



Canada Revenue
Agency

Agence du revenu
du Canada

Auditing Charities

Table of contents

	Page		Page
Why does the Canada Revenue Agency audit charities?	3	What are the charity's responsibilities?	5
What triggers a charity audit?.....	3	Do you have any comments on the audit?	5
How do we conduct an audit?	3	Need more information?	5
What happens when the audit report is completed?	4	Electronic mailing list	5
Objection and appeal process	5		

Why does the Canada Revenue Agency audit charities?

This booklet provides information on how and why the Canada Revenue Agency (CRA) audits charities and what you can expect from an audit.

The CRA is responsible for monitoring the operations of registered charities within Canada to make sure they comply with the requirements of the *Income Tax Act* (the Act). Audits are an important element of this process.

For example, the Act requires that registered charities devote all of their resources, including financial, human, and physical resources, to **charitable purposes**. To verify how a charity uses its resources, we look at the information in a charity's annual returns, financial statements, and other documents.

The administrative procedures that we follow ensure that we treat all charities fairly, impartially and consistently throughout the audit process.

Generally, aside from the most serious cases of non-compliance, the CRA takes an education-first approach to compliance. This provides charities with the opportunity to correct their actions through education or compliance agreements before resorting to other measures such as sanctions or revocation.

What triggers a charity audit?

The following are some of the reasons that a charity is selected for audit:

- random selection;
- to review specific legal obligations under the Act;
- to follow-up on possible non-compliance or complaints; and
- to confirm that assets have been distributed after revocation.

Occasionally, we will make an on-site visit to gather information to help us understand the purposes and activities of an organization that has applied for registered charity status. This is referred to as a pre-registration audit.

How do we conduct an audit?

When we conduct an audit of a registered charity, we do not necessarily limit the process to examining a charity's financial affairs. Usually, in addition to reviewing its finances, we also review any evidence that might indicate whether or not the charity is satisfying its legal obligations under the Act and is operating for charitable purposes.

There are two primary types of audit: the field audit and the office audit. The size and complexity of a charity's operation will often dictate the type of audit required.

The field audit

We conduct the field audit on the charity's premises. Either a single auditor or a team of auditors conducts the audit. The length of time required to complete an audit depends on several factors, including:

- whether the audit is general or specific in nature;
- the quality of the charity's books and records;
- the time required for the charity to provide additional information; and
- the size and complexity of the charity's operations.

The first step in this process is to review all of the information we have in our files about the charity. This may include the governing documents, descriptions of programs and activities, annual information returns, financial statements, and other sources, where appropriate.

The auditor will first telephone the charity to notify it of the audit, arrange a mutually convenient time and location to meet with the charity, and tell the charity what items will be reviewed during the audit to allow the charity to gather the necessary materials. The auditor confirms the details of this conversation in writing.

The audit process usually includes examining the charity's ledgers, journals, bank accounts, expense accounts, investments, agreements, contracts, governing documents, annual reports, minutes or other records of board and staff meetings, and other documents that relate to the charity's activities.

When they arrive on the charity's premises, the auditors show their agency identification cards. The auditors may want to discuss with the charity's representatives some of the information they obtained when they reviewed the files. This discussion helps the auditors understand the charity's activities and operations before they begin examining the books and records. The auditors may also want to tour the premises to better understand the transactions recorded in the books and to observe the charity's programs and activities. During the audit, the auditors may also need additional information and help from the charity's representatives.

Generally, before finalizing the audit report, the field auditors will review and discuss their preliminary findings with one or more of the charity's representatives. This review ensures that the auditors have received all the information they need to consider when they evaluate the audit.

The office audit

An office audit is conducted by the Charities Directorate at CRA Headquarters, as opposed to the charity's place of business. Typically, a single auditor conducts an office audit.

An office audit involves a complete review of all information and documentation available in the charity's file. This may include the governing documents, descriptions of programs and activities, annual information returns, financial statements, and other sources, where appropriate.

Occasionally, it may be necessary to contact the charity to obtain additional information or clarification. In this case, the auditor contacts the charity either by phone or by registered mail.

What happens when the audit report is completed?

When the audit is completed, a letter is sent to the charity outlining the results of the audit.

- If the charity's operations and activities appear to comply with the Act, we will confirm that there will be no change to the charity's registered status.
- In cases where the audit has raised concerns, the letter will notify the charity of our specific concerns.

The Charities Directorate can use the following tools, ranked in order of their potential severity, to obtain compliance: education letters, compliance agreements, sanctions, or the revocation of a charity's registration. The facts of a particular case will determine which compliance measure will be adopted. In cases of serious non-compliance, we are prepared to move directly to sanctions or revocation.

Detailed information about our compliance approach and procedures can be found in "Guidelines for Applying the New Sanctions", available at <http://www.cra-arc.gc.ca/tax/charities/policy/newsanctions-e.html>.

Education letters

An education letter does not adversely affect a charity's registration. The letter identifies where the charity has not complied with the Act or CRA policy. The letter provides guidance to the charity so that it can take the required steps to become fully compliant.

For example, an education letter might be appropriate when a charity's official receipts do not contain all of the required information. An education letter would be issued to inform the charity of the receipt requirements.

Compliance agreements

In more serious cases of non-compliance, the Charities Directorate may enter into a compliance agreement to correct the situation.

The agreement outlines the non-compliance issues and the remedial actions that the charity has agreed to undertake, sets out the timelines for the necessary changes, and outlines the consequences if the charity fails to abide by the agreement. Representatives of both the charity and the CRA sign the agreement. We follow up to ensure that the charity complies with the agreement.

A compliance agreement may be proposed in situations where a charity was unaware of the legal requirements or thought it was meeting the requirement, but made an error in the calculation or interpretation of the law.

Sanctions

In more serious cases of non-compliance, sanctions may be imposed. Sanctions include a temporary suspension of a charity's tax receipting privileges and its status as a qualified

donee or financial penalties. A list of sanctions can be found at www.cra.gc.ca/tax/charities/policy/csp/penalties-e.html.

A **financial penalty** is first proposed and the charity is given an opportunity to address our concerns if it feels that a penalty should not be applied. If we do not hear from the charity or do not accept its representations, the Directorate will notify the charity with a *Notice of Assessment* that a penalty has been imposed.

Similarly, **suspension of a charity's tax receipting privileges and its status as a qualified donee** is first proposed and the charity is given an opportunity to address our concerns. If we do not hear from the charity or do not accept its representations, the Directorate will notify the charity with a *Notice of Suspension* that a suspension has been imposed.

Information about charities that are subject to sanction is posted on the Charities Directorate Web site.

Revocation of registration

Where we find a **serious case of non-compliance** with the Act, we will revoke the charity's registered status. While revocation is generally a last resort, the Act allows for revocation at any time, where appropriate to the circumstances. This includes cases where one or more of the following factors are present:

- The organization had a previous record of serious non-compliance, and the current form of non-compliance is both serious and intentional;
- The non-compliance has had a substantial, adverse effect on others (beneficiaries, donors, or funders), particularly where the organization cannot or will not remedy the harm done; and
- The organization cannot or will not bring itself into compliance.

We notify the charity of our concerns in writing. The letter explains that the concerns are grounds for revoking the charity's registered status. At that time, we give the charity the opportunity to address our concerns if it feels we should not revoke its registration.

If, after considering any representations a registered charity provides, the Directorate determines that there is sufficient cause to revoke a charity's registered status, we send the charity a *Notice of Intention to Revoke* by registered mail. The notice states that we plan to revoke the charity's registration.

On revocation of a charity's registration:

- It can no longer issue official donation receipts;
- The organization is no longer exempt from income tax unless it qualifies as a non-profit organization; and
- It may be subject to a tax equivalent for the full value of its remaining assets (revocation tax).

Objection and appeal process

As discussed above, a charity may be subject to certain penalties or the loss of its registered status as a result of an audit. As of June 13, 2005, charities have the right to object to the following decisions:

- *Notice of Intention to Revoke* a charitable registration;
- *Notice of Annulment* of charitable registration;
- *Notice of Assessment* concerning a revocation tax or one of the financial penalties applicable to charities;
- *Notice of Suspension* of tax-receipting privileges and qualified donee status; and
- *Notice of Designation*.

When a charity receives one of these notices and feels that the CRA has not interpreted the facts or applied the law correctly, the charity can object in writing to the Assistant Commissioner of the Appeals Branch at 25 Nicholas Street, Ottawa, ON K1A 0L5. The charity must set out the reasons for the objection and all the relevant facts.

An objection must be filed no later than 90 days after the day of mailing of the notices listed above. The Appeals Branch is responsible for the objection process, and its mandate is to conduct fair, transparent, and impartial reviews of the decisions rendered by the CRA. Further information regarding filing a notice of objection is available at www.cra.gc.ca/tax/charities/policy/csp/csp-005-e.html.

If a charity disagrees with the CRA's decision concerning its objection, the charity has the right to appeal to either the Federal Court of Appeal or the Tax Court of Canada, depending on the type of appeal. Further information regarding appeals to a Court is available at www.cra.gc.ca/agency/programs_services/disagree/charities-e.html.

What are the charity's responsibilities?

- File annual T3010A information return
- Meet annual spending requirement (disbursement quota)
- Keep adequate books and records
- Issue complete and accurate donation receipts
- Engage only in allowable activities
- Inform the Charities Directorate of any changes to the charity's mode of operation or its legal structure
- Maintain the charity's status as a legal entity

Do you have any comments on the audit?

If we have recently audited your charity, we would like to hear about your observations or concerns.

Do you feel we properly informed you about the audit process? Did you find the exercise helpful in understanding your obligations with respect to an organization that is a registered charity under the Act?

Please send your comments to:

Director, Compliance Division
Charities Directorate
Canada Revenue Agency
Ottawa ON K1A 0L5

Need more information?

Visit the Charities and Giving Web site at www.cra.gc.ca/tax/charities topics include:

- Forms and publications;
- Policies;
- Newsletters;
- Charities Listings; and
- Outreach activities.

You can reach the Charities Directorate by calling:

- 1-800-267-2384 for toll-free, long distance calls (English);
- 1-888-892-5667 for toll-free, long distance calls (bilingual);
- 1-800-665-0354 for toll-free TTY service for persons who are deaf or hard of hearing or have a speech impairment.

You can write to us at:

Charities Directorate
Canada Revenue Agency
Ottawa ON K1A 0L5

Electronic mailing list

We encourage all officers, directors, and employees of registered charities to subscribe to *Charities What's New* Electronic Mailing List (EML). Subscribers will be notified about additions to the Charities and Giving Web site, including Charities Newsletters, policy statements and commentaries, new guidelines, draft guidelines for consultation, and information about outreach activities.

To subscribe, visit our Web site at www.cra.gc.ca/eservices/maillist/subscribecharities-e.html and follow the easy steps.