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COMMENTARY

THE CHARITY PAPERS

Bringing the Provinces Back In:

Creating a Federated Canadian Charities Council

Adam Aptowitzer

In this issue...

The regulatory regime for Canadian charities is fundamentally flawed. Historical happenstance and lack of provincial initiative created a regulatory vacuum that federal tax officials filled. There is a better way.

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The Study in Brief

Canadian charities need a new regulatory system. Currently, charities are regulated primarily at the federal level by the Canada Revenue Agency (CRA). But because charities, by virtue of the donation tax credit, can reduce the tax base, the CRA's regulating them conflicts with its mandate to protect the tax base.

The CRA is the regulator of charities by the happenstance of history and the absence of action by the provinces to assert their constitutional power in this area. The result is a regulatory environment that is costly for charities, stymies the development of new charities, and injects tax bureaucrats into the arena of social policymaking.

This *Commentary* proposes reforming the system through the creation of a federal-provincial "Canadian Charities Council" that would assume from the CRA responsibility for registering charities, advancing the common law definition of charity, regulating non-tax-related aspects of the charity system, adjudicating disputes regarding a charity's registration, and ensuring compliance with the rules the Council creates. Involving the provinces, as the Constitution intended, and encouraging their cooperation with the federal government can only benefit the regulation of Canada's charitable sector.

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INDEPENDENT • REASONED • RELEVANT

As the size and complexity of Canada's taxation regime have grown, so too has the role of the tax collection bureaucracy. For the Canada Revenue Agency (CRA), this expansion has had unforeseen consequences for its administration of non-taxable entities.

The CRA now finds itself with a conflicting mandate: to protect the tax base while regulating charities that subtract from the base because of the donation tax credit.[1] This structure arose for legal and historical reasons as the unintended result of interplay among the Constitution, Parliament's desire to protect the integrity of the donation tax credit system, and the general lack of regulation in the sector. Over time, as the lack of sector regulation became a greater cause for public concern, the CRA stepped in as the de facto regulator of charities in the public interest.

The current registration system and the tax authorities that administer it are ill suited to regulate charities. In addition, as the federal government lacks the jurisdiction to regulate the sector properly, charities must work in a system that is forced to do a job for which it was not designed, its components added in response to particular pressures. The better way is a comprehensive and flexible system that proactively involves the provinces and that is enforced by a government agency with the expertise for such work. Assuming Canadians wish to nurture and grow the charitable sector, the need for a regulatory system with vision, a well-trained workforce, and a well-defined mandate in which charities are not simply a tangential offshoot, should be obvious.

The origins of the current situation can be traced back to the *Constitution Act, 1867,*[2] which grants authority for the regulation of charities to the provinces. Thus, the federal government has been unable to set up either a legislative regime or an administrative process with which to regulate the sector directly. The provinces, however, generally have not exercised their authority, leaving the federal government, through the CRA, to enter the field by requiring that charities comply with certain requirements for registration under the *Income Tax Act* (ITA)[3] – requirements that likely would be unconstitutional if enacted as a separate regulation regime. Thus, as a technical matter, the federal government's registration system is understood not to be an infringement upon provincial powers because it is a function of the income tax system's registration mechanism, rather than outright regulation. Although the provinces have not objected to this incursion, the regime's legitimacy is impaired by their lack of input into the federal government's regulatory attempts. For charities, the situation has led to mounting discontent with the current system's institutional focus.[4]

This discontent is multifaceted. One major area of concern is with how the common law definition of "charity" is stagnating. Some question the need for evolution at all, but such a view ignores the role that charities now play in confronting the world's ills. The definition must evolve to allow new charities to be created that can meet the challenges as they arise.[5] The current stagnation problems with the definition of charity and the reliance on the common law to evolve that definition have been the subject of many scholarly pieces. Recognizing the issue, the CRA has taken upon itself the role of evolving the definition through the use of administrative policies. Nevertheless, it is clear that the definition of charity is a legal question, and

The author wishes to thank and acknowledge Arthur B.C. Drache Q.C. C.M. for his insight and the benefit of his experience in preparing this paper, and Professor Richard Jochelson of the University of Manitoba for his comments with respect to the constitutional elements of this paper. Of course, any errors are solely the responsibility of the author.

1 Under the *Income Tax Act* only individual donors are eligible for a credit while corporate donors receive a deduction. As the net effect on the tax base is the same (although to varying degrees), I do not distinguish between them and refer to them collectively as the donation tax credit.

2 (U.K.), 30 & 31 Vict., c.3, s. 92(7) reprinted in R.S.C. 1985, App. II., No. 5.

3 R.S.C. 1985 (5th Supp.), c.1.

4 Over the years, a series of articles in the *Canadian Not for Profit News* has reflected this mood.

5 Before her elevation to the Supreme Court of Canada, Bertha Wilson wrote that it was crucial that we "become sensitive to the role of private philanthropy in the drive for social progress" (Wilson [1972] "By Way of Introduction" … 1997, 5).

should not to be decided by administrative policy by an organization whose jurisdiction to do so is questionable. Thus, while not originally a problem of the registration system, the definitional issue has become part of it. And leaving aside questions about the solution to the definition problem, there is a major issue regarding the involvement of the CRA in the process of charity regulation which deserves further scrutiny. Other areas of dissatisfaction stem from the fundamental problem that arises when the CRA, as the administrator of fiscal policy, attempts to regulate charities which are effectively creatures of social policy. When the agency goes beyond its general mandate and seeks, for example, to determine the appropriate level of political involvement by charities, or the definition of "religion," or whether a charity's activities are effectively fulfilling its purpose, the agency exceeds its design and the implementation of the charitible agenda becomes frustrated.

This frustration with the regulator and the general regulatory regime has been recognized in several high-profile reports. The most notable of these were published in the 1990s after two sets of public consultations: the Broadbent Report (Broadbent 1999) and the report of the Joint Regulatory Table (1999), part of the Voluntary Sector Initiative, and two reports commissioned by the Department of Canadian Heritage and the Kahanoff Foundation (Drache and Boyle 1998; Drache and Hunter 2000).[6] All of these projects concluded that – indeed, some began with – the principle that Canada's current system for administering charities was untenable and that change was necessary.

There would be ample reason to re-examine the regime in any case, even in the absence of discontent with the CRA's administration of the sector. From the constitutional perspective, any system in which the federal government plays the predominant role in charity regulation is less than wholly legitimate.[7] More important, the Constitution's limits on the federal government's ability to regulate the sector properly ill serves Canadians as the charitable sector grows in size and influence.[8] What is needed is a new regulator that provides a stronger framework for the development of new charities, that regulates charities through a comprehensive regime, and that resolves disputes in a way that serves both the interests of justice and the welfare of the sector and that of the public it serves.

Ultimately, however, short of a constitutional amendment, these concerns can be addressed only by convincing the provinces to exercise their jurisdiction and – as a harmonized system of rules is clearly in the interests of Canadians – to act in a coordinated manner. One approach to this end would be for the federal government to bring the provinces to the table in a joint federal-provincial charity council that would assume responsibility for registering charities. Such a council would advance the common law definition of charity, regulate non-tax-related aspects of the charity system, adjudicate disputes over a charity's qualifications for registration, and ensure compliance with the council's rules. The CRA would retain jurisdiction over the tax components of operating as a charity – most notably, the receipting of charitable gifts. The goal is a system where governments enact laws to directly create results and bureaucratic mechanisms to enforce them are dedicated to that purpose.

Background

Constitutional Authority

Canada inherited its charity law system from the United Kingdom upon the promulgation of the *British North America Act* (now the *Constitution Act, 1867*). The Act itself provides that:

6 In the interest of full disclosure, it should be noted that Arthur Drache has reviewed this paper and that the author is associated with Mr. Drache at the law firm of Drache – Tax, Estates & Charity Law.

7 I argue later in this paper, however, that the federal government might indeed have some jurisdiction over charities that operate interprovincially.

8 According to Statistics Canada, the voluntary sector is made up of approximately 81,000 non-profit organizations, 83,000 registered charities, and 73,000 small grassroots organizations. Total assets of registered charities alone are in the billions of dollars.

> In each Province the Legislature may exclusively make Laws in relation to Matters coming within the Classes of Subjects next hereinafter enumerated; that is to say,
>
> 7. The Establishment, Maintenance, and Management of Hospitals, Asylums, Charities, and Eleemosynary[9] Institutions in and for the Province, other than Marine Hospitals.

At Confederation, there was neither an income tax credit nor deduction for donations to charity. Indeed, there was no income tax, and so the main effect of this clause was to devolve to provincial attorneys general the Crown's traditional role of protecting charitable property. Included in this role was the general duty to determine what qualified as charitable and, if necessary, to regulate the sector. On the other hand, constitutional authority to levy an income tax is part of the shared federal and provincial jurisdiction. Thus, the federal government has authority to register organizations that qualify as charities for special tax benefits under the ITA. As a matter of practicality, most provinces have delegated the collection of their portion of the income tax to the federal government. Since the two levels of government share this power, there is no legal issue with the delegation of the collection power from one level. The same is not true of the charity regulation power, however, so the federal government's ostensible regulation of charities is exceptional and should be re-examined.[10]

Development of the ITA

Canada's first income tax act, the *Income War Tax Act, 1917,*[11] included both an exemption from income tax and a deduction for donations by taxpayers to certain wartime charities. This deduction was later changed to a tax credit and expanded to include all charities. The term "charity" was never defined in the statute, however, but left to the common law.[12] In fact, during the parliamentary debates in 1930 over the genesis of the current donation tax credit system, opposition parties were resolute in their resistance to the federal government's having the discretion to determine which charities were eligible for preferential treatment.[13] This left the definition, as it is today, with the common law.

Taken together with the ability to create new charities at will, the tax deduction system at the time stood open to abuse by taxpayers' claims for donations to causes whose charitable nature (or existence) was doubtful. In 1967, in an attempt to stymie such abuse, the system was changed so that only donations to organizations registered as charities with the federal government (and necessarily approved by it) could qualify for the preferential tax treatment (see Drache, Hayhoe, and Stevens 2007). The provinces, meanwhile, had made little effort to exert their constitutional authority and legislate a definition of "charity" or otherwise regulate the sector. Had they done so, the federal provision to register charities might have been unnecessary; in the absence of movement on their part, the federal government seized the opportunity to provide the framework under which charities would come to be regulated.

9 Of, relating to, or supported by charity.

10 The CRA itself notes that, although it has no real jurisdiction to regulate fundraising, it will take account of "inappropriate" fundraising in determining a charity's registered status (Canada 2009c, 2). In this way, the CRA is assuming the role of regulator of charities in the public interest despite the limited tools and jurisdiction at its disposal.

11 (Can.), 7-8 Geo. 5, c.28.

12 The ITA also studiously avoids defining "charity." The Supreme Court of Canada has noted that lack of a legislated definition of "charity" is not accidental: "[T]he fact that the ITA does not define 'charitable,' leaving it instead to the tests enunciated by the common law, indicates the desire of Parliament to limit the class of charitable organizations to the relatively restrictive categories available under the landmark Pemsel case which serves as the foundation of modern charity law and the subsequent case law. This can be seen as reflecting the preferred tax policy" (*Vancouver Society of Immigrant and Visible Minority Women v M.N.R.,* [1999] 1 S.C.R. 10).

13 *House of Commons Debates* (1930) 16th Parliament, 4th Session, Vol. III, Sess. 2513-19.

Decisions and Disputes

THE CHARITIES DIRECTORATE: As the ITA is by far the largest single source of codified charity law in Canada – and the CRA is the administrator of the ITA, the CRA has become by default the regulator of the entire charitable sector. Indeed, the CRA states quite openly that it is the "regulator of registered charities in Canada" (Canada 2008). The branch of the CRA tasked with enforcing the provisions of the ITA pertaining to charity regulation is the Charities Directorate (see Figure 1). Since the imposition of the registration system in 1967, the federal government has legislated a significant regulatory regime that goes well beyond simple registration of charities to include such areas as political advocacy,[14] charitable disbursements,[15] fundraising activities,[16] and even whether specific practices qualify as religion.[17] Indeed, some of the CRA's administrative efforts border on social engineering.[18] Thus, the Directorate has grown from simply registering charities to playing a large role in the development of the charities sector. This is encompassed in the mission statement the Directorate has chosen for itself: "Our mission is to promote compliance with the income tax legislation and regulations relating to charities through education, quality service, and responsible enforcement, thereby contributing to the integrity of the charitable sector and the social well-being of Canadians" (Canada 2009a).

There are, however, major structural problems with continuing to allow the Directorate, as a branch of the CRA, to administer the charities sector.[19] To begin with, there is a direct and obvious conflict of interest created when the organization responsible for maintaining the integrity of the national tax base is also responsible for registering and policing non-taxable entities that are capable of detracting from the tax base. This conflict was recognized explicitly in the Broadbent Report in the context of the registration of new charities: "Revenue Canada, by most accounts, has tended to be restrictive in its use of the concept, as one would expect of a tax-raising department" (Broadbent 1999, 70).[20] More generally, as protector of the tax base, the CRA has a direct incentive to stymie the development of new charitable areas.

The institutional conflict of interest has practical implications that affect charities when the CRA uses the Directorate to target charities involved in tax practices of which the CRA disapproves.[21] For example, the Directorate has threatened to revoke charitable registrations for improper T4 issuance, when other penalties exist for this express purpose.[22] More publicly, it has targeted charities that accept donations as part of aggressive tax sheltering, regardless of the severity of wrongdoing on the part of the charities.[23] Another example is the *Redeemer Foundation* case,[24] where the Directorate used the audit of a charity to obtain a list of donors in order to issue reassessments against them.

14 One CRA document notes that it "seeks to clarify the extent to which charities can usefully contribute to the development of public policy under the existing law" (Canada 2003).

15 See, for example, Canada (1998).

16 See, for example, Canada (2009c).

17 See, for, example Canada (2002), where the CRA must decide if a given belief system qualifies as a religion.

18 See, for example, Canada (2005, 2009b) and a soon-to-be-released CRA consultation paper on the definition of religion.

19 One should note that the Directorate is not a legally established entity and has no separate mandate or purpose from that of the CRA. See *Canada Revenue Agency Act,* S.C. 1999, c.17, ss. 5(1).

20 This view was originally voiced in the report of the Royal Commission on Taxation (Canada 1966, 132).

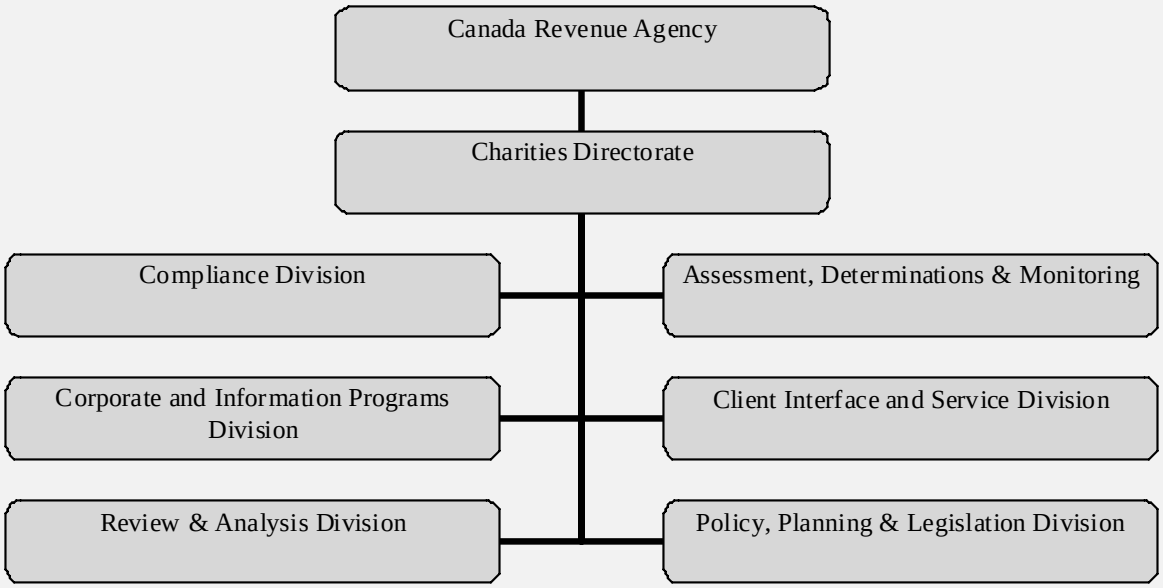
21 The propriety of this strategy must be divorced from the propriety of the plans being targeted. For a sense of this strategy, see Canada (2000b).

22 Indeed, auditors are directed to review these transactions during audits of charities' operations – see Technical Operations Manual 1454.2(10), available through Access to Information. Findings of such improper use, however, should not lead to revocation.

23 See, for example, Canada (2009d), which warns about receiving inflated receipts from charities.

24 *Redeemer Foundation v Canada (National Revenue)*, 2008 SCC 46.

Figure 1: Current Structure of the Charities Directorate



Source: Adapted from Canada 2009a.

The discussion of which practices are appropriate for the CRA to use in enforcing the ITA against charities is reflective of the general questions about the mandate of the Charities Directorate. Many in the sector believe that the Directorate's purpose should be to promote the interests of charities and the work they do – indeed, the Directorate encourages this view – but how can a body protect and nurture the charitable sector while enforcing the ITA and protecting the tax base? Few Canadians would argue with the importance of nurturing the charitable sector. Moreover, this laudable goal is within reach, as both the Broadbent Report and the Joint Regulatory Table have shown, but it requires separating the charity regulation role from the ITA enforcement role in a concrete and formal fashion.

Perhaps obviously, regulation of the charitable sector requires knowledge, training and experience particular to this area. It is unrealistic and unfair to expect Directorate officials hired by the CRA, and who must generally fill positions related to collecting taxes, to have the requisite skills to regulate charities. This is particularly true as CRA employees tend to move between different CRA departments with some frequency, if for no other reason than career advancement. Thus, assignment to the Directorate can be career limiting and, unless the individual has a strong commitment to the charitable sector, he or she will be obliged to leave the Directorate for greater career options. To some degree this situation exists in all large organizations but the incentive to leave the Directorate has created a dearth of very senior charity law professionals within the Directorate.

Perhaps of more concern is that Directorate employees are responsible for social policy decision-making because of their ostensible power to regulate the sector. Canadians should be thankful that the Directorate takes the job seriously, but it is entirely inappropriate for the taxing authority to turn its collective mind to (among other things) the definition of religion, the charitable nature of amateur sport, or whether a charity has engaged in

political activity or advocated a "controversial" subject.[25] The Broadbent Report recognized the same problem in the context of the political advocacy rules:

> It is up to the discretion of Revenue Canada to determine which political activities are considered acceptable and whether permissible levels of activity have been exceeded. A 1998 decision by the Federal Court of Appeal in the *Human Life International* case has further restricted the definition of permissible advocacy activity, however, by stating that "activities designed essentially to sway public opinion on a controversial social issue are not charitable but are political." This interpretation gives even greater discretion to Revenue Canada because it will define what is a controversial social issue and potentially further control advocacy activities....
>
> Given that public policy advocacy is closely linked to the core mission of many voluntary organizations, it may seem strange to address issues of advocacy in the context of the regulation of financial management. Advocacy is regulated, however, by limiting the amount of an organization's resources that can be spent on it.…In our view, the ten percent rule is badly formulated, poorly understood and potentially highly arbitrary in its application by Revenue Canada. An inappropriate political burden is placed on tax officials. (Broadbent 1999, 86-87.)

The application of non-tax decisions should be reserved for elected officials and for public servants with specific expertise and delegated authority in the area. Do we really want unelected tax bureaucrats to be responsible for such social decisions?[26]

THE APPEALS BRANCH: In 2005, the Charities Redress Section (CRS) of the Appeals Branch was opened to provide a review of Directorate decisions upon application by a charity or proposed charity. The CRS is meant to be staffed by individuals versed in the mechanics of charity law and able to take a sober second look at a file before it proceeds to court. Given its relative newness, however, it is difficult to assess the branch's operations. Nevertheless, its structure and place within the CRA framework raise many of the same doubts that are expressed about the Directorate, such as the qualifications of tax officials to make charity law and social policy decisions and the independence of the branch from the greater pressures of the CRA's larger role as protector of the tax base. Indeed, the mandate of the Charities Redress Section is to assess whether Directorate decisions conform to general CRA policy.

THE FEDERAL COURT OF APPEAL: While the Constitution originally mandated that disputes over charity issues be heard in the provincial courts, the effective takeover of the area by the ITA has redirected the hearing of these types of cases through an ill-adapted version of the dispute resolution system used by private taxpayers. If the CRS confirms a Directorate decision, the charity can appeal the confirmation to the court level. Appeals of decisions regarding registration, revocation, or annulment proceed directly to the Federal Court of Appeal (FCA), (as opposed to a lower division of the federal court system), whereas appeals of decisions regarding so-called intermediate sanctions proceed to the Tax Court of Canada.

The FCA's jurisdiction is generally to hear matters involving the federal government at the appellate level. As registration of charities was included in the federal ITA, it was inevitable that the FCA would become the country's most important court for charities (as opposed to the Supreme Court of Canada, which picks the cases it hears). This is unfortunate, for three reasons. First, the FCA is designed to be an appellate-level court, meaning that no oral testimony is heard and all evidence is presented in the form of written documentation, so that litigants who do not retain experienced representation until late in the dispute resolution process – or at all – often have a file that is not documented properly. Second, it can be particularly difficult to present the charitable nature of an

25 Religious charities were so concerned about CRA activism in the social arena that they prevailed upon Parliament to include a provision in the ITA that charities could not be deregistered for refusing to perform same-sex marriages. See R.S.C. 1985 (5th Supp.), c.1., ss.149.1(6.21).

26 Moreover, the potential for misuse and bias abounds, as the CRA itself has admitted; see, for example, Canada (1999).

organization without oral testimony – think of the difficulty of proving that a soup kitchen is charitable on the basis of documents alone. Finally, the FCA is simply not user friendly for a small local charity that lacks the funds to appeal to what some regard as the second-highest court in the land.[27]

It is somewhat unusual that the FCA is the court of first instance – that is, the first level of court to hear a matter – for appeals of CRA decisions regarding registration, revocation, and annulment of charitable status. It is apparently a result of Parliament's belief that appeals of CRA decisions were similar to appeals of other administrative bodies – such as the Competition Tribunal, the Canadian Radio-television and Telecommunications Commission, and the Canadian Transportation Agency – that deal primarily with factual matters decided by experts and that also go directly to the FCA. As a matter of principle, however, the FCA tends to grant a degree of deference to such tribunals, on the basis that Parliament has a policy reason for appointing experts, rather than judges, to sit on them.[28] This is not to say that the FCA simply rubber stamps Directorate decisions, but that Directorate decisions are subjected to a standard of reasonableness rather than the stricter standard of correctness.[29] This attitude of deference seems to have been extended to CRA decisions on charity law matters, even though the CRA is accorded no such deference with respect to general tax matters (see Chan 2008) and its rulings on the registration of charities are *prima facie* matters of law rather than of fact. The combined effect of a court that does not hear oral testimony and a generally deferential attitude to CRA findings is a barrier that any charity would find difficult to overcome.

Involving the Provinces

The constitutional limitation on the federal government's involvement in the charitable area has forced it to disguise its regulation of the area as conditions of registration.[30] Unfortunately, the ITA is limited in how far it reasonably can be stretched to encompass regulation under the rubric of registration, in two ways. First, it is often too blunt a tool to use on topics that require a detailed set of rules – on the undertaking of political activities, for example, the *Income Tax Act* contains only broad constructs.[31] Second, not every offence can be codified as a regulation of a charity. For example, the current rules punish charities whose directors misuse charitable property. As a matter of justice, it is the guilty parties (the directors) who should be punished, not the victim (the charity), but punishing directors is clearly a provincial power and cannot be dealt with as part of the registration system.

Although provincial abdication of the charity sphere led to the current federal regulation, inertia itself is now a disincentive for the provinces to assert their jurisdiction.[32] After all, if the federal government is legislating in the area, why should the provinces bother, particularly as it does not bring in any additional tax revenue? Such a view is, however, short sighted: charities might not bring in revenue but they certainly redirect revenue away from provincial coffers and take on social functions that would have otherwise have fallen to the provinces. More important, since charities that provide supplemental funding in areas of provincial responsibility, such as health and education, receive a disproportionately large share of government funding (see Table 1), there should be sufficient incentive to ensure their proper regulation and growth. As well, since the federal government's retention of sole

27 Unlike the FCA, some courts have relaxed rules of evidence and allow self-represented litigants. Moreover, as an appellate-level court, the FCA has rules of procedure that are arguably more complex and require a trained advocate to navigate successfully.

28 See *United Brotherhood of Carpenters and Joiners of America, Local 579 v Bradco Construction Ltd.,* 1993 CanLII 88 (S.C.C.), [1993] 2 S.C.R. 316, at p. 335, cited with approval in *Canada (Director of Investigation and Research) v Southam Inc.,* [1997] 1 S.C.R. 748, at para.50, for evidence of this situation.

29 See *Fuaran Foundation v Canada (Customs and Revenue Agency)* (2004), 10 E.T.R. (3d) 26 (FCA) and *Hostelling International Canada – Ontario East Region v MNR* 2008 FCA 396.

30 For some recognition of this by the CRA, see Canada (2009c).

31 See R.S.C. 1985 (5th Supp.), c.1., ss 149.1(6.1) and (6.2).

32 Attempts to involve the provinces in charity governance are not new. Plans were announced in 2000 to ask each province to appoint a representative to a board of management; the plan failed but it is not clear why. See Canada (2000a).

Table 1: Total Charity Revenue by Government Source, 2003

Sources of Revenue	Arts and Culture	Education and Research	Universities and Colleges	Health	Hospital	Social Services	Environment
				(percent)			
Federal government payments and grants	8	18	8	8	0	5	9
Provincial government payments and grants	13	27	48	60	81	51	9

Source: Statistics Canada 2004.

discretion to register such organizations gives it a significant degree of control over the spending of their funds, it would be appropriate for the provinces to assume a greater role in determining how the funds are spent.

The jurisdiction of provincial attorneys general over charities initially arose from their responsibility to protect charitable property. This duty exists to this day, even though the provinces, with the exception of Ontario and relatively minor enactments elsewhere, are almost wholly absent from the field. The ITA, however, places the CRA in the exact opposite position to this duty of the Crown in that its fines, which are part of the Act's "intermediate sanctions," effectively attack a charity's property. Given that the CRA has assumed for itself the mantle of regulator of charities in the public interest, it is singularly incongruous that the ITA should force it to seize charitable property to satisfy a punishment in this manner.

CURRENT PROVINCIAL INVOLVEMENT: Although regulation of charities is clearly within their jurisdiction, the provinces – with Ontario as a notable exception – have abandoned any serious regulation of charitable operations.[33] Piecemeal statutes, however, govern a variety of smaller issues. So, for example, while no significant statutes detail appropriate charities' administration costs, spending requirements, political activities, or extraprovincial operations, the provinces generally provide limited direction on issues such as fundraising, telemarketing, and property taxes. Some provinces also have more specific rules on extraprovincial fundraising. Quebec, as usual, asserts its jurisdiction in this area, an exercise that merely mirrors the rules of the ITA rather than any particular Quebec policy towards charities.

The notable exception among the provinces is Ontario, which has passed several laws relating to charities,[34] and the Office of the Public Trustee has authority to oversee the charity regime. It also enforces the common law fiduciary responsibilities of directors – duties that are applicable to directors in every province but that only Ontario makes any serious attempt to enforce.[35] Ironically, given the inactivity of most provinces, a degree of efficiency has been achieved in the regulation of the sector in that national charities have not been forced to comply with different regulatory regimes in each province. Nevertheless, the fact that charities would have to comply with provincial regulations cannot serve as a reason not to enact any; even if the result would be a different charity regime in each province, it arguably would be more beneficial to the sector than is the current situation.

33 The provincial tax deduction/credit for donations is not part of the scheme to regulate charities.

34 Notably the *Charities Accounting Act,* R.S.O. 1990, c. C.10.

35 To be fair, the Office of the Public Trustee has exercised this power in relatively few instances.

Policy Justifications of the Current System

The regime for regulating charities in Canada is, in large part, a result of the attempt to address various policy concerns that have arisen from time to time regarding the sector.[36] These additions have been forced into a system of fundamental tension between the desire to have a standardized system of regulation for charities across the country and the constitutional impediments to such a system. Indeed, as Bob Wyatt[37] notes, "the lack of development of charity law is, at once, complex and entirely simple. The complexity comes from a regulatory environment developed to fit a dysfunctional constitutional and legal arrangement for the supervision and regulation of charities" (Wyatt 2009).

Thus, a major policy justification for the current regime is that, with various degrees of efficiency, it has solved many of the problems that once beset the sector. While a single, standardized set of rules was never a direct aim of the system, it is surely more efficient than having a separate regulatory regime in each province, and it is a powerful reason to involve the federal government as the unifying factor in any future regulatory regime change. Indeed, provincial inaction has avoided the kinds of problems corporations face in, say, securities regulation, where complying with a separate regime in each province can be expensive, onerous, and time consuming. In the case of charities, one could imagine that having a differing regime in each province might result in either the diminution of national charities into provincial ones or the outright flouting of provincial laws.

Past Proposals for Reform

The Broadbent Report, while recognizing some of these problems, limited itself to recommendations on specific policy changes that would benefit charities without changing the regime that currently exists. This relatively tame suggestion was likely a product of several factors. As the report scarcely mentions constitutional difficulties, it is likely they were seen as insurmountable,[38] and the recommendations basically preserve the status quo with the exception of the charitable definition (albeit with the call for a new agency to educate and encourage compliance).[39] With respect to the definitional issue, the report suggests that Parliament should legislate an all-encompassing definition rather than rely on the Directorate and the courts to do so.[40]

The Joint Regulatory Table's final recommendations also attempted to address many of the same problems, but remained within the current structural status quo. For example, it suggested that policy guidelines be constructed regarding the regulator's ability to extend the common law; that the regulator encourage the provinces to make appropriate legislative change and to coordinate with Ottawa; and that the federal

36 For example, the registration system originally was implemented to curtail abuses arising from the donations to groups that simply assumed the title of "charity."

37 Bob Wyatt is executive director of the Muttart Foundation, an organization dedicated to improving operations in the charity sector; he was also the co-chair of the Joint Regulatory Table.

38 Miller (1999) criticizes the report as nothing more than a way for the sector to attempt to re-establish the confidence of the public in its regulation without undertaking fundamental reform.

39 When the Broadbent Report was first circulated for comment, it contained three suggestions for a new regulatory regime, so clearly the idea had some support even ten years ago. Since then, history has served only to strengthen the saliency of this idea.

40 April, Clemens, and Francis (1999) strongly criticize the Broadbent Report's final recommendation, pointing out that the proposed Voluntary Sector Commission – essentially to advise the CRA and facilitate a better relationship between charities and the CRA – could be accomplished through better and more cost-effective means. They do suggest, however, that, it might be useful to have an independent body composed of people with legal expertise that could make recommendations to the CRA regarding the charitable definition or hear appeals of CRA decisions.

In 2002, the Canadian Centre for Philanthropy (now Imagine Canada) and the now-defunct IMPACS (Institute for Media, Policy, and Civil Society) launched an unsuccessful campaign to change the definition of charity-related political activities; see IMPACS and Canadian Centre for Philanthropy (2002).

minister should work with the appropriate provincial ministers. It also proposed importing some of the practices of the British Charities Commission.[41] Without addressing the constitutional question, however, such recommendations can only go so far in improving the regulatory system.

Two reports commissioned by the Department of Canadian Heritage and the Kahanoff Foundation (Drache 1998; Drache and Hunter 2000), while explicitly recognizing the constitutional difficulties, limited their recommendations to the role of the Directorate (and the court) in defining charity in Canada. In resolving this part of the problem, Drache (1998) suggested creating a specialized charity body with two parts, one to register new charities and the other to serve as a tribunal to adjudicate disputes over registration. A board of registrars would be responsible for qualifying applicants as charities, and those denied registration could appeal to the tribunal, which would hear submissions from the rejected applicant and any other interested parties (including the CRA), while the registrar itself would appear in the nature of *amicus curaie* (a friend of the court). Further appeals would take place in the Tax Court, which would be entitled to hear oral evidence on the issue.

The *Report on the Law of Charities* by the Ontario Law Reform Commission (1996) explicitly cited the British Charity Commission as an excellent model but lamented its impossibility in Canada due to the constitutional difficulties. In the opinion of the Law Reform Commission, it would have required a charity body in each province and instead endorsed change only at the federal level. However, the Ontario Commission recognized that such changes could make the entire charitable registration scheme a function of tax considerations (and bifurcate the charitable definition along federal-provincial lines) but suggested that both risks could be managed.

Another paper, written by Monahan and Roth (2000), noted that the Commission failed to consider a quasi-judicial agency composed of federal and provincial components. While they felt that a body in which the provinces delegated their authority over charities would likely be ideal, it was not politically viable. Instead, they proposed a narrowly construed organization which was only responsible for an initial decision as to the charitable nature of an applicant.

A Canadian Charities Council: A Fresh Approach to Reform

It is clear that the need for change in the sector is understood. Unfortunately, the constitutional difficulties seem to have stymied any momentum for meaningful reform. Perhaps momentum could be developed with a fresh approach to the constitutional impediment.

Overall Philosophy

It should be understood that despite the widespread desire for change within the sector, the initial policy considerations that led to the current system still exist and should therefore be taken into account in the design of a new system. Thus, any new model should include a registration system and a harmonized set of rules for charities across the country, yet address the jurisdictional issues, the disguise of a regulatory system as a registration system, and the entrusting of the charity system to the tax administration. And importantly, a new adjudication process should be developed for disputes over what qualifies as a charity. Furthermore, it is equally clear that the new system must evolve so that charity regulation in Canada is more comprehensive and flexible, not limited to the ITA, and administered by a body dedicated to that

41 The Ontario Law Reform Commission (1996) also cited the British Charity Commission as an excellent model but lamented its impossibility in Canada due to constitutional difficulties, holding that a different charity body would be required in each province. Instead, the Commission endorsed change only at the federal level. It recognized that such changes could make the entire charitable registration scheme a function of tax considerations (and bifurcate the charitable definition along federal-provincial lines) but suggested that both risks could be managed.

mission. It is assumed that the charitable donation tax credit/deduction system and its receipting corollaries would remain within the ITA and be administered by the CRA, but that the regulation of charities should take place by a new organization under a different statutory regime.

Constitutional Jurisdiction

Although resolutions to the current situation have been suggested periodically by those in the sector, the constitutional problem seems to have stymied creativity when designing a potential new system. It is clear, then, that no fundamental changes can take place in regulating the sector without some solution to the underlying constitutional question.

The most obvious answer would be a constitutional amendment authorizing the federal government to exercise properly the jurisdiction it already ostensibly exercises. Although such an amendment, in and of itself, is only minimally controversial – coming as it does in an area in which the provinces do not exert even the jurisdiction they have – the acrimonious constitutional debates of the Mulroney era have made any possibility of an amendment unlikely.

Nevertheless, it bears pointing out that section 94a was added to the *Constitution Act, 1867* in order to include disability and survivor benefits in the federal pension plan, and although the *Canada Pension Plan Act* contains a variety of complex provisions that allow the provinces to opt out and create their own pension plans, the fact that a constitutional amendment was created – albeit in the 1960s – might give some hope to those in a position to test the waters for such a change. That being said, in view of the importance of charities in delivering provincial services, the federal government's assumption of constitutional jurisdiction to the exclusion of the provinces would not be desirable, even if it were possible.

Some in the charitable sector look to the creation of a national securities commission for guidance, but one should note that the federal government posits that it has shared jurisdiction over this area, based on the trade and commerce provision of the Constitution. Although the report of the Expert Panel on Securities Regulation (2009),[42] and the coming reference to the Supreme Court will be of some interest to the charitable sector, unfortunately the Constitution contains no analogy of the trade and commerce provision relevant to charities.

Could the provinces not simply delegate their powers to the federal government in order to facilitate regulation of the charitable sector? Unfortunately, the Supreme Court of Canada ruled such delegation unconstitutional in a case involving Nova Scotia in 1951.[43] The Constitution, in its division of powers section, gives the responsibility for charities to the provinces, stating that the "Province may exclusively make laws in relation to…Charities, and Eleemosynary Institutions in and for the Province." It could be argued, therefore, that a province is limited to the regulation of a charity so long as the activity involved falls exclusively within the province, but that interprovincial regulation is beyond its jurisdiction. Necessarily, the jurisdiction to regulate the interprovincial activity of charities should fall within the powers of the federal government. Moreover, this would fit within the general scheme of the Constitution, which gives jurisdiction over issues affecting more than one province to the federal government. Of course, if the regulation of national charities were accepted by the provinces (or the courts) as within the federal government's jurisdiction, there would remain the question of how to regulate charities that operate only within one province. I offer a solution to this potential problem below, but in the age of the Internet the problem might prove more theoretical than practical – it is hard to imagine a charity that does not remain at least open to donations from, if not actually conducting operations in, more than one province.

Thus, the federal government arguably does have some authority to regulate the sector outside of its

42 Chaired by Tom Hockin, former federal minister of finance under Brian Mulroney, the panel was commissioned to explore the possibility of a national securities regulator.

43 *Nova Scotia (A.G.) v Canada (A.G.),* [1951] S.C.R. 31. In this case, the province would have had to delegate certain powers regarding employment to the federal Parliament and certain taxation powers would be delegated from the federal government to the province to create an unemployment insurance plan.

power to register charities. Although use of this power would mean efficient, federal regulation for national charities, without provincial cooperation there would be no new system for those charities that operate exclusively within one province. Different methods of cooperation are possible, but they ultimately would involve some type of mirroring of the federal regulations to ensure a standardized set of laws for charities across the country.

As the federal government's jurisdiction to govern the sector rests on shaky legal ground, perhaps the most viable option in terms of creating a standardized set of charity regulations is a hybrid system, in which charity regulation and registration would be the responsibility of a new joint federal-provincial body, but the tax provisions would be retained in the ITA. All but the registration provisions in the ITA would be repealed, and registration under the ITA would be both contingent and automatic upon registration as a charity by, a "Canadian Charities Council" composed of representatives of each province and the federal government.

This Council would be structurally similar to the CRA's Board of Management. The CRA Board of Management oversees the organization and management of the CRA and sets out policies related to resources, services, property, personnel, and contracts.[44] This Board is composed of 15 members appointed by the federal cabinet but 11 of whom are nominated by the provinces. Most of these representatives are from the private sector. Notably, while the Board is answerable to Parliament through the Minister of National Revenue (although see below for our comments on this point in respect of a charity council), it has no access to confidential taxpayer information and is not involved in the actual application of the ITA or its policies. Similarly, the Council here would not be involved in individual cases but would oversee the public service machinery necessary to properly administer the sector.

Such a Council would require each province to pass legislation investing the Council with the authority now invested in the provincial attorneys general to regulate charities in their province.

In return, each province would be entitled to appoint a representative to the Council at its discretion. It is anticipated that the province would choose an appointee from the charitable sector and in this way the input of the sector could be solicited while maintaining provincial participation.

Finally, given the often overwhelming importance of front line experience in regulating the sector, the federal government should retain the authority to appoint at least one representative of the sector to the Council.[45] It should be noted that while the Council would not involve itself in individual cases, the authority to do so would devolve from the participation by the provinces on the Council. Thus, the references below to the 'Council' should be taken as references to the Council in its jurisdictional capacity but not necessarily the actual council of representatives.

The provincial delegation of authority to the Council, would not breach the Supreme Court's ruling in the Nova Scotia case, as the provinces would be delegating, not to the federal government, but to an independent council. As Monahan and Roth note: "Of course, it would be theoretically possible for the Provinces to delegate their jurisdiction over charities to a national charity commission. If this were a practical possibility, there would be a strong case in favour of transferring to such an agency the entire Federal jurisdiction over charities as well, including the power to make the initial determination on application for registration" (2000, 11).

The Council could operate so that any province that did not want to participate would not be required to do so. However, since registration under the ITA would be contingent on registration by the Council, and as the Council could not register charities in a non-participating province, charities in an uncooperative province would not be registered for federal income tax

44 Taken from http://www.cra-arc.gc.ca/gncy/brd/rls-eng.html

45 Of course, in addition to formal involvement, input from the sector can always be sought and may well occur on an ad hoc basis given that different situations may involve different sensitivities or regional issues.

purposes. While somewhat heavy handed, this should be sufficient incentive to induce provincial participation; it also has the merit of being an attractive argument from a technical point of view.[46] Moreover it would help standardize the definition of charity across the provinces,[47] encourage a national standard in charity regulation, harmonize the administration of the sector over the entire country, and provide greater legitimacy for regulatory laws than currently exists. Of course, if none of the provinces opted in (or if they quit the Council *en masse*), Parliament would always retain the right to reintroduce legislation in the ITA as a requirement of registration. Clearly, this worst-case (and current) scenario would happen only if the provinces made a concerted effort to avoid exerting the constitutional authority they already have.

Aside from shouldering their constitutional responsibility in this sector, however, the provinces should be motivated to become involved because of their interest in ensuring that charities, which perform so many duties that would otherwise add to the financial responsibility of provincial governments, are being created and administered properly. Furthermore, since, on every donation, each province (above a minimum threshold) foregoes tax revenue at generally equal to the highest marginal tax credit in that province, one would expect the provinces to want to ensure that such funds were spent properly.

The Need for Independence

A common theme of the Broadbent Report (1999), the Joint Regulatory Tables report (1999), and the papers by Drache (1998) and Drache and Hunter (2000) is that any new charity entity be "independent" – that is, free from government interference. As Drache and Hunter point out, there are two types of independence: accountability within our system of government, and independence in the manner in which appointments are made within a body such as the proposed Council.

With respect to the first type of independence, I essentially concur with Drache and Hunter – though their recommendation is solely in the context of a charity tribunal – that, ideally, the Council should not report to any minister but instead should issue an annual report to Parliament and (I would add) to the provincial legislatures.[48] Such independence would inoculate the Council from any government interference that might tend to push the administration of charities into the political realm, and it should allow the Council to handle politically difficult cases in an impartial manner.[49]

With respect to independence regarding appointments to the Council, this likely would be the subject of negotiation between the provinces and the federal government, but I expect that, ultimately, provinces would appoint their own representatives.

The Structure of the Council

The Council would be structured into three sections: one that deals exclusively with the definition of charity and the registration of new charities, a second that is devoted specifically to charity regulation and a third that is an internal tribunal.

46 Unfortunately, convincing the provinces to become involved might be difficult. Charities bring in no wealth, and the regulation of charities is simply not a politically hot topic, the occasional news report involving a high-profile charity notwithstanding. On the other hand, the provinces seem continually to miss the point that, although charities do detract from the provincial tax base, they assume responsibilities that would otherwise be left to provincial handling. Considering their lack of interest in seizing their jurisdiction in this area, the provinces would have a difficult time justifying opposition to a plan that would improve governance of the sector and involve only a limited commitment on their part. Even Ontario, the province with the greatest independent presence in the sector, could scarcely raise an objection to a plan to give its current infrastructure additional reach and power.

47 Technically, as the Constitution places charity regulation within provincial jurisdiction, it was intended that each province would define "charity" individually. Thus, unless steps are taken to harmonize definitions, left to the common law they could vary substantially among the provinces.

48 This model seems to be working well for the Canada Pension Plan Investment Board, which is statutorily required to report to the federal minister of finance and the appropriate provincial ministers. See *Canada Pension Plan Investment Board Act,* S.C. 1997, c. 40, s. 50.

49 There is a current perception that the Directorate does not have the political will to be seen revoking the charitable status of popular charities.

THE REGISTRATION SECTION: The purpose of the registration section of the proposed Council would be to approve the registration of charities and to consider novel extensions of the definition to new types of organizations, supported by legal precedents in Canada or other common law jurisdictions. The section could also be mandated to consider the broad social climate in which the proposed extension of the definition was being made. One imagines that, for the most part, this new division would operate in a similar manner as the current Directorate. In fact, if the proposed Council were established, the transfer of Directorate staff and operations responsible for regulations would likely be the appropriate first step in creating the registration section. As an entity distinct from the CRA, however, the new section would register or deregister organizations in accordance with the law and social policy, free from any of the tax authority's directives or policies. Moreover, as career advancement would not depend on a transfer from the Council, a wealth of experience might be created, nurtured, and sustained there for the benefit of the sector.

THE CHARITY REGULATION SECTION: The Council's second section would be mandated to promulgate the rules needed to regulate charities more generally. When removed from the context of the registration regime, rules on, for example, related business, political activity, and excess business holding likely would become more detailed and comprehensive, allowing for nuanced legislation and a variety of possible penalties for both the charity and its directors. Furthermore, the Council should pass rules that are not currently in the ITA to fulfill the provincial responsibility to protect charitable property and to provide national contiguity in rules relating to such issues as fundraising, telemarketing, operating during disasters, operating overseas, and other issues of concern.

Among other benefits, a charities regulation section would bestow a constitutional legitimacy on the Council's decisions that those of the CRA now lack. From a technical perspective, one would imagine that the Council would draft new regulations or policies – akin to the authoritative pronouncements of Ontario Securities Commission – and publish them to the sector. Compliance with these regulations would be a mandatory condition of registration with the Council – and therefore under the ITA as well. The Council presumably would employ a group of individuals to audit and enforce the rules and to work in conjunction with the provinces to monitor Canadian charities effectively. Ideally, the legislation currently contained in the ITA would be duplicated on a more comprehensive basis and supplemented with laws that, in fact, would assert provincial jurisdiction over the protection of charitable property. The Council would also have the added benefit of being able to take delicate, nuanced, and timely approaches to issues facing the sector.

THE INTERNAL TRIBUNAL SECTION: Applicants whose proposals for registration are rejected, or charities with regulation disputes, should be able to appeal the decision to an internal tribunal, a system that is being used with considerable success in England as part of the Charity Commission. As to the fundamentals of such a tribunal section, Drache and Hunter (2000, 14) note that "[t]he core to the concept of a Canadian charity Tribunal is that it would be in a position to interpret the common law (as does the English version) and any legislative initiatives from an independent perspective, rather than from within a framework that gives priority to the collection of taxes."

The tribunal should not act as a formal court body but be composed of specialized tribunal adjudicators with experience in law and the social context in which charities operate. Moreover, it should have the political authority to extend the common law definition of charity, rather than simply implementing CRA policy. In some ways, the tribunal would fall somewhere between the Charities Redress Section of the Appeals Branch process on the one hand and the Federal Court of Appeal on the other. Tribunal members could conduct hearings around the country, in a somewhat informal manner that allows self-represented applicants to use oral testimony and relaxed rules of evidence to present their case for charitable status. The tribunal could also hear from intervenors, including members of the public, the CRA, and the registration branch of the Council. As a matter of course, its decisions should be published.

Appeals of tribunal decisions should be returned to the provincial Superior Courts for a new hearing. These courts are well suited to expedite different types of litigation in a more cost-effective manner than the Federal Court of Appeal. Furthermore, in a lower court trial, a judge would be able to evaluate all the evidence, including oral evidence, rather than simply review the record. Provincial Superior Courts are already used for complex litigation and are familiar with the procedures and administration needed to handle these types of cases, especially within the related matters of trusts and estate litigation. It would also accomplish an objective of the Joint Regulatory Table (1999) by accelerating the speed at which case law is generated, which would be of benefit to all charities.[50]

Clearly, this would place an additional burden on provincial resources, but one might argue that it is hardly inappropriate given that returning charity litigation to the provincial courts is in keeping with the original intention of the Fathers of Confederation. Indeed, as the Council would act with the authority of the provincial attorneys general, it would be entirely appropriate to refer disputes to the provincial courts. Moreover, as the Council would be responsible for implementing a system of charity regulation outside the general tax collection regime, it would be inappropriate to return such appeals to the Tax Court as contemplated in previous reports.

THE ROLES OF THE CRA AND DEPARTMENT OF FINANCE: Under the proposed system, the CRA's role in administering charities – but not its main function as the protector of the tax base – would end. This would have the dual effect of maintaining a registration system for income tax purposes while still giving the CRA authority to attack tax schemes, which invariably are based on a charity's right to issue tax receipts. Registration under the ITA would be automatic upon registration by the Council, so the CRA would no longer have the conflicted responsibility of maintaining the tax base and administering socially based non-taxable entities. Simply put, the CRA would revert to an organization whose specific purpose is to collect taxes. Nevertheless, the CRA and the Department of Finance would retain the crucial role of maintaining the integrity of the receipting system, which likely would lead to their having a continued consulting relationship with the Council to ensure that the entire system worked harmoniously.

Conclusion

No system of regulation can ever be perfect, but it is clear and widely agreed that changes are long overdue to the current regime of charity regulation. Unfortunately, significant political will is required to overcome the inertia on reform whenever constitutional difficulties accompany the issue. There is always the possibility that the federal government could force the provinces to act simply by refusing to register new organizations unless they participate in the new regime. It would be far better, however, if the provinces worked with the federal government, the sector, and interested parties to find a way to exert the authority that is constitutionally theirs in any case. Indeed, if all the actors behaved as they are supposed to under the Constitution, Canada's system of regulation could only strengthen Canadian charities and the work they do.

50 One must acknowledge, however, that there is no particular body of expertise on charities in the provincial courts and, given their number, such expertise is unlikely to be developed to the same degree across the country.

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