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**Update on Ineligibility Requirements: CRA's
Policy on Ineligible Individuals**

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OVERVIEW

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- REVIEW OF CRA GUIDANCE ON INELIGIBLE INDIVIDUAL PROVISIONS
- PRACTICAL APPLICATIONS FROM THE INELIGIBLE INDIVIDUAL PROVISIONS AND THE GUIDANCE

A. BACKGROUND TO INELIGIBLE INDIVIDUALS

- On August 27, 2014, the Canada Revenue Agency (“CRA”) released CG-024, its Guidance on how the ineligible individual provisions in the *Income Tax Act* should be interpreted and enforced (“Guidance” or “CG-024”)
- Under the *Income Tax Act*, CRA may refuse to register an applicant for charitable registration or suspend receipting privileges or revoke the registration of a charity or a registered Canadian amateur athletic association (“RCAAA”) if an ineligible individual is on the board or part of senior management of a charity, or is in a position to control or manage the organization

1. Legislative Background

- The provisions were introduced in the 2011 Federal Budget and came into force January 1, 2012.
- The Guidance emphasizes that CRA intends to enforce the provisions in a balanced way and that the sanctions are discretionary
- The “ineligible individual” provisions came as a result of concerns from CRA that it had no authority to refuse applications for charitable status based on the identity of the applicant for charitable status
- The new provisions are intended to provide CRA with the necessary authority to withhold or remove charitable status in situations where potential risk factors for abuse are present.

2. Who are “Ineligible Individuals”?

- Subsection 149.1(1) of the ITA was amended to define an ineligible individual as an individual who has been:
 - convicted of a relevant criminal offence unless it is a conviction for which
 - a pardon has been granted and the pardon has not been revoked or ceased to have effect, or
 - a record suspension has been ordered under the *Criminal Records Act* and the record suspension has not been revoked or ceased to have effect,
 - convicted of a relevant offence in the five-year period preceding that time

- a director, trustee, officer or like official of a registered charity or a RCAA during a period in which the charity or association engaged in conduct that can reasonably be considered to have constituted a serious breach of the requirements for registration under this Act and for which the registration of the charity or association was revoked in the five-year period preceding that time

- an individual who controlled or managed, directly or indirectly, in any manner whatever, a registered charity or a registered Canadian amateur athletic association during a period in which the charity or association engaged in conduct that can reasonably be considered to have constituted a serious breach of the requirements for registration under this Act and for which its registration was revoked in the five-year period preceding that time

- a promoter in respect of a tax shelter that involved a registered charity or a registered Canadian amateur athletic association, the registration of which was revoked in the five-year period preceding that time for reasons that included or were related to participation in the tax shelter
- CG-024 goes on to describe the meaning of key terms such as “relevant,” “relevant criminal offense,” “relevant offense,” “serious breach,” “a person who controls or manages,” and a “promoter of a tax shelter” as set out later in this presentation

B. WHY BE CONCERNED?

- On September 13, 2014, CRA revoked the charitable registration of the Friends and Skills Connection Centre.
 - One of the reasons cited in the notice of intention to revoke registration was that during the audit period one of the organization's directors was found to have previously been a director of another charity which had engaged in conduct that constituted a serious breach of the requirements for registration under the ITA
 - Previously, the only other publicly known instance of CRA applying the ineligible individual provisions was the revocation of Jesus of Bethlehem Worship Centre as a charity on July 11, 2014, which occurred prior to the Guidance being issued

- In an FAQ on the CRA website dated August 10, 2011, CRA indicated that it would be “developing detailed administrative guidance on how these new rules will be applied.”
- The length of time that it has taken to produce the Guidance is an indication of the complexities involved in the issues that it addresses
- The Guidance emphasizes that a charity must provide “adequate documentary evidence” such as copies of ledgers, cheques or financial reports indicating who has access to a charity’s assets if it hopes to avoid sanctions or revocations
- A mere statement that someone is not an ineligible individual will not be sufficient

C. REVIEW OF CRA GUIDANCE ON INELIGIBLE INDIVIDUAL PROVISIONS

1. Understanding who is an Ineligible Individual

- What is a “relevant criminal offence”?
 - A “relevant criminal offence” is a criminal offence under the laws of Canada or an offence that would be a criminal offense if it were committed in Canada
 - Only offences in federal statutes are criminal
 - A person convicted of a relevant criminal offence remains an ineligible individual unless a pardon is granted or a record suspension is ordered

- What is a “relevant offence”?
 - A “relevant offence” is an offence under provincial legislation or an offence under federal legislation that is not a criminal offence
 - Examples of relevant offences are breaches of charitable fundraising legislation, consumer protection legislation, and securities legislation
 - A person convicted of a relevant offence is an ineligible individual for five years from the date of conviction

- What is a “relevant” offence?
 - An offence is a “relevant” criminal offence or relevant offence if it relates to financial dishonesty or if it is relevant to the operation of an organization
 - Examples of financial dishonesty include: misappropriation of funds; forgery; and fraud
 - Offences are likely relevant to an organization if the victim is similar to the beneficiaries of the program; the operation of the organization provides an opportunity for a similar offence; or the organization’s operations would be at risk if a similar offence was committed

- What is a “serious breach”?
 - The definition of “serious breach” described in the Guidance is somewhat broader than some may have anticipated
 - The Guidance states at paragraph 17 that, “to determine whether someone is or is not an ineligible individual, the breach that resulted in revocation must be serious.”
 - The Guidance goes on to state that, “The CRA considers **any** revocation resulting from an audit to be a serious breach”

- Revocation for failure to file an annual return or lapse in governing documents would not be considered a serious breach under the ineligible individual provisions
 - Examples provided by Guidance include: revocation for issuing fraudulent receipts; misappropriating assets; or participating in abusive gifting tax shelters
 - CRA will also consider “repeated infractions as aggravating factors in determining whether the breach that resulted in revocation is serious”
- Consequences of “any revocation resulting from an audit” constituting a serious breach has broad ramifications

- While revocation may occur due to abuse of the charitable registration system, i.e., improper receipting or involvement in a tax shelter, many revocations can occur for broader and less concrete reasons
 - e.g., failing to maintain adequate books and records, filing an “inaccurate or incomplete” T3010, charitable purposes being broad and vague, or partisan political activities

- Who is a “director, trustee, or like official”
 - Depends upon the governing documents of the organization
 - A “like official” is “person who has governing responsibilities or authority, whether or not this is stated in the governing document”
 - This may include a pastor of a church or religious organization where the individual may not be on the board, but has “significant influence” or a “veto” over the decisions of the board
 - May also apply to a founder, or similar positions within a charity

- Who is a person who “controls or manages”
 - A person who “controls or manages” can include a director, trustee, or officer, but is also wider to include any person that knows, or ought to have known, how the organization operates
 - Individuals who control or manage a charity are accountable, whether or not they directly participated in the non-compliant conduct
 - Individuals who have the power to make decisions about the actions of the organization or appropriate the organization’s assets have control, e.g., individuals who manage can hire or dismiss employees or prepare budgets

2. CRA's Enforcement Approach

- The Guidance states that CRA will focus on “deliberate abuse of the registration system” and will administer ineligible individuals “with a view to limiting threats to beneficiaries and assets”
- CRA will consider:
 - What impact did the conduct have?
 - Did the ineligible individual engage in the conduct more than once?
 - Is there an opportunity for the ineligible individual to repeat the conduct?
 - If repeated, what impact would that conduct have on beneficiaries and assets?

- Is the organization aware of the person's past conduct and the person is an ineligible individual?
- Has the ineligible individual's roles and responsibilities been appropriately restricted?
- Are there appropriate financial controls in place to safeguard assets?
- How is the safety of beneficiaries ensured?
- A lack of enforcement action by CRA does not mean that CRA has endorsed an ineligible individual to remain within the organization
- Any enforcement will follow CRA's usual course of action concerning an audit, i.e., the organization will have an opportunity respond in writing, and object where the organization disagrees with CRA

3. Responding to CRA

- Generally, an organization may:
 - provide information to prove that the person in question is not an ineligible individual
 - provide evidence that the ineligible individual is not, or is no longer a director, trustee, officer, or like official, or does not directly or indirectly, in any way control or manage the organization
- Alternatively, where the organization wants an ineligible individual to remain it may:
 - Show that the ineligible individual's roles and responsibilities are restricted;
 - Show that appropriate and adequate control measures in place; or
 - Show how the organization benefits

- How do we document controls and/or other safeguards concerning ineligible individuals
 - Guidance states that CRA will be “satisfied only with adequate documentary evidence in support of the organization’s response.”
 - Examples include:
 - Minutes that demonstrate signing authority (e.g., where financial dishonesty is a concern);
 - Policies concerning financial controls and due diligence; or
 - Financial reports and other documents indicating an ineligible individual does not have access to finances

D. PRACTICAL APPLICATIONS

- What if my organization wants an ineligible individual to be involved?
 - The Guidance recognizes that it may “be appropriate in some cases for an organization to welcome an ineligible individual into its operations”
 - e.g., prisoner rehabilitation programs, drug and alcohol addiction programs, and the prevention of juvenile delinquency
 - However, the Guidance states that, “The onus is on the organization to explain the role and contribution of the ineligible individual if the CRA expresses concern about him or her”
 - Organization may “outline what internal measures have been put in place to protect vulnerable beneficiaries and assets of the organization.”

- Implement Due Diligence Policies
 - Appendix B to the Guidelines provides a summary of good governance processes that can help protect the beneficiaries and assets of an organization, although they are not required under the *Income Tax Act*
 - While the Guidance indicates that CRA may not necessarily enforce the ineligible individual provisions in all cases, the prudent approach for a registered charity or RCAA is to assume that CRA will, and therefore implement the practices discussed in the Guidance, and in consultation with legal counsel

- The Guidance notes that the practices are, “are meant to help registered organization’s focus on areas that might expose their beneficiaries or assets to risk”
 - i.e., where a charity works with vulnerable beneficiaries, or where financial assets such as the bank account are exposed
 - For example, where a bank account is opened in the name of an officer without the knowledge of the board, or where only one individual has signing authority for cheques or other financial instruments

- Due diligence practices
 - Include, developing and implementing “practices and policies to protect the organization’s interests;”
 - Conducting a risk assessment that considers the specific circumstances of the organization
 - Adopting practices that make fraud less likely to occur
 - Segregating duties so that no one person has complete control of a financial transaction
 - Including measures in a policy for the regular monitoring of staff and volunteers

- What should a policy concerning ineligible individuals cover?
 - Demonstrate the level of risk assessment the board should conduct prior to the ineligible individual coming on board or senior management
 - Outline steps are to be taken in order to minimize the risk the individual poses
 - For example, with respect to the proposed director having a “relevant criminal offence” related to financial dishonesty, the policy would provide that the said individual would not serve as treasurer or have any signing authority with respect to the finances of the organization

- Considerations in drafting a policy:
 - Who will the policy apply to?
 - Will the policy govern those who wish to be a director, trustee, or like official?
 - Will the policy also govern senior management individuals and other employees who may be impacted by the ineligible individual provisions?
 - May also want to utilize the self-assessment questionnaire for individuals impacted by ineligible provisions in the Guidance

- Will the policy have a broad or narrow focus?
 - Where the organization wishes to have an ineligible individual on the board, i.e., a pardoned criminal to assist with rehabilitation programs, the policy may be narrow in scope
 - Other policies may deal with prevention
- While a policy will be of assistance in demonstrating to CRA that the organization has exercised due diligence, a policy will only be useful if it is followed in practice and updated regularly

- Will the policy coordinate with other operating policies of the charity?
 - e.g., how will the policy concerning ineligible individuals impact the work of the nominating committee (if applicable), or other election procedures
- How will the policy address corporate law rights?
 - e.g., Under the *Canada Not-for-profit Corporations Act*, and other jurisdictions, members may have a right to bring a proposal concerning the nomination of a director

- Implement Board Screening Procedures
 - Guidance states that, “the legislation does not require registered organizations to do searches or to proactively determine whether an ineligible individual is a member of the board or controls and manages the organization”
 - However, potential revocation means it will likely become necessary for many organizations
 - Even if the charity wanted to review the information required to independently assess whether an individual is ineligible, it may not be publicly or easily available
 - Possible to search for relevant criminal offences in Canada, but abroad?

- Many relevant offences (e.g., *Securities Act* convictions) are not tracked in publicly available databases in Canada, or unlikely abroad
- Names of directors and like officials of revoked charities are not maintained in a single publicly available database
- Not likely that an individual who otherwise controlled or managed the operation of a charity would be identified in publicly available documents – likely information solely in CRA's control

- Criminal records involve a highly sensitive and personal issue and therefore appropriate procedures should be established to protect privacy
 - Policy should carefully address how personal information will be managed, and may need to cross-reference to the privacy policy of the organization
 - Nominating Committee or other individuals who may not be on the board of an organization need to treat such information carefully

- Reference in the by-laws, constitution, or other governing documents of the organization
 - The Guidance also state at Appendix A that “An organization’s bylaws or governing document may outline how it will deal with an ineligible individual.”
 - Many registered charities or RCAAAs are incorporated, but some charities may be established as a trust or an unincorporated association
 - The governing documents, i.e., by-laws for a corporation, or similar document, normally set out qualification requirements for directors and officers

- The organization may wish to amend its by-laws in order that an individual is qualified as a director provided that he or she is not an ineligible individual, and that such individual is disqualified as a director where he or she becomes one
 - A signed consent for the director may also include a declaration that the individual meets the requirements necessary to be a director set out in the by-laws
- Where the organization wishes to have an ineligible individual involved, this approach may not be appropriate
- In such circumstances, the by-laws may want to cross-reference to an operating policy established by the board of directors concerning ineligible individuals

- Review Employee Hiring Practices for Managers
 - Employees cannot necessarily be terminated simply because they are an ineligible individual, even if doing so may be necessary to safeguard the beneficiaries or assets of the organization
 - Employees' rights under common law, employment standards and human rights legislation will have to be respected in dealing with the “ineligible individual” issue and may very well lead to a substantial financial cost for termination

- Include a contractual provision governing how the employment relationship may change if an employee who controls or manages the organization becomes an ineligible individual
 - Removal of management staff that are “ineligible individuals” could have important employment law ramifications
 - For existing staff it may difficult to remove them
 - For new management staff it will be important to include this in an employment contract
- Obtain legal advice from employment counsel

- What if I sit on more than one board?
 - It is common for many directors to be involved on the boards of various charities and non-profit organizations
 - It is less common for senior management to be involved in more than one charity
 - Sometimes directors of charities will overlap as part of a multiple corporate structure
 - These structures may need to be considered in light of the ineligible individual provisions, as an ineligible individual serving on more than one board may jeopardize more than one organization

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