the Charities File: ON BOARD

Treasurer's Chest: FAQs from a Treasurer's Perspective

The following material is designed to provide basic information about concepts that are relevant for a treasurer of a registered charity. It is divided into three sections.

Given that this information provides a brief overview of a concept and does not address all the nuances that must be considered, it is recommended that the reader access the more detailed information and examples available on the CRA website.

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A. Financial Definitions and Accountability

What is financial accountability?
Registered charities are accountable to government and the public at large for the money they raise and how they use their resources.

What is Disbursement Quota (DQ)?
The disbursement quota (DQ) is the minimum amount a registered charity has to spend on charitable activities or gifts to **qualified donees** to keep its registered status. This amount varies according to a charity's designation (i.e.: whether it is a charitable organization, a public foundation, or a private foundation).

The purpose of the disbursement quota is to ensure that registered charities actively use their donations to help others according to their charitable purposes.

In general, it is an expenditure test based on tax-receipted **gifts** (line 4500 from T3010) and gifts received from other registered charities in the previous fiscal period (line 4510 from T3010). The value of enduring property spent in the fiscal period or transferred to qualified donees as well as certain properties must also be considered.

What is a financial statement?
Registered charities must provide financial statements as part of their filing requirements for the annual information return even if the charity was not active during the **fiscal period** or had a zero balance. They should accurately show the different sources of revenue and the expenditures for the fiscal period being reported.

At a minimum, financial statements should consist of:

- A statement of **assets** and liabilities (balance sheet), and
- A statement of revenue and expenditures (**income statement**).

Financial statements may also include:

- Accounting policies (for example, depreciation rates);
- Details of investments (for example, maturity dates and interest rates);
- Sources of revenue (for example, type of government grant);
- Non arm's length party transactions;
- Information about funds subject to a direction from the donor that they be held for a period of 10 years or more; or
- Future obligations.

If a registered charity has income over $250,000 the CRA recommends that financial statements be professionally audited, otherwise, the treasurer for the charity should sign them.

What is an Income Statement?
A financial statement that summarizes the results of business activities (**income** and expenses) for a given period of time. This is sometimes called a profit and loss statement.

Income is the sum of revenues earned in a specific period of time. It includes revenues from salaries, wages, benefits, tips, and commissions, profits from operating a business or profession, and investments earned.

What is an asset?
Assets are the entire property of an organization or society. This can include:

- Current Assets: cash, bank accounts, short-term investments, amounts receivable, inventories
- Long term Assets: long-term investments that will mature in one year or later (for example, stocks or bonds)
- Fixed Assets: capital assets (for example, a building or equipment)

Should the financial statements included with the T3010B return be audited?
The Charities Directorate does not require that a charity's financial statements be audited. However, other government authorities, a charity's head body, or its funding bodies may require audited statements.

- The charity's treasurer should sign financial statements that have not been audited.

What is a fiscal period?
A registered charity's taxation year is a fiscal period. A fiscal period is the 12 months (or, for incorporated organizations, a period of up to 53 weeks) covered by an organization's financial statements. A fiscal period end or year end is the date on which the period covered by the organization's financial statements ends.

How can I change the fiscal period for our charity?
A registered charity must get permission from the Charities Directorate before it can change its fiscal period end, since such a change affects the charity's filing obligations. To ask for a change, send a letter with the following information; the new fiscal period end; the reason for the change; the proposed effective date; and the signature of a director/trustee or other authorized representative of the charity.

- If a registered charity receives approval to change its fiscal period end, it will have a transition period that is not a full 12 months. Therefore, it must file a separate information return for the months of transition.
- A return for the transition period or for the new fiscal period cannot be processed until the change in fiscal period end has been approved. Therefore, the charity should submit a request as soon as it decides to make the change.

What is an accrual method of accounting?
With this method, income (which is all of the proceeds a registered charity received during a fiscal period, minus all expenses) is reported in the fiscal period it is earned, regardless of when it is received. The expenses are also deducted in the fiscal period they are incurred, whether they are paid or not. This method is generally used by businesses or professionals.

As a rule, you must calculate your net charitable income according to the accrual method of accounting. Consequently, you must

- Report your income for the fiscal period in which it was earned, regardless of whether it was actually paid to you during that period; and
- Deduct your expenses for the fiscal period in which they were incurred, regardless of whether you actually paid them during that period.

What books and records must I keep to ensure compliance with CRA expectations?
A registered charity must keep adequate books and records in either English or French, at a Canadian address it has on file with us, so that the CRA can verify official donation receipts issued, as well as its income and expenditures.

A charity must also keep information that we can use to determine whether its activities continue to be charitable. This additional information will vary from charity to charity but could include, for example, copies of minutes of meetings, correspondence, publicity brochures, or advertisements.

The charity should retain its books and records as follows:

- Duplicates of receipts must be retained for a minimum of two years from the end of the calendar year in which the donations were made
- Books and records, together with the accounts and vouchers, containing the summaries of the year-to-year transactions of the charity, must be held for a minimum of six years from the end of the fiscal period to which they relate.

The following must be kept as long as the charity remains registered and for two years after the registration is revoked:

- All records of any donations received by a registered charity that are subject to a direction by the donor that the property given be held by the charity for a period of not less than 10 years;
- Minutes of meetings of the executive;
- Minutes of meetings of the members; and
- All governing documents and by-laws.

Books and records may be destroyed at an earlier time than outlined above if the Minister gives written permission for their disposal.

What is a Qualified Donee?

Qualified donees are organizations that can, under the *Act,* issue official tax receipts for gifts that individuals or corporations make to them.

Qualified donees include:

- Registered charities;
- Registered Canadian amateur athletic associations;
- Registered national arts service organizations;
- Housing corporations in Canada constituted exclusively to provide low-cost housing for the aged;
- The United Nations and its agencies;
- Universities outside Canada with a student body that ordinarily includes students from Canada (these universities are listed in Schedule VIII of the *Income Tax Regulations*);
- Charitable organizations outside Canada to which Her Majesty in right of Canada (the federal government or its agents) has made a gift during the registered charity's fiscal period, or in the 12 months immediately before the period;
- Municipalities in Canada;
- Her Majesty in right of Canada or a province or territory (the federal government, a provincial or territorial government, or their agents);
- As of May 8, 2000, municipal or public bodies performing a function of government in Canada.

B. Issues related to payment of Board members or volunteers

What is an undue benefit?
Under the *Income Tax Act*, a registered charity cannot confer on a person an undue benefit (e.g., a transfer of property or other resources of the charity to a person who does not deal with the charity at arm's length or who is the beneficiary of a transfer because of a special relationship with a donor or charity.)

What is at arm's length and what the implications of this concept to a charity?
At arm's length is a tax concept describing a relationship in which the parties are acting independently of each other. The opposite, not at arm's length, covers people acting in concert without separate interest, including individuals who are related to each other by blood, marriage, adoption, common-law relationships, or close business ties.

For example, it is necessary to consider partnership in a business in determining whether there is an arm's length relationship between directors of an applicant charity. It is our view that where the identified directors of a charity are all partners in the same firm or a combination of partners and employees of the firm such as secretaries, then these persons are not dealing at arm's length for the purpose of the designation of the charity. These persons are not acting in their own separate interests as they would be in ordinary common dealing between one another; rather they are acting in concert without separate interest

Can I pay Board Members for their service to the Charity?
The *Income Tax Act* stipulates that no part of the income of a "charitable organization" shall be payable to, or otherwise available for the personal benefit of any proprietor, member, shareholder, trustee or settlor thereof. The Department considers the meaning of the term "trustees" to include persons having the general control and management of the administration of a charity, including directors of corporations established for charitable purposes.

The Department's position regarding the remuneration of directors is that *bona fide* payments for services rendered do not constitute a "personal benefit" of the type prohibited by the Act. Accordingly, a registered charity may remunerate its directors for other services they actually perform on behalf of the charity, but not simply for accepting the title of director, as long as these payments are reasonable under the circumstances. Nevertheless, a charity could be contravening the requirements of the Act if it enters into a lucrative employment agreement with one of its directors.

Can a charity pay for out-of-pocket expenses incurred by volunteers?
While it is acceptable for a registered charity to reimburse volunteers for expenses incurred on behalf of the charity, a charity cannot simply issue an official donation receipt to a volunteer *in lieu* of reimbursing the expenses. A charity can reimburse a volunteer for the expenses incurred on behalf of the charity and later accept the return of the payment as a gift, provided that the amount is returned voluntarily. (e.g. exchange of cheques, thus ensuring the charity has proper financial records justifying the receipts it issues to the volunteer and the volunteer can document that he or she has transferred property to the charity.)

A charity should also have a policy in place on reimbursing volunteers. The policy should specify both the type of expenditures the charity is prepared to repay (*e.g.*, for reasonable accommodation if the volunteer is travelling on the charity's business), and appropriate procedures to document the volunteers' payments, such as submitting credit-card slips.

C. Information related to receipting practices of charities

What guidelines affect a charity with respect to fundraising?
A registered charity can raise funds to support its charitable purposes.

Fundraising activities may be external activities, such as soliciting donations through telemarketing, direct mail, or door-to-door canvassing, putting on events, or distributing information through the media or a charity's own publications. They may also be internal activities, such as prospect research or hiring of fundraisers. Whether such activities are carried out under contract, by staff, or by volunteers does not affect the activity.

However, fundraising is not itself a charitable activity. As a result, fundraising cannot the primary emphasis of the charity and a 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.

What can a charity issue a tax-receipt for?
Under the *Income Tax Act*, a charity can issue official donation receipts for income tax purposes for donations that legally qualify as **gifts.**

What is a gift?
A gift is defined as a voluntary transfer of property without valuable consideration.

To qualify as a gift, all three of the following conditions must be met:

- Some property, either in the form of cash or **a gift-in-kind**, is transferred by a donor to a registered charity.
- The property is given voluntarily. The donor must not be obliged to part with the property, for instance as the result of a larger contract or a court order.
- The donor is transferring the property to the charity without expecting anything in return. No benefit of any kind may be provided to the donor or to anyone designated by the donor as a result of a gift.

What is a gift-in-kind?
Gifts-in-kind, also known as non-cash gifts, are gifts of property. They include items such as artwork, equipment, securities, shares, land and cultural and ecological property.

A contribution of service, that is, of time, skills or efforts, is not property and, therefore, does not qualify as a gift or gift in kind for purposes of issuing official donation receipts.

Who can receive a tax receipt?
Under the *Income Tax Act*, a donor can be an individual or a corporation. An individual can claim a tax credit for **the eligible amount of gifts** made to qualified donees. A corporation can deduct the eligible amount of gifts made to **qualified donees** from its taxable income.

An official donation receipt must bear the name and address of the donor.

What is split receipting?
Split receipting is the method used for calculating **the eligible amount of a gift** for receipting purposes when the donor has received an **advantage** (consideration) in return for his or her donation. To

determine the eligible amount for receipting purposes, the value of the advantage must be subtracted from the value of the gift.

Criteria for split receipting:

- Where a donor receives an advantage in exchange for a gift, the registered charity must be able to accurately determine the fair market value of that advantage.
- The gift, minus the advantage, must still constitute a voluntary transfer of property and meet the intention to make **a gift threshold**.

What is an advantage?
An advantage is what a donor may receive in return for his or her donation (for example, a meal, tickets to a show), and it must be taken into consideration when determining the eligible amount of a gift for receipting purposes. Determining the fair market value of an advantage is similar to determining the fair market value of a gift in kind. However, while only donations of property can be receipted as gifts in kind, the fair market value of any type of advantage (for example services, meals, accommodation) must be taken into consideration when determining the eligible amount of a gift for receipting purposes.

What is a gift threshold?
In cases where the value of an advantage received for a gift is more than 80% of the value of the gift itself, it is generally considered that there is no true intention to make a gift. Therefore, registered charities cannot issue a receipt where the value of the advantage returned to the donor is more than 80% of the fair market value of the gift (gift threshold).

What is the eligible amount of a gift for receipting purposes?
The amount by which the **fair market value (FMV)** of the gifted property exceeds the amount of an advantage, if any, in respect of the gift.

The advantage is generally the total value of all property, services, compensation, or other benefits that a person is entitled to receive as partial consideration for, in gratitude for, or is in any other way related to the gift. The advantage may be contingent or receivable in the future, either by the donor or a person or partnership not dealing at arm's length with the donor.

What is fair market value (FMV)?
Fair market value generally means the highest price, expressed in dollars, that a property would bring in an open and unrestricted market, between a willing buyer and a willing seller who are both knowledgeable, informed, and prudent, and who are acting independently of each other.

What is the de minimis rule and how does it is affect the value of the advantage?
Certain advantages are of nominal value, and are considered too minimal to affect the value of a gift. In applying the de minimis rule, advantages that have a combined value that does not exceed the lesser of $75 or 10% of the value of the gift are considered too minimal to affect the amount of the gift. These advantages do not need to be deducted from the value of gifts when issuing receipts. The de minimis rule does not apply to cash or near cash equivalents.

What does not qualify as a gift and thus, cannot be receipted?
The following items do not qualify as a gift and thus, not eligible to be receipted:

- Contributions of services (i.e., time, skills, effort). Contributions of services are not property and do not qualify. However, a charity can pay for services rendered and later accept the return of all or a portion of the payment as a gift, provided it is returned voluntarily
- A payment from a business for which the business receives a material advantage such as promotion or advertising in return. For taxation purposes, the business may be able to claim the contribution as an advertising expense
- A gift subject to a direction by the donor that the charity transfer the funds to a specified person or family. In such an instance, the donor has made a gift to the person or family and not to the charity
- A gift subject to a direction by the donor that the charity give the funds to a non-qualified donee.
- The payment of a basic fee for admission to an event or to a program (e.g., fees for day-care or nursery school facilities)
- The payment of membership fees that convey the right to attend events, receive literature, receive services, or be eligible for entitlements of any kind (e.g., free access to facilities the public has to pay for). However, membership fees are considered as gifts if they confer no more than the right to vote at a meeting and to receive reports of the charity's activities, unless such reports are otherwise available for a fee
- Any portion of the purchase price of a lottery ticket or other chance to win a prize, even though the lottery proceeds benefit one or more charities
- The payment of tuition fees (some exceptions in Information Circular 75-23)

What information should appear on an official donation receipt?
An official donation receipt must include, in a manner that cannot be readily altered, at least the following information:

- a statement that it is an official receipt for income tax purposes;
- the charity's BN (Business Number)/Registration number, name and address in Canada as recorded with our Charities Division;
- the serial number of the receipt;
- the place or locality where the receipt was issued;
- if it is a cash donation, the day on which or the year during which the charity received the donation;
- if the donation is a gift other than cash, i.e., a gift-in-kind:
    - the day on which the charity received the donation,
    - a brief description of the gift, and
    - the name and address of the appraiser of the property if an appraisal was completed;
- the day on which the charity issued the receipt (if that day differs from the date on which the charity received the donation);
- the name and address of the donor including, in the case of an individual, the first name and initial;
- the amount of a cash donation, or if the donation is a gift other than cash, the amount that is the fair market value of the gift at the time it was made; and
- the signature of the individual(s) authorized by the charity to issue receipts.

In preparing official donation receipts, a registered charity must indicate the year in which it actually received a gift. If a gift is dated, mailed, and postmarked in one year and received in the next year, the charity can issue a receipt indicating the year appearing on the postmark as the date it received the gift. A charity must keep on file a copy of all official receipts that it issues.