T3010A returns for the December 31, 2006 through December 31, 2007 fiscal periods, as there were numerous errors and omissions.

4. Failure to Issue Receipts in Accordance with the Act

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*.

When a registered charity issues a receipt to acknowledge a gift of non-cash property, the charity is responsible to ensure that the value on the receipt is accurate. Generally, a member of a charity, or another individual, can attest to the value of the property if the value of the property is less than \$1,000 and as long as the member or individual has sufficient knowledge of the property.

In those circumstances where the value of the property exceeds \$1,000, we strongly recommend that the property be appraised by an independent third party; an independent party is one who is not affiliated with the charity or the donor. The person should be knowledgeable about the principles, theories, and procedures of the applicable valuation discipline and follow the *Uniform Standards of Professional Appraisal Practice* or the standards of the profession. In each scenario, the person determining the fair market value of the item should be competent and qualified to evaluate the particular property being donated. Also, he should be knowledgeable about and active in the marketplace for the specific property.

We recognize that appraisals are not required under the Act or its Regulations. However, it is our view that the onus remains with the Organization to ascertain that the value assigned to non-cash gifts received is reflective of the fair market value of the goods being donated.

The Organization has not shown that it sought, nor has it provided, independent appraisals of the non-cash property received. It has issued receipts to acknowledge non-cash gifts that were not issued in accordance with Regulation 3501.

We would add that where a charity issues receipts with incorrect or false information, subsection 188.1(7) provides for a possible alternative to a revocation action. This provision provides for a penalty equal to 5% of the eligible amount stated on the receipt. This penalty increases to 10% for a repeat offence within five years. A charity that issues an official donation receipt that includes deliberately false information may be liable to a penalty equal to 125% of the eligible amount stated on the receipt and if the penalty is in excess of \$25,000, the charity is also liable to one year's suspension of its charitable status. We do not believe that this is an appropriate alternative, given the serious nature of the matter of non-compliance.

In conclusion, it is our view that the Organization has not complied with the requirements of the Act in that it has issued receipts for gifts or donations otherwise than in accordance with the Act and the Regulations or that contains false information.

5. Failure to Meet Disbursement Quota

In order to maintain its status as a charitable organization within the meaning of paragraph 149.1(2)(b) of the Act, a registered charity must, in any taxation year, expend amounts that are equal to at least 80% of the aggregate amounts for which it issued donation receipts in its immediately preceding taxation year. A charity is allowed by virtue of 149.1(20) of the ITA to offset any shortfalls in its disbursement quota by applying any excesses in its disbursement quota from its immediately preceding taxation year and 5 or less of its immediately subsequent taxation years.

In considering the application of expenditures used to meet the disbursement quota a charity must ensure that it is expensed directly on charitable activities and/or programs. This would include such payments as salaries to persons performing duties directly related to a charitable program, but would not include amounts paid for purely administrative expenses such as fundraising costs, legal or accounting fees and the like.

Based on our findings, the Organization has failed to satisfy its disbursement quota requirement for the fiscal periods ending June 30, 2006, June 30, 2007 and December 31, 2007. As such, the audit noted a disbursement quota shortfall of nearly \$3.5 million.

The Charity's Options:

a) No Response

You may choose not to respond. In that case, the A/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 in the manner described in subsection 168(1) of the Act.

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 A/Director General of the Charities Directorate will decide on the appropriate course of action, which may include:

- no compliance action necessary;
- the issuance of an educational letter;
- resolving these issues through the implementation of a Compliance Agreement; or
- the Minister giving notice of its intention to revoke the registration of the Charity by issuing a Notice of Intention in the manner described in subsection 168(1) of the Act.

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 contact the undersigned at the numbers indicated below.

Sincerely,

Katie Spoelstra
Audit Division
Kitchener Tax Services Office
166 Frederick Street
Kitchener, Ontario N2G 4N1



Internet: www.cra-arc.gc.ca

Enclosure: Appendix A

Pediatric AIDS Canada (the Organization)

DETAILS RELATED TO THE AUDIT

The following presents details and support of the position expressed in our letter that the Organization is non-compliant in the following areas:

1. Failure to Devote all of its Resources to its Charitable Purposes.
2. Failure to Maintain Adequate Books and Records.
3. Failure to File an Information Return as Required by the Act.
4. Failure to Issue receipts in Accordance with the Income Tax Act.
5. Failure to Satisfy the Disbursement Quota Requirement.

The Organization was previously audited for the 1995 to 1999 fiscal periods ending. As a condition of maintaining its continued registration, the Organization agreed to "fully abide by the terms set out in the press statement and agrees that, if asked by a third party, it will acknowledge that the facts in the press statement are true."

1. Failure to Devote all of its Resources to its Charitable Purposes

It is our view, based on our audit, that the Organization does not operate for wholly charitable purposes and the activities it undertakes on a day-to-day basis do not support its charitable purposes in a manner consistent with charitable law. In fact, the evidence on the file, as outlined below, demonstrates a preponderance of effort and resources devoted to non-charitable activities. The Organization has devoted a substantial portion of its efforts and resources to fundraising and to participating in an international donation arrangement with a comparatively minor portion of its resources devoted to its registered purpose.

Fundraising Activities

The Organization receives and devotes a substantial portion of its actual cash contributions to fundraising. The Organization has employed the professional fundraising services of Xentel DM Incorporated, Fundraising Initiatives Inc. and Blakely & Associates to raise funds for the Organization and compensates each based on an agreed rate per hour or per presentation. During the audit period, the Charity has received and receipted over \$4.6 million in third party fundraising income and has paid over \$2.8¹ million, or nearly 61% of total fundraising revenues, for these telemarketing services.

In reviewing the Organization's records, it has reduced its total party fundraising expenses by approximately 30%. The Organization recorded this reduction under the heading "Education and Advocacy" and reported this amount as charitable expenditures on the annual information returns filed. The Organization's rationale for reducing gross fundraising expenses is a belief that a portion of the scripts used to solicit funds contained information

¹ Based on summation of lines 5450 and 5460 of the Registered Charity Information Returns filed

about the Organization's purpose and that it had always reported its fundraising expenses this way.

The CRA's position is, as outlined in our publication "Completing the Registered Charity Information Return – T4033B", total fundraising costs are the total expenses a registered charity pays out for fundraising activities whether carried out by the charity or by contracted third parties. Our position is expanded further to consider the purpose behind the expenditure when determining whether the expenditure is a qualifying expenditure for purposes of the disbursement quota. It is our position the third party fundraisers were engaged to solely solicit funds and accordingly, all amounts paid to the third party fundraisers should have been reported as fundraising expenditures only.

Our previous audit revealed the Organization reported most of its fundraising expenses as charitable expenditures. Following this audit, the Organization issued a press release on September 5, 2000 stating that the CRA found that the Organization's *"fundraising costs were unacceptably high; that the distribution of pamphlets by [the Organization] mainly to donors did not constitute a charitable activity, but rather an attempt to solicit donations"*. In the press release, the Organization stated that it *"terminated all its contracts with professional fundraisers and adopted an internal code of conduct whereas, inter alia, no more will be spent on administration and fund-raising to ensure effective management and resource development. [The Organization] will also advise [the CRA] within 14 days of the signature of any future agreements with professional fundraisers, and will provide it within the same delay with copies of such agreements and agree to their public release"*.

Our current audit revealed the Organization failed to abide by the terms of its agreement with the CRA, has continued to engage third party fundraisers to solicit donations on behalf of the Organization, that a substantial portion of the Organization's resources are devoted to compensating these fundraisers and that it continues to allocate a portion of its fundraising expenses to charitable activities.

It is our view that by pursuing this non-charitable purpose, the Organization 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 Pediatric AIDS Canada.

Gift-in-Kind Shipments

The Organization also reports a significant amount of donated goods (i.e., pharmaceuticals) being distributed by the Organization internationally as part of its own charitable programs. During the audit period, the Organization has reported it has received and distributed over \$15.5 million of goods and has paid \$877,000 to Lifesgood Inc. to allegedly source and deliver these goods. The Organization purportedly values these goods using the Ontario Drug Benefit Formulary (ODBF) or the US Red Book. There are legitimate concerns the Organization has entered into this donation arrangement in an attempt to conceal its non-charitable activities, i.e. fundraising, and to falsely inflate its charitable activities. We provide the following findings to support our concerns:

Ownership of Goods:

The Organization represents that it receives goods from Lifesgood Inc., and that it pays Lifesgood Inc. a fee to procure, handle and ship the goods to the Organization's partner organizations in Africa. Our audit has been unable to confirm the Organization obtained legal title to or beneficial ownership of the goods Lifesgood Inc. allegedly procures for it. In general, ownership of property would also involve rights and obligations associated with that ownership. The documentation provided during the course of our audit does not support that Lifesgood Inc. or the previous "owners" of the pharmaceuticals relinquished ownership of the goods. The Organization did not receive copies of invoices from the original supplier of the pharmaceuticals nor did the Organization acquire or obtain documentation associated with the manufacturing of the pharmaceuticals such as certificates of analysis, certificates of pharmaceutical product, certificates of use, Good Manufacturing Practice documentation and/or quality control certificates. Throughout the audit, the Organization stated that these documents were not available to them. It is our presumption, that if the goods were in fact donated to or otherwise acquired by the Organization, this documentation would have been made available at the time the goods were gifted to or purchased by the Organization.

Although the Organization has agreed to pay a nominal fee to Lifesgood Inc. for the goods, it seems unlikely that paying such a cost would equate with the Organization becoming the owner of the goods. Especially since the reported fair market value was reportedly much greater than the amount paid to procure the goods. The Organization also does not appear to have any of the obligations associated with shipping the goods; these costs were purportedly the responsibility of Lifesgood Inc. and the recipient agencies.

Supervision, Direction and Control:

The Organization has not exhibited its direction and control over the international shipments nor has it demonstrated how the shipments were in furtherance of its own registered charitable objects. Our review has found that the Organization does not have legal title to, or beneficial ownership of, the goods it reports as having received, nor has the Organization shown that it had direction and control over the shipments. As a result, the Organization has not shown that through its programs and arrangements for the undertaking of activities, it devotes all of its resources to its own charitable activities.

The Organization's documentation provided in support of its activities overseas fail to prove the Organization's active and on-going direction and control of its programs overseas. The audit was unable to reveal the criteria utilized by the Organization to identify and select qualified and competent organizations to work with; the criteria employed to determine which entities would receive goods, the type of goods to be received and in what quantities; the directions provided to Lifesgood Inc. or any other agents for shipping, storage and distribution of the goods; or any periodic reports received from Lifesgood Inc. or any other agents supporting its on-going activities undertaken on behalf of the Organization. The shipments were turned over to the recipient agencies upon arrival at their destination with no further input or direction from the Organization. The Organization also did not receive reports from the recipient agencies that would indicate the recipient agencies were reporting to the Organization about the progression or completion of the

Organization's charitable programs. As such, we are unable to assess whether the distribution of the pharmaceuticals were undertaken on behalf of the Organization or were those of the original suppliers of the pharmaceuticals. Furthermore, we are unable to assess the Organization's due diligence in establishing that the goods were in line with the Organization's registered objects or were goods that were used in charitable programs.

Valuation of Goods

Further, if the Organization owned the goods, the Organization would have to ensure the goods were recorded and reported at their fair market value. The onus is on the Organization to show the value assigned to goods is reflective of the fair market value. Each registered charity is responsible for the accurate reporting of any gift-in-kind it receives, regardless of whether an official donation receipt is issued or not. It is our position the factual fair market value of the pharmaceutical goods would be no more than the actual cost paid to Lifesgood Inc., if the Organization was able to satisfy that it obtained legal title or beneficial ownership of the goods.

We have concerns with the valuation methodology used by the Organization. According to [REDACTED], the "donated" pharmaceutical goods from Lifesgood Inc. were valued based on the Ontario Drugs Benefits Formulary (ODBF). If the goods were not listed on the ODBF, the Organization used the Red Book value (from the United States). The Organization failed to provide the documentation it maintained or relied upon to support the use of these valuation methods despite our numerous requests starting in December 2008 and throughout the audit.

We recognize that appraisals are not required under the Act or its Regulations; however, it is our view that the onus remains with the charity to ensure the value assigned to non-cash gifts received is reflective of the factual fair market value of the goods being received. For property with a value in excess of \$1,000, we strongly recommend that the property be appraised by an independent third party; an independent party is one who is not affiliated with the charity or the originator of the property. The person determining the fair market value of the item should be competent and qualified to evaluate the particular property being donated, as well as be knowledgeable about the marketplace for the specific property. They should be knowledgeable about the principles, theories, and procedures of the applicable valuation discipline and follow the *Uniform Standards of Professional Appraisal Practice* or the standards of the profession.

Given that the Organization has not sufficiently demonstrated that it had ownership of the goods, the valuation of these goods is considered unnecessary and was undertaken to artificially inflate the Organization's total income and charitable expenditures. If the Organization did acquire legal title to or beneficial ownership of the goods, we fail to understand why the Organization did not use the actual amount paid to Lifesgood Inc. to procure the goods.

Conclusion

It is our position the Organization has not demonstrated the international activities it has reported were programs executed and controlled by the Organization. Further, the

Organization has failed to demonstrate the goods it represents it has received and distributed have actually been received and distributed, particularly in the amounts represented. As such, we are not prepared to recognize the amounts reported as pharmaceutical distributions as expenditures incurred for charitable purposes.

The pharmaceutical distributions represent approximately 65-80% of the Organization's reported revenue and 83 to 91% of the Organization's reported expenditures. As per above, the Organization devotes a substantial portion of its total tax-receipted fundraising income to fundraising expenditures. By reporting the pharmaceutical distributions as charitable expenditures, the Organization is able to report that it devoted, on average, 14% to fundraising and administrative expenses and thereby meets its annual disbursement quota. However, when the pharmaceutical distributions, and the misallocated fundraising expenses, are removed from the amounts reported as charitable expenditures, the Organization has devoted, on average, 19% to charitable activities. In this regard, the Organization is not devoting all its resources to charitable activities.

It is our view that by pursuing these non-charitable purposes, the Organization 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 Pediatric AIDS Canada.

Gifts to Non-Qualified Donees

The Organization's financial statements show that it made a "*non-interest bearing*" loan with "*no fixed terms of repayment*" towards "*the start-up cost*" of the American Foundation for Children with AIDS (AFCA) totalling \$119,353 in fiscal periods ending June 30, 2005 and June 30, 2006. This loan was made without any written agreements and/or contracts. In fiscal period ending December 31, 2007, this "loan" was changed to a "pledge". The Organization stated it agreed to forgive the loan in order for AFCA remove the "liability" off its books so it could apply for government funding.

It is our position that this transaction (original loan) and the transactions that follow (loan forgiveness, changing loan to pledge) constitute a gift to a non-qualified donee. The Organization has presented no evidence to show the "loan" or "pledge" was in furtherance of the Organization's own charitable activities nor does it appear to have been made for investment purposes. Further, it appears there were no legitimate "loan" conditions as the agreement shows the repayment terms "*as able*" indicating the Organization had no direction or control over the use of the funds or the collection of these funds when the "loan" was due.

Pursuant to paragraph 168(1)(b) of the Act, the Minister may give notice to a registered charity that he proposes to revoke its registration where a registered charity ceases to comply with the requirements of the Act for its registration as such. For this reason, it appears to us that there are grounds for revocation of the charitable status of Pediatric AIDS Canada.

2. Failure to Maintain Adequate Books and Records

The audit found that the Organization failed to maintain adequate books and records to support the activities and income and expenses it reported on its Registered Charity Information Return (T3010A).

Fundraising

The Organization uses at least three methods of third party fundraising in the audit period. The account names used in QuickBooks and in the trial balance are named (and not numbered) in such a manner that we are unable to identify the respective revenues and expenditures for each method of fundraising used. As such, we could verify the amounts reported on the T3010A were complete.

Gifts in Kind

As per above, the supporting records provided to substantiate the Organization's activities were incomplete and inadequate:

- The Organization has not shown that it had legal title to, or beneficial ownership of the goods it purported to have received, nor has the Organization shown how the goods were valued.
- The Organization has not provided adequate documentation regarding how the Organization selected intermediaries and assessed their competence to carry out charitable programs on its behalf.
- The Organization has not provided adequate documentation on how it directed and controlled the distribution of goods to beneficiaries.

General Books and Records

Our review of the Organization's overall books and records noted the following concerns:

- The record keeping system relating to the general expenses were such that we were unable to trace the expenses from the source invoice to the general ledger and vice versa. For example, the invoices did not reference the respective Quick Books account(s) and/or or journal entry number.
- The account names per QuickBooks were such that it was difficult to reconcile the Quick Book accounts to the trial balance and financial statements accounts.
- The Organization does not document and/or follow many of its policies and procedures. Additionally, there appears to be limited internal control regarding its financial reporting processes (e.g. expenditure limits, credit card use & reimbursements, etc). This is confirmed via the Organization's own investigation in June 2009 in which it *"identified numerous deficiencies and practices not in accordance with the stands set forth by the PAC board"*. The investigation *"led to the termination of the entire management team in August of 2009"*.

Donor Database

In the audit period, the Organization uses software system entitled "Donor Quest" to record and maintain its donor database and to issue official donation receipts. This software and all the records relating to the receipting system are maintained by a third party offsite. While a copy of the donor database was provide electronically, we were not given access to test the system's compliance with Regulation 3501. Furthermore, our queries regarding the system and/or software could not be answered by any of the Organization's staff. The Organization has little to no control over the database or the donation receipting system in general. The Organization relies solely the third party supplier to receive the donor information from Xentel, etc., and to input, process, amend and analyse the data. The printing of the official donation receipts were also done offsite and the Organization was not involved in this process either. The security and safeguarding of the donor database system and of the official donation receipts were unknown to the Organization. Additionally, we found that the Organization does not have a written agreement and/or contract with the third party indicating a lack of internal controls and due diligence.

Additionally, the donor database information provided did not reconcile to T3010 annual information returns filed. The variances are noted below:

	31-Dec-07	30-Jun-07	30-Jun-06	Total
Amounts/Donor Quest	1,334,676.63	1,916,200.73	,944,516.61	5,195,393.97
Amounts/T3010 (line 4500)	1,224,926.00	1,878,671.00	,966,171.00	5,069,768.00
Variance	109,750.63	37,529.73	- 21,654.39	125,625.97

The Organization was provided with numerous opportunities to explain the variance but failed to do so. On November 17, 2009, the new management team provided us with a summary reconciliation they completed after their analysis of the current system.

	31-Dec-07	30-Jun-07	30-Jun-06	Total
Amounts/FRA summary sheets	1,256,454.63	1,894,561.73	1,959,551.61	5,110,567.97
Amounts/T3010 (line 4500)	1,224,926.00	1,878,671.00	1,966,171.00	5,069,768.00
Variance	31,528.63	15,890.73	- 6,619.39	40,799.97

The subsequent reconciliation shows a decrease in the variance between the donor database and the T3010; however, the material variances are still unexplained. The Organization acknowledges deficiencies in the old software system and states it purchased and implemented a new software system that would provide a *"comprehensive reporting and tracking system"*.

3. Failure to File an Information Return as Required by the Act:

The Registered Charity Information Returns (T3010A), for fiscal periods ending June 30, 2006, June 30, 2007 and December 31, 2007 filed by the Organization were inaccurately completed.

Gifts in Kind

The Organization overstated its charitable income and expenditures by including the alleged value of the pharmaceuticals received via Lifesgood Inc. Per above, the Organization has not demonstrated that it actually had legal title to or beneficial ownership of the goods reported to have been received by it and that if it had ownership of the goods, has not demonstrated that it directed or controlled the distribution of these goods as part of the Organization's own charitable activities. Additionally, we do not believe the value assigned to the pharmaceuticals is reflective of the pharmaceuticals factual fair market value.

Fundraising

The Organization also overstated its charitable expenditures by including a portion of the fundraising fees paid to its third party fundraisers. These fees include those paid to Xentel DM, Fundraising Initiatives, and Blakely & Associates. The CRA's position is, as outlined in our publication "Completing the Registered Charity Information Return - T4033A", total fundraising costs are the total expenses a registered charity pays out for fundraising activities whether carried out by the charity or by contracted third parties. Our position is expanded further to consider the purpose behind the expenditure when determining whether the expenditure is a qualifying expenditure for purposes of the disbursement quota. It is our position the third party fundraisers were engaged to solely solicit funds and accordingly, all amounts paid to the third party fundraisers should have been reported as fundraising expenditures only.

AFCA Loan

As noted above, the Organization loaned monies to AFCA, which it wrote off in fiscal period ending December 31, 2007. The \$114,380 transactions were reported on lines 4510, 4920 and 5040 of the T3010A return. Based on our review, it appears the Organization re-classified the "loan receivable" to "pledge receivable" and moved it from one asset account to another as noted in its financial statements. Pledge donations were never received so no attempts were made to collect the debt. As such, the income should not have been reported at line 4510 (income from other registered charities) and the expenditure should not have been claimed on lines 4920 and 5010.

Under paragraph 168(1)(e) of the Act, the Minister may, by registered mail, give notice to the charity that he proposes to revoke its registration because it fails to comply with or contravenes section 230 of the Act dealing with books and records. For this reason, it appears to us that there are grounds for revocation of the charitable status of Pediatric AIDS Canada.

4. Failure to Issue Receipts in Accordance with the Act

The official donation receipts issued by the Organization did not comply with the requirements of Regulation 3501 of the Act and IT-110R3 entitled, "*Gifts and Official Donation Receipts*" as follows:

- The Organization's address printed on the receipts is outdated;
- We were unable to determine whether all the numbers in the series of receipts were accounted for;
- The Organization did not retain at least one exact copy of the official income tax receipt (in paper or electronic format);
- Official receipts containing a facsimile signature were not pre-numbered by a printing press or numbering machine;
- We were unable to assess whether unused official receipts with an attached facsimile signature are kept in a secure location or locked up during off hours and not accessible to anyone not issuing receipts;
- There is no log system maintained and up to date that accounts for the number of official receipts purchased against those that are officially issued and/or voided;
- The integrity of the computer system could not be sufficiently guaranteed. We could not test whether access to the system was controlled with passwords or whether access to the network system had appropriate predefined user rights such as the right to enter date, correct data, and to print receipts;
- The system could not print out a listing of the official donation receipts issued, including the donor's name and address, the date of the donation, the receipt number, the date of the receipt, the type of the gift and the amount of the donation;
- We were unable to determine if lost receipts contained all the information plus a notation to the effect "This cancels and replaces receipts # (?)";
- Replaced receipts are not retained and we were unable to assess whether they were marked with "Cancelled"; and
- We were unable to determine if all copies of spoiled or voided receipts are marked "Cancelled".

Under paragraphs 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 its Regulations. For this reason alone, there are grounds for revocation of the charitable status of Pediatric AIDS Canada under paragraph 168(1)(d) of the Act.

5. Failure to Meet Disbursement Quota

Based on our calculations, and for the reasons described in detail above, the Organization has not met its disbursement quota for the fiscal periods ending June 30, 2006, June 30, 2007 and December 31, 2007 due to:

- Amounts reported as distributions of pharmaceuticals are not being recognized at the values provided to and used by the Organization. As discussed above, the

Organization has been unable to substantiate the factual value of the property distributed, that the goods were actually distributed and that the programs were carried on as programs of the Organization.

- Amounts reported as pharmaceutical distributions are not being recognized as charitable expenditures as the Organization has not demonstrated the international pharmaceutical distributions were programs executed and controlled by the Organization.

The audit found that the Organization consistently used the values the Organization assigned to the pharmaceuticals to record the gift of and distribution of goods received. The Organization has not shown it sought independent valuations for the goods received nor has it demonstrated it physically inspected the goods received. We are of the opinion the Organization chose to report the value of the goods provided in an endeavour to increase the amounts it reported as expenditures on charitable activities. As we discussed above, the Organization devotes a substantial amount of its tax-receipted cash donations to non-charitable activities such as fundraising and administration, and without the donations of the goods, the Organization would find it difficult to meet its annual disbursement quota.

For the goods received from Lifesgood Inc., the Organization incurred pharmaceutical acquisition costs exceeding \$877,000 yet purportedly received property valued at \$15.5 million. The non-cash gifts had little impact on the financial statements other than increasing the Organization's total income and total expenses but the true significance of the non-cash gifts was unmistakable in the Organization's classification of these gifts as charitable expenses for disbursement quota purposes. As a result of the Organization's classification of the non-cash property as charitable expenses, the Organization was able to report it had met its annual disbursement quota and was able to accrue disbursement quota excesses. Based on our calculations, the Organization has a disbursement quota shortfall of at least \$3.5 million. It is evident to CRA that the Organization's "advantage" received from receiving these goods was the disbursement quota excesses it has accrued despite devoting a major portion of the Organization's net cash to fundraising and administration expenses.

- The Organization included a portion of its third party fundraising expenses as charitable expenses.

We have calculated the Charity's cumulative disbursement quota shortfall, a product resulting from the reclassification fundraising expenses and international distribution expenses from charitable program expenses to non-charitable expenses as follows:

Re-calculation of the Disbursement Quota:				
	2006-06-30	2007-06-30	2007-12-31	Total
Tax-receipted gifts from previous fiscal period (line 4500)	\$1,768,374	\$1,966,171	\$1,878,671	
Disbursement quota requirement for fiscal period (80% of above)	1,414,699	1,572,936	1,502,936	
Total amount spent on charitable programs (line 5000) as revised by CRA audit	365,777	410,635	224,383	
Disbursement SHORTFALL	\$1,048,922	\$1,162,301	\$1,278,552	\$ 3,489,776

Our previous audit revealed cumulative disbursement shortfalls mainly as a result of the Organization reporting the expenditures it incurred for fundraising activity as charitable expenses. In the September 5, 2000 press release, the Organization agreed to *"meet or exceed the requirements for expenditures on charitable activities or gifts to qualified donees ...per subsection 149.1(1) of the Income Tax Act"*.

As per paragraph 168(1)(b) of the Act, 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, it appears to us that there are grounds for revocation of the charitable status of Pediatric AIDS Canada.

PEDIATRIC AIDS CANADA/USA

COMMENTS ON REPRESENTATIONS OF MAY 7, 2010

Failure to Devote Resources to Charitable Purposes:

The audit conducted by the Canada Revenue Agency (CRA), identified that Pediatric AIDS Canada/USA (the Organization), based on the activities of the Organization and the level of financial activity and resources devoted, is not devoting its resources to entirely charitable purposes. In our view, the Organization's original purpose, which is to support research concerning pediatric AIDS in Canada, has been sidetracked by its participation in an international donation arrangement and third party fundraising with residual funds devoted to its registered charitable purpose.

Fundraising Activities:

The CRA's audit has concluded that from July 1, 2005 to December 31, 2007, the Organization issued official donation receipts in excess of \$5.06 million, paid \$3.26 million for fundraising and administration expenses while devoting \$1.8 million to its own charitable activities.¹

Your representations disagree with our findings and state that the amounts paid "were in fact reasonable in the circumstances," yet the representations do not address our findings that the amounts paid represent a significant portion of the Organization's resources. In our view the amounts devoted to actual charitable activities is insufficient to demonstrate that the Organization devotes all of its resources to charitable activity when the vast majority of the amounts received are devoted to fundraising and administration.

Gift-in-Kind Shipments:

As described in our previous letter, our audit revealed that the Organization does not maintain the requisite level of direction and control for all goods it purportedly distributes internationally. The Organization reported \$15.5 million in "gifts" received from Lifesgood Inc. The Organization reports these "gifts" as their own activities but has not provided confirmation the goods existed in the quantities and values recorded by Lifesgood Inc. and that the goods were property of the Organization to be distributed to international entities of the Organization's own evaluation and selection. Our audit has determined that the Organization pays an amount to Lifesgood Inc. to source and deliver the goods yet we fail to recognize that the fee paid to acquire the goods, is equivalent to the value of the goods being represented. The Organization paid \$877,000 to allegedly acquire \$15.5 million in goods.

¹ Referencing the December 2008 and 2009 information returns filed by the Organization, total tax-receipted donations of over \$4.15 million and total other gifts (i.e. non-cash gifts) of over \$14.2 million have been received. The Organization allegedly received and distributed an additional \$14.9 million in non-cash goods related to the international donation arrangement, incurred \$2.9 million in fundraising expenses and administrative costs with \$490,000 devoted to the Organization's own programs.

In its reply, the Organization cites CRA policies with respect to the distribution of goods outside of the country. While we acknowledge that the CRA accepts that certain goods by their very nature can only be used for charitable activities, as described in further detail below, this does not relieve the Organization of its responsibilities. A registered charity must be able to demonstrate that it was responsible for the charitable activity itself, that the charitable activity actually occurred and that it occurred on the scale represented. It is simply not sufficient to state that millions of dollars in relief activities occurred, claiming these as charitable expenditures against the organization's disbursement quota, without sufficient proof as to ownership, values, volumes, destinations or ultimate use. Absent such documentation, the CRA has no means of determining whether the goods exist, testing what the value of the goods shipped are, or even whether the goods are, in fact, distributed for charitable activities or instead sold, disposed of or sit unused.

Per our previous letter, it is CRA's position that the Organization participates in this international donation arrangement to artificially inflate its expenditures on charitable activities and to meet its annual disbursement quota with minimal actual cash outlay. The Organization reports the "gifts" received from Lifesgood Inc. as both income and expenses against its disbursement quota. Outside of this activity, the Organization devotes a substantial amount of its tax-receipted cash donations to non-charitable activities such as fundraising and administration, and without the donations of non-cash property, the Organization would find it difficult to meet its annual disbursement quota. As reported above, the Organization received \$5.06 million in cash donations yet devoted \$3.26 million or 64% of cash donations to fundraising and administrative costs with \$1.8 million or 30% spent on charitable programs. In our view, the Organization participates in this international donation arrangement to artificially offset the disproportionate expenditures on non-qualifying expenses for disbursement quota purposes.

Direction and Control

The case law supports the position that the existence of an agency agreement alone is not sufficient; in order for an organization to show that it exercises sufficient direction and control over its resources and activities, it must evidence that it effectively implements and enforces the agreement, which the Organization was clearly unable to do.

In *The Canadian Committee for the Tel Aviv Foundation vs. Her Majesty the Queen*,² the organization under review had an agency agreement in place, but was unable to produce sufficient documentary evidence to demonstrate that the agreement was enforced and adhered to. The Canadian Federal Court of Appeal (FCA) upheld the Minister's decision to revoke the organization, based, in part, on the following areas of non-compliance:

"Under the scheme of the [*Income Tax Act*], it is open to a charity to conduct its overseas activities either using its own personnel or through an agent. However, it cannot merely be a conduit to funnel donations overseas. In this case, the Agency Agreement was ignored by the Committee, and the Minister was not satisfied that the Committee's explanations of its conduct overseas were sufficient to overcome his conclusion that the Committee had no direction and control over how funds were spent by its agent. The evidence that was provided would suggest that the Committee was merely acting as a conduit

² [2002] FCA 72

for Canadian donors to overseas donees. For example, the evidence discloses that the Committee sent the majority of the funds it raised to its agent in Israel, but provided little documentary evidence of the Committee's control over how those funds were spent." (paragraph 30)

And,

"While a charity may carry on its charitable activities through an agent, the charity must be prepared to satisfy the Minister that it is at all times both in control of its agent, and in a position to report on the agent's activities. In this case, the Minister's main reasons for revocation are that the Committee could not demonstrate, through documentary evidence, that it exercised a sufficient degree of direction of control over the use of its funds by its agent in Tel Aviv and the Committee did not keep proper books and records of activities carried on by its agent. Even though the Minister's reasons are couched in terms of non-compliance with the Agency Agreement, the requirements under the latter are, in my view, simply a means of ensuring compliance with the [*Income Tax Act*]." (paragraph 40)

In the case of *Bayit Lepletot*³, the FCA reiterated that a charity which operates via an agent must be in a position to show that its agent is actually carrying out the activities in question *on its [the Charity's] behalf*.

"It is open for [a charity] to carry on its charitable works through an agent but it must be shown that the agent is actually carrying on the charitable works. It is not sufficient to show that the agent is part of another charitable organization which carries on a charitable program. The question which remains in such a case, as it does here, is who is carrying on the charitable works. It was incumbent upon the appellant to show that they were being carried on its behalf. On the record before us it was open to Minister to conclude that it had failed to do so." (paragraph 5)

As such, the existence of an agency relationship and agreement does not suffice. Evidence demonstrating that the agent acted in accordance with the terms of the arrangement, under the charity's continuous instruction and supervision, is also necessary. In the case of the Organization, it has not provided a sufficient basis, by way of documentary evidence, to support its contention that the activities carried on by its purported agent were, in fact, its own.

Further support for this position is found in the case of *Canadian Magen David Adom for Israel v. Minister of National Revenue*⁴:

"[A] charitable organization is obliged to carry on its charitable activities itself. If it does not do so, its registration may be revoked. A charitable organization that wishes to operate in a location where it has not officers or employees must somehow act through a person in that location. That obviously could be done by establishing an agency relationship between the charity and the person. Evidence that such a relationship has been established by contract, and that the contract has been adhered to, might well be the most straightforward means of proving to the Minister that a person purporting to carry out the charitable activities of a

³ *Bayit Lepletot v. Minister of National Revenue*, [2006] FCA 128

⁴ [2002] FCA 323, at paragraph 66

charity in a particular location is in fact acting on behalf of the charity. It is possible that the same result might be achieved by other means. *However, a charity that chooses to carry out its activities in a foreign country through an agent or otherwise must be in a position to establish that any acts that purport to be those of the charity are effectively authorized, controlled and monitored by the charity*" (emphasis added).

Per the Organization's submission, it "specifically [relies] on CRA policy that where the charitable activities of an organization involve the transfer of goods outside the country, CRA will consider the transfer of property in this manner to be reasonable where the nature of the property can only be used for a charitable purpose." The Organization further contends "[t]hese goods, by their very nature, can only be used for the treatment of medical illnesses and fall squarely with CRA's policy which allows a transfer of property to a non-qualified donee without the necessity of a structured and formal arrangement" and "maintains that the valuation methodology used was appropriate in the circumstances."

Again, while the CRA acknowledges this slight relaxing of its strict requirements in certain circumstances, a charity must nonetheless be able to support the use of property purportedly received and distributed by it and the relating amounts reported as charitable expenditures. In the case of the Organization, there is no evidence in support of the status and activities of the recipient, or that the donated goods were used for charitable purposes or formed part of the Organization's own activities. A charity cannot simply forgo its responsibilities and diligence simply because of the nature of goods being distributed. In our view, the Organization has not demonstrated that it obtained title to the goods and maintained control over its resources, nor can it demonstrate the ultimate use and distribution of the goods by its agents, such that it can claim it distributed at least \$15.5 million of goods on charitable activities carried on by it. In fact, it is our view that the Organization simply pays fees to Lifesgood Inc. assuming that charitable goods are distributed such that it can claim the related expenditure.

Gifts to a Non-Qualified Donee:

Our audit revealed the Organization gave \$119,353 to the America Foundation for Children with AIDS (AFCA) in 2005 and otherwise made a gift to a non-qualified donee when the loan was re-classified to a pledge. The representations state that the Organization believes the loan will be repaid by AFCA by paying expenditures on the Organization's behalf – expenditures related to the shipping and administrative costs related to its purported shipments. Our audit failed to reveal, and no further documentation was provided, to support the Organization's submissions. Accordingly, we remain of the position that the Organization has made a gift to a non-qualified donee.

For these reasons, and those set out in our letter of February 4, 2010, we continue to be of the view that the Organization is not devoting substantially all of its resources to its own charitable activities. Under paragraph 168(1)(b) of the Act, the Minister may, by registered mail, give notice to the registered 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. It is our position that Pediatric AIDS Canada/USA has not demonstrated that it devoted all of its resources to charitable activities carried on by it. For these reasons, and for each reason alone, there are grounds to revoke the charitable status of Pediatric AIDS Canada/USA.

Disbursement Quota:

The Organization maintains that its expenditures on programs outside Canada are charitable expenditures despite a lack of evidence to demonstrate that the Organization actually received goods, how values were established, any control and direction over the use of the goods or how goods were ultimately distributed. It remains our position that amounts reported by the Organization as distributions of pharmaceuticals were not programs carried out by the Organization and were not reflective of the goods factual fair market value. Additionally, the fundraising amounts recorded by the Organization as education and advocacy expenses impact the disbursement quota, as we do not deem the expenditures to be incurred for a charitable purpose. As above, the Organization reported 30% of its third party fundraising expenses as charitable expenses, thereby overstating its true charitable expenditures.

As described in our previous letter, we remain of the view that the Organization is in a significant disbursement quota shortfall position. The legislation proposed in the 2010 Budget applies to fiscal periods ending after March 4, 2010. Therefore under paragraph 149.1(2)(b) of the Act, the Minister may, by registered mail, give notice to the registered charity that the Minister proposes to revoke its registration because it fails to meet its annual disbursement quota. It remains the CRA's position that the Organization failed to meet its annual disbursement quota and has a disbursement quota shortfall exceeding \$3.4 million. For this reason, it appears that there are grounds for revocation of the charitable status of Pediatric AIDS Canada/USA.

Other Issues:

Our position remains unchanged with regard to the remaining areas of non-compliance identified in our February 4, 2010 letter. No further information has been provided by the Organization and the representations submitted do not alter our findings. It is our position the Organization failed to issue receipts in accordance with the Act, filed an inaccurate Registered Charity Information Return in each of the fiscal periods ending 2005 to 2007 and failed to maintain adequate documentation to support the receipt and distribution of non-cash property overseas.

Under paragraphs 168(1)(c), (d) and (e) of the Act, the Minister may, by registered mail, give notice to the registered charity that the Minister proposes to revoke its registration because it fails to file an information return as and when required, fails to issue official donation receipts in accordance with the Act and failed to maintain adequate records. It remains the CRA's position that the Organization failed to file an information return as and when required, failed to issue receipts in accordance with the Act and failed to maintain adequate records. For this reason, it appears to us that there are grounds for revocation of the charitable status of Pediatric AIDS Canada/USA.

Section 149.1: [Charities]

149.1(2) Revocation of registration of charitable organization

The Minister may, in the manner described in section 168, revoke the registration of a charitable organization for any reason described in subsection 168(1) or where the organization

- (a) carries on a business that is not a related business of that charity; or
- (b) fails to expend in any taxation year, on charitable activities carried on by it and by way of gifts made by it to qualified donees, amounts the total of which is at least equal to the organization's disbursement quota for that year.

149.1(3) Revocation of registration of public foundation

The Minister may, in the manner described in section 168, revoke the registration of a public foundation for any reason described in subsection 168(1) or where the foundation

- (a) carries on a business that is not a related business of that charity;
- (b) fails to expend in any taxation year, on charitable activities carried on by it and by way of gifts made by it to qualified donees, amounts the total of which is at least equal to the foundation's disbursement quota for that year;
- (c) since June 1, 1950, acquired control of any corporation;
- (d) since June 1, 1950, incurred debts, other than debts for current operating expenses, debts incurred in connection with the purchase and sale of investments and debts incurred in the course of administering charitable activities; or
- (e) at any time within the 24 month period preceding the day on which notice is given to the foundation by the minister pursuant to subsection 168(1) and at a time when the foundation was a private foundation, took any action or failed to expend amounts such that the Minister was entitled, pursuant to subsection (4), to revoke its registration as a private foundation.

149.1(4) Revocation of registration of private foundation

The Minister may, in the manner described in section 168, revoke the registration of a private foundation for any reason described in subsection 168(1) or where the foundation

- (a) carries on any business;
- (b) fails to expend in any taxation year, on charitable activities carried on by it and by way of gifts made by it to qualified donees, amounts the total of which is at least equal to the foundation's disbursement quota for that year;
- (c) since June 1, 1950, acquired control of any corporation; or
- (d) since June 1, 1950, incurred debts, other than debts for current operating expenses, debts incurred in connection with the purchase and sale of investments and debts incurred in the course of administering charitable activities.

149.1(4.1) Revocation of registration of registered charity

The Minister may, in the manner described in section 168, revoke the registration

- (a) of a registered charity, if the registered charity has made a gift to another registered charity and it can reasonably be considered that one of the main purposes of making the gift was to unduly delay the expenditure of amounts on charitable activities;
- (b) of the other charity referred to in paragraph (a), if it can reasonably be considered that, by accepting the gift, it acted in concert with the registered charity to which paragraph (a) applies; and
- (c) of a registered charity, if a false statement, within the meaning assigned by subsection 163.2(1), was made in circumstances amounting to culpable conduct, within the meaning assigned by that subsection, in the furnishing of information for the purpose of obtaining registration of the charity.

Section 168: Notice of intention to revoke registration

168(1) Where a registered charity or a registered Canadian amateur athletic association

- (a) applies to the Minister in writing for revocation of its registration,
 - (b) ceases to comply with the requirements of this Act for its registration as such,
 - (c) fails to file an information return as and when required under this Act or a regulation,
 - (d) issues a receipt for a gift or donation otherwise than in accordance with this Act and the regulations or that contains false information,
 - (e) fails to comply with or contravenes any of sections 230 to 231.5, or
 - (f) in the case of a registered Canadian amateur athletic association, accepts a gift or donation the granting of which was expressly or impliedly conditional on the association making a gift or donation to another person, club, society or association,
- the Minister may, by registered mail, give notice to the registered charity or registered Canadian amateur athletic association that the Minister proposes to revoke its registration.

168(2) Revocation of Registration

Where the Minister gives notice under subsection (1) to a registered charity or to a registered Canadian amateur athletic association,

- (a) if the charity or association has applied to the Minister in writing for the revocation of its registration, the Minister shall, forthwith after the mailing of the notice, publish a copy of the notice in the *Canada Gazette*, and
- (b) in any other case, the Minister may, after the expiration of 30 days from the day of mailing of the notice, or after the expiration of such extended period from the day of mailing of the notice as the Federal Court of Appeal or a judge of that Court, on application made at any time before the determination of any appeal pursuant to subsection 172(3) from the giving of the notice, may fix or allow, publish a copy of the notice in the *Canada Gazette*,

and on that publication of a copy of the notice, the registration of the charity or association is revoked.

168(4) Objection to proposal or designation

A person that is or was registered as a registered charity or is an applicant for registration as a registered charity that objects to a notice under subsection (1) or any of subsections 149.1(2) to (4.1), (6.3), (22) and (23) may, on or before the day that is 90 days after the day on which the notice was mailed, serve on the Minister a written notice of objection in the manner authorized by the Minister, setting out the reasons for the objection and all the relevant facts, and the provisions of subsections 165(1), (1.1) and (3) to (7) and sections 166, 166.1 and 166.2 apply, with any modifications that the circumstances require, as if the notice were a notice of assessment made under section 152.

Section 172: Appeal from refusal to register, revocation of registration, etc.**172(3) Appeal from refusal to register, revocation of registration, etc.**

Where the Minister

- (a) refuses to register an applicant for registration as a Canadian amateur athletic association,
- (a.1) confirms a proposal, decision or designation in respect of which a notice was issued by the Minister to a person that is or was registered as a registered charity, or is an applicant for registration as a registered charity, under any of subsections 149.1(2) to (4.1), (6.3), (22) and (23) and 168(1), or does not confirm or vacate that proposal, decision or designation within 90 days after service of a notice of objection by the person under subsection 168(4) in respect of that proposal, decision or designation,
- (b) refuses to accept for registration for the purposes of this Act any retirement savings plan,
- (c) refuses to accept for registration for the purposes of this Act any profit sharing plan or revokes the registration of such a plan,
- (d) refuses to issue a certificate of exemption under subsection 212(14),
- (e) refuses to accept for registration for the purposes of this Act an education savings plan,
- (e.1) sends notice under subsection 146.1(12.1) to a promoter that the Minister proposes to revoke the registration of an education savings plan,
- (f) refuses to register for the purposes of this Act any pension plan or gives notice under subsection 147.1(11) to the administrator of a registered pension plan that the Minister proposes to revoke its registration,
- (f.1) refuses to accept an amendment to a registered pension plan, or
- (g) refuses to accept for registration for the purposes of this Act any retirement income fund, the applicant or the organization, foundation, association or registered charity, as the case may be, in a case described in paragraph (a) or (a.1), the applicant in a case described in paragraph (b), (d), (e) or (g), a trustee under the plan or an employer of employees who are beneficiaries under the plan, in a case described in paragraph (c), the promoter in a case described in paragraph (e.1), or the administrator of the plan or an employer who participates in the plan, in a case described in paragraph (f) or (f.1), may appeal from the Minister's decision, or from the giving of the notice by the Minister, to the Federal Court of Appeal.

Section 180: Appeals to Federal Court of Appeal

180(1) Appeals to Federal Court of Appeal

An appeal to the Federal Court of Appeal pursuant to subsection 172(3) may be instituted by filing a notice of appeal in the Court within 30 days from

- (a) the day on which the Minister notifies a person under subsection 165(3) of the Minister's action in respect of a notice of objection filed under subsection 168(4),
- (b) the mailing of notice to a registered Canadian amateur athletic association under subsection 168(1),
- (c) the mailing of notice to the administrator of the registered pension plan under subsection 147.1(11),
- (c.1) the sending of a notice to a promoter of a registered education savings plan under subsection 146.1(12.1), or
- (c) the time the decision of the Minister to refuse the application for acceptance of the amendment to the registered pension plan was mailed, or otherwise communicated in writing, by the Minister to any person,

as the case may be, or within such further time as the Court of Appeal or a judge thereof may, either before or after the expiration of those 30 days, fix or allow.

Section 188: Revocation tax

188(1) Deemed year-end on notice of revocation

If on a particular day the Minister issues a notice of intention to revoke the registration of a taxpayer as a registered charity under any of subsections 149.1(2) to (4.1) and 168(1) or it is determined, under subsection 7(1) of the Charities Registration (Security Information) Act, that a certificate served in respect of the charity under subsection 5(1) of that Act is reasonable on the basis of information and evidence available,

- (a) the taxation year of the charity that would otherwise have included that day is deemed to end at the end of that day;
- (b) a new taxation year of the charity is deemed to begin immediately after that day; and
- (c) for the purpose of determining the charity's fiscal period after that day, the charity is deemed not to have established a fiscal period before that day.

188(1.1) Revocation tax

A charity referred to in subsection (1) is liable to a tax, for its taxation year that is deemed to have ended, equal to the amount determined by the formula

$$A - B$$

where

A is the total of all amounts, each of which is

- (a) the fair market value of a property of the charity at the end of that taxation year,
- (b) the amount of an appropriation (within the meaning assigned by subsection (2) in respect of a property transferred to another person in the 120-day period that ended at the end of that taxation year, or
- (d) the income of the charity for its winding-up period, including gifts received by the charity in that period from any source and any income that would be computed under section 3 as if that period were a taxation year; and

B is the total of all amounts (other than the amount of an expenditure in respect of which a deduction has been made in computing income for the winding-up period under paragraph (c) of the description of A, each of which is

- (a) a debt of the charity that is outstanding at the end of that taxation year,
- (b) an expenditure made by the charity during the winding-up period on charitable activities carried on by it, or
- (c) an amount in respect of a property transferred by the charity during the winding-up period and not later than the latter of one year from the end of the taxation year and the day, if any, referred to in paragraph (1.2)(c) to a person that was at the time of the transfer an eligible donee in respect of the charity, equal to the amount, if any, by which the fair market value of the property, when transferred, exceeds the consideration given by the person for the transfer.

188(1.2) Winding-up period

In this Part, the winding-up period of a charity is the period, that begins immediately after the day on which the Minister issues a notice of intention to revoke the registration of a taxpayer as a registered charity under any of subsections 149.1(2) to (4.1) and 168(1) (or, if earlier, immediately after the day on which it is determined, under subsection 7(1) of the Charities Registration (Security Information) Act, that a certificate served in respect of the charity under subsection 5(1) of that Act is reasonable on the basis of information and evidence available), and that ends on the day that is the latest of

- (a) the day, if any, on which the charity files a return under subsection 189(6.1) for the taxation year deemed by subsection (1) to have ended, but not later than the day on which the charity is required to file that return,
- (b) the day on which the Minister last issues a notice of assessment of tax payable under subsection (1.1) for that taxation year by the charity, and
- (c) if the charity has filed a notice of objection or appeal in respect of that assessment, the day on which the Minister may take a collection action under section 225.1 in respect of that tax payable.

188(1.3) Eligible donee

In this Part, an eligible donee in respect of a particular charity is a registered charity

- (a) of which more than 50% of the members of the board of directors or trustees of the registered charity deal at arm's length with each member of the board of directors or trustees of the particular charity;
- (b) that is not the subject of a suspension under subsection 188.2(1);
- (c) that has no unpaid liabilities under this Act or under the Excise Tax Act;
- (d) that has filed all information returns required by subsection 149.1(14); and
- (e) that is not the subject of a certificate under subsection 5(1) of the Charities Registration (Security Information) Act or, if it is the subject of such a certificate, the certificate has been determined under subsection 7(1) of that Act not to be reasonable.

188(2) Shared liability — revocation tax

A person who, after the time that is 120 days before the end of the taxation year of a charity that is deemed by subsection (1) to have ended, receives property from the charity, is jointly and severally, or solidarily, liable with the charity for the tax payable under subsection (1.1) by the charity for that taxation year for an amount not exceeding the total of all appropriations, each of which is the amount by which the fair market value of such a property at the time it was so received by the person exceeds the consideration given by the person in respect of the property.

188(2.1) Non-application of revocation tax

Subsections (1) and (1.1) do not apply to a charity in respect of a notice of intention to revoke given under any of subsections 149.1(2) to (4.1) and 168(1) if the Minister abandons the intention and so notifies the charity or if

- (a) within the one-year period that begins immediately after the taxation year of the charity otherwise deemed by subsection (1) to have ended, the Minister has registered the charity as a charitable organization, private foundation or public foundation; and
- (b) the charity has, before the time that the Minister has so registered the charity,
 - (i) paid all amounts, each of which is an amount for which the charity is liable under this Act (other than subsection (1.1)) or the Excise Tax Act in respect of taxes, penalties and interest, and
 - (ii) filed all information returns required by or under this Act to be filed on or before that time.

188(3) Transfer of property tax

Where, as a result of a transaction or series of transactions, property owned by a registered charity that is a charitable foundation and having a net value greater than 50% of the net asset amount of the charitable foundation immediately before the transaction or series of transactions, as the case may be, is transferred before the end of a taxation year, directly or indirectly, to one or more charitable organizations and it may reasonably be considered that the main purpose of the transfer is to effect a reduction in the disbursement quota of the foundation, the foundation shall pay a tax under this Part for the year equal to the amount by which 25% of the net value of that property determined as of the day of its transfer exceeds the total of all amounts each of which is its tax payable under this subsection for a preceding taxation year in respect of the transaction or series of transactions.

188(3.1) Non-application of subsection (3)

Subsection (3) does not apply to a transfer that is a gift to which subsection 188.1(11) applies.

188(4) Idem

Where property has been transferred to a charitable organization in circumstances described in subsection (3) and it may reasonably be considered that the organization acted in concert with a charitable foundation for the purpose of reducing the disbursement quota of the foundation, the organization is jointly and severally liable with the foundation for the tax imposed on the foundation by that subsection in an amount not exceeding the net value of the property.

188(5) Definitions

In this section,

"net asset amount"

"net asset amount" of a charitable foundation at any time means the amount determined by the formula

$A - B$

where

A is the fair market value at that time of all the property owned by the foundation at that time, and

B is the total of all amounts each of which is the amount of a debt owing by or any other obligation of the foundation at that time;

"net value"

"net value" of property owned by a charitable foundation, as of the day of its transfer, means the amount determined by the formula

$A - B$

where

A is the fair market value of the property on that day, and

B is the amount of any consideration given to the foundation for the transfer.

Section 189**189(6) Taxpayer to file return and pay tax**

Every taxpayer who is liable to pay tax under this Part (except a charity that is liable to pay tax under section 188(1)) for a taxation year shall, on or before the day on or before which the taxpayer is, or would be if tax were payable by the taxpayer under Part I for the year, required to file a return of income or an information return under Part I for the year,

- (a) file with the Minister a return for the year in prescribed form and containing prescribed information, without notice or demand therefor;
- (b) estimate in the return the amount of tax payable by the taxpayer under this Part for the year; and
- (c) pay to the Receiver General the amount of tax payable by the taxpayer under this Part for the year.

189(6.1) Revoked charity to file returns

Every taxpayer who is liable to pay tax under subsection 188(1.1) for a taxation year shall, on or before the day that is one year from the end of the taxation year, and without notice or demand,

- (a) file with the Minister
 - (i) a return for the taxation year, in prescribed form and containing prescribed information, and
 - (ii) both an information return and a public information return for the taxation year, each in the form prescribed for the purpose of subsection 149.1(14); and
- (b) estimate in the return referred to in subparagraph (a)(i) the amount of tax payable by the taxpayer under subsection 188(1.1) for the taxation year; and
- (c) pay to the Receiver General the amount of tax payable by the taxpayer under subsection 188(1.1) for the taxation year.

189 (6.2) Reduction of revocation tax liability

If the Minister has, during the one-year period beginning immediately after the end of a taxation year of a person, assessed the person in respect of the person's liability for tax under subsection 188(1.1) for that taxation year, has not after that period reassessed the tax liability of the person, and that liability exceeds \$1,000, that liability is, at any particular time, reduced by the total of

- (a) the amount, if any, by which
 - (i) the total of all amounts, each of which is an expenditure made by the charity, on charitable activities carried on by it, before the particular time and during the period (referred to in this subsection as the "post-assessment period") that begins immediately after a notice of the latest such assessment was mailed and ends at the end of the one-year period exceeds
 - (ii) the income of the charity for the post-assessment period, including gifts received by the charity in that period from any source and any income that would be computed under section 3 if that period were a taxation year, and
- (b) all amounts, each of which is an amount, in respect of a property transferred by the charity before the particular time and during the post-assessment period to a person that was at the time of the transfer an eligible donee in respect of the charity, equal to the amount, if any, by which the fair market value of the property, when transferred, exceeds the consideration given by the person for the transfer.

189(6.3) Reduction of liability for penalties

If the Minister has assessed a registered charity in respect of the charity's liability for penalties under section 188.1 for a taxation year, and that liability exceeds \$1,000, that liability is, at any particular time, reduced by the total of all amounts, each of which is an amount, in respect of a property transferred by the charity after the day on which the Minister first assessed that liability and before the particular time to a person that was at the time of the transfer an eligible donee in respect of the charity, equal to the amount, if any, by which the fair market value of the property, when transferred, exceeds the total of

- (a) the consideration given by the person for the transfer, and
- (b) the part of the amount in respect of the transfer that has resulted in a reduction of an amount otherwise payable under subsection 188(1.1).

189 (7) Minister may assess

Without limiting the authority of the Minister to revoke the registration of a registered charity, the Minister may also at any time assess a taxpayer in respect of any amount that a taxpayer is liable to pay under this Part.