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RE: Strengthening Canada's AML and Anti-Terrorist Financing Regime and its effect on Canadian charities

Blumberg Segal LLP is a law firm based in Toronto that provides legal services to Canadian non-profits, registered charities and donors. Blumberg Segal LLP maintains a website, globalphilanthropy.ca, that provides extensive information and resources to Canadian charities to encourage them to comply with their legal obligations and strive for higher standards in their operations. We also encourage donors to be generous but careful in the way they practice charity and philanthropy. Our firm is concerned about the well-being of the non-profit and charitable sector and has a special interest in encouraging international philanthropy. We are pleased that Finance will be conducting a consultation on "updating Canada's regime for combating money laundering and terrorist financing."

In the consultation paper, "Strengthening Canada's Anti-Money Laundering and Anti-Terrorist Financing Regime," proposals 4.3 and 4.4 relate to registered charities. Proposal 4.3 would allow the Canada Border Services Agency (CBSA) to share information with the CRA's Charities' Directorate on seizure reports when CBSA seizes forfeited currency. Proposal 4.4 allows the Financial Transactions Reports Analysis Centre of Canada ("Fintrac") to be more proactive and broad in its disclosure to CRA. Presumably, these recommendations will facilitate the Charities Directorate having greater awareness of potential money laundering or terrorist activities and other serious non-compliance that could potentially involve registered charities. The two proposals seem reasonable to implement and I have no objections to them.

We are concerned, however, that these relatively minor proposals may not be sufficient to protect charities from the misuse of charitable assets whether by terrorists, money launders or other criminals.

Importance of the Charitable Sector

According to the T3010 Registered Charity Information Return data from CRA, the charity sector has a total combined revenue of approximately \$192 billion per year. Currently, charities are approximately 8% of the economy and provide many vital services such as hospitals, universities, international assistance and social services. While there are a number of charities with revenues over \$1 billion, many charities are small. In fact, most charities have revenue under \$100,000. Most charities do not even have one paid staff person. Volunteers often end up doing the financial management and compliance work, yet the turnover rate of volunteers is a significant problem. In many other cases paid staff, who are not knowledgeable about financial management and compliance end up handling the finances of the charity.

According to the T3010 numbers in 2010, approximately 5200 charities identify funding projects outside of Canada and spending in total approximately \$2.6 billion. Some of the most important work done by charities involves international humanitarian assistance and international development work.

Threat to the Charity Sector

It has always been acknowledged that there is the possibility that Canadian charities could be used to support terrorism. In a recent presentation by the Director of the Review and Analysis Division of the Charities Directorate, it was noted that there are more than forty Criminal Code listed terrorist organizations¹ and his division has identified and responded to ten of these organizations either trying to establish a registered Canadian charity, involved with a Canadian charity or receiving funding or support from a Canadian charity. On our globalphilanthropy.caTM website we have provided information from publicly accessible sources on a number of Canadian charities involved with directly or indirectly supporting terrorism. **While one wants to deter charities being used for AML and terrorism it is important not to impose unrealistic expectations or requirements on charities, who often have very limited resources and capacity.**

¹ <http://www.publicsafety.gc.ca/prg/ns/le/cle-eng.aspx>

Suggestions

We will suggest a few thoughts in terms of how the charitable sector can be made more secure while not imposing unrealistic expectations on charities:

- **Canadian rules on “direction and control”² provide a good framework for Canadian charities operating outside of Canada, to avoid involvement with terrorism or any diversion of assets for private gain. However, many charities that conduct foreign activities are unaware of the rules.** In addition to not understanding Canadian rules, many charities do not understand the local laws and practices which can have an effect on their operations. Many Canadian charities do not realize the difficulties and complexities involved in operating abroad, especially in places that are suffering from endemic violence or post conflict situations. Many charities naively think that a well-intentioned effort based on trust will result in a positive outcome. There is a need for charities to have a better understanding of the rules that exist and how to comply with them.
- **Many Canadian charities operating abroad lack sufficient capacity to effectively carrying out their mission in a way that protects their assets especially in more difficult areas.** There are currently no requirements with respect to governance, risk management, capacity, training, understanding Canadian or foreign compliance requirements, internal controls or experience for a Canadian charity to operate abroad. This makes it more likely that resources will be used inappropriately. It is not surprising that while many charities do great work abroad, others cause more harm than good. This harm includes having funds ending up with the wrong people and also damaging the reputation of Canada and its charitable sector. There is an expectation in some quarters that charities spend as little as possible on “administration”³ and consequently this fixation on low overhead may increase the likelihood that some charities cannot properly account for how their funds are being spent. This often results in questions surrounding whether charitable funds are being used for legitimate charitable activities or something else. Helping charities to build their capacity to deal with foreign activities would be an important investment in protecting the sector and preventing funds going directly or indirectly to terrorism.
- **“Shelf charities” are being used by a small number of professional advisors and financial institutions to avoid the scrutiny and delay involved with a regular charity application.** In other words, some people apply for a large number of charities which

² <http://www.cra-arc.gc.ca/chrts-gvng/chrts/plcy/cgd/tsd-cnd-eng.html>

³

http://www.globalphilanthropy.ca/images/uploads/How_Much_Should_A_Canadian_Charity_Spend_on_Overhead_in_The_Canadian_Donor_Guide.pdf

does not identify the directors or officers who will be ultimately “purchasing” or taking over the charity. This evades the protections provided by the CRA charity application process.

- **A foreign person or entity can control a Canadian charity without the Charities Directorate even being aware.** As part of the application process and the subsequent T3010 filings there is no requirement to disclose the names of the members of the organization. In some cases, organizations may have only one or two members who are really controlling the organization and who have the legal authority under corporate law to replace one or all of the directors. While there is nothing wrong with having one member, if this one member is involved with promoting terrorism then this obviously raises concerns. In cases where there are less than five members, it is advisable that CRA should be asking for that information.
- **Lack of transparency about the misconduct of registered charities until after they have been revoked for cause.** We also have too much “confidentiality” when it comes to a small number of people using charities to directly or indirectly support terrorism as well as other nefarious conduct. If there is evidence that a charity is supporting terrorism or other extreme forms non-compliance, the CRA should be empowered to publish a warning to the public and should not have to wait for revocation for the CRA to disclose the last letters to the charity. Otherwise, the public will probably not be aware of any allegations of impropriety and the public may in good faith donate to a charity only to find out later that the charity was involved in directly or indirectly supporting a listed terrorist organization.
- **There is very little transparency on the 80,000 non-profits that are not registered charities or other types of qualified donees in Canada. However, these organizations are tax exempt, may receive government funding and also solicit donations from the public.** Prior to the introduction of the *Canada Not-for-profit Corporations Act* (CNCA), non-profits did not have to publicly disclose their finances, which included their revenues, expenditures, compensation and programs. With the new CNCA, financial statements of certain Federal non-profit “soliciting corporations” may need to be disclosed now. This does not affect provincial non-profits, Federal non-soliciting corporations, or corporations under the old *Canada Corporations Act*. While non-profits that are not charities in some cases are required to file the two page Form T1044 -Non-Profit Organization (NPO) Information Return, such form is not made available to the public either electronically or by request. In essence, except for the limited disclosure under the CNCA, there is no transparency for these non-profits in Canada. S. 241 of the *Income Tax Act* should be amended to allow the CRA to disclose information contained on the Non-Profit Organization (NPO) Information Return. In some cases a person who is prepared to support terrorism may also be prepared to forego the tax benefits of donating to a registered charity and donate to a non-profit.

Listed above are a few ideas to help protect the charitable sector from the small number of people who may wish to abuse charities and non-profits.

Public trust is very important for the charitable sector. As we have seen from the UK and US examples, when you have people committing acts of terrorism that have links to charities, it causes both regulatory scrutiny of the sector and public distrust. Therefore it is appropriate to take reasonable steps to prevent the involvement of non-profits and charities in terrorism.

If you require further information or wish to discuss this submission, please do not hesitate to contact us.

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