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The New Qualifying Disbursement Regime and Healthcare Charities

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INTRODUCTION & OVERVIEW



- For a more detailed commentary see the [Charity & NFP Law Bulletin No. 524](#)
- Information is current as of February 9th, 2024, but subject to change

A. SETTING THE STAGE

- Implementing effective healthcare philanthropy requires a working knowledge of what healthcare charities can and cannot do with the funds that they raise
- In this regard, many healthcare charities may need to work with other organizations from time to time in order to achieve their charitable purposes
- When those other organizations are Canadian registered charities or other types of qualified donees (“QD”) listed in the *Income Tax Act* (“ITA”), it is possible to do so because a Canadian registered charity is able to make gifts to other QDs
- However, when a healthcare charity is wanting to work with an organization that is not a qualified donee (“Non-QD”), compliance issues become more challenging
- Examples of working with Non-QDs could include:
 - A healthcare charity wanting to fund a community health initiative run by a community organization that is a Non-QD
 - A hospital foundation with broad community purposes wanting to make a grant to a local indigenous healthcare charity that is a Non-QD

- As a result of amendments to the ITA on June 23, 2022 (Bill C-19), there is now a new option of making qualifying disbursements to Non-QDs in the form of either a “gift” or “otherwise making resources available” as discussed below (“Qualifying Disbursement Regime”)
- The CRA describes this as making a “grant” to a Non-QD
- CRA released a draft guidance on November 30, 2022 (“Draft Guidance”), followed by the release of its final guidance on December 19, 2023, [CG-032 Registered charities making grants to non-qualified donees](#) (“Final Guidance”)
- The Final Guidance is a significant rewrite of the Draft Guidance
- This presentation reviews the following:
 - What the new Qualifying Disbursement Regime involves
 - A brief overview of key aspects of the Final Guidance
 - Issues to consider with the Qualifying Disbursement Regime
 - How the new Qualifying Disbursement Regime compares to the existing Own Activities / Direction & Control Regime (“Own Activities Regime”)
 - Some practical comments that healthcare charities may want to consider

B. BRIEF EXPLANATION OF THE QUALIFYING DISBURSEMENT REGIME

1. Before Bill C-19 Amended the ITA on June 23, 2022

Canadian registered charities could only use their resources in one of two ways under the ITA:

1. Conducting their own activities by devoting their resources to charitable activities carried on by their own staff and volunteers or through intermediaries under direction and control

2. Making gifts to qualified donees (“QDs”)

If a charity wanted to work with an organization that was not a QD, it had to demonstrate that it was conducting its own activities by exercising direction and control over the Non-QD organization concerning how it utilized any funds or other resources provided by the charity

2. Bill C-19 Introduced the New Option of Qualifying Disbursement Regime

- It is very important to read the actual ITA wording

ss. 149 (1) of ITA “**qualifying disbursement** means a disbursement by a charity, by way of a gift or by otherwise making resources available,

(a) subject to subsection (6.001), to a qualified donee, or

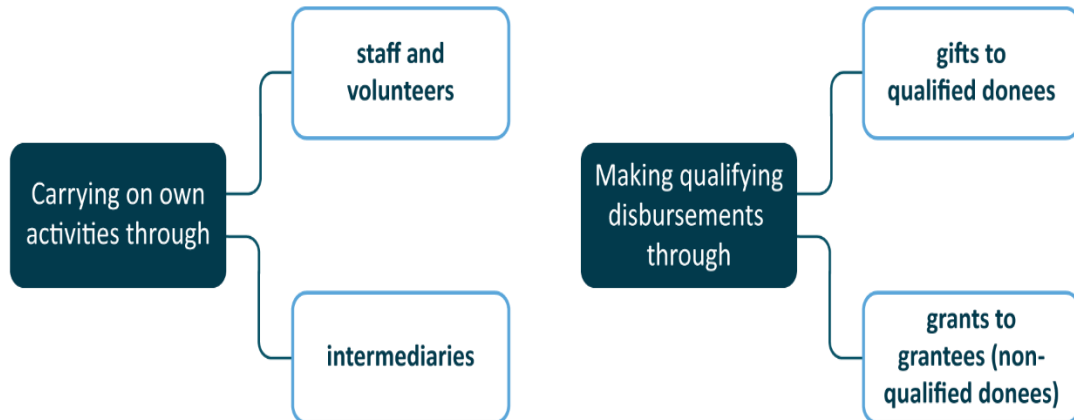
(b) to a grantee organization, if

- (i) the disbursement is in furtherance of a charitable purpose (determined without reference to the definition charitable purposes in this subsection) of the charity,
- (ii) the charity ensures that the disbursement is exclusively applied to charitable activities in furtherance of a charitable purpose of the charity, and
- (iii) the charity maintains documentation sufficient to demonstrate (A) the purpose for which the disbursement is made, and (B) that the disbursement is exclusively applied by the grantee organization to charitable activities in furtherance of a charitable purpose of the charity;”

“**grantee organization**” includes a person, club, society, association or organization or prescribed entity, but does not include a qualified donee;

3. After Bill C-19 Became Law on June 23, 2022

- Canadian registered charities now have two regimes to choose from as graphically depicted in the Final Guidance:



C. OVERVIEW OF KEY ASPECTS FROM CRA FINAL GUIDANCE

1. Section 1.1: Background and Approach by the CRA

- In Section 1.1, the Final Guidance provides background information in relation to its use by the reader, stating that “[t]his guidance is not law”
- Rather, it is explained that the Final Guidance contains recommended ways that “a charity can meet the Income Tax Act requirements while taking reasonable, flexible, and proportionate measures based on the nature of each grant”
- This is a helpful clarification for those in the charitable sector who do not have a legal background and may otherwise assume that a guidance from the CRA is law
- The reality is that CRA’s recommendation in the Final Guidance will become de facto law over time because there is nothing else to guide a charity on what a qualifying disbursement involves

2. Section 1.4: Explanation of CRA's Interpretation and Approach to Qualifying Disbursements

- Section 1.4 includes a summary chart setting out the various qualifying disbursement requirements contained in subsection 149.1(1) of the ITA, and then explains how CRA intends to interpret each requirement and apply the related accountability requirements
- The chart also contains CRA's related recommendations for each requirement and where in the Final Guidance more detailed comments from CRA can be found
- This is a helpful resource for charities to consult in determining how best to fulfill CRA's accountability requirements
- CRA acknowledges that despite its best efforts, a charity may not be able to ensure that grant resources will be applied as intended
- CRA states that it aims to adopt a reasonable, flexible, and proportionate approach to granting

3. Section 2: How Can a Charity Operate?

- Explains how “granting” under the Qualifying Disbursement Regime differs from “direction and control” under the Own Activities Regime
- A charity may convert its relationship with a Non-QD (e.g. change from direction and control to a grant) but the charity must meet all accountability and direction and control requirements at time of change, and needs to document this change in its books and records

4. Section 3.0: Due Diligence Review

- “due diligence” is defined as “steps taken to satisfy the legal requirements for granting under the Income Tax Act” through accountability tools
- “accountability tools” refers to due diligence measures to meet accountability requirements
- “accountability requirements” refer to ITA requirements for making a grant
- The ITA requirements that are referenced as part of the “accountability requirements” include ITA terms of: “ensures”, “exclusively applied”, “in furtherance of a charitable purpose” and “maintains documentation sufficient to demonstrate”

- In Section 3, the CRA recommends the following “due diligence” steps be taken by charities who wish to make grants:

3.1: Establish how the grant activity furthers the charity’s charitable purpose

- A charity’s grant activity must further at least one of its own charitable purposes as set out in its own governing documents, *i.e.* a grant by a charity which furthers any charitable purpose more generally (but is not one of the charity’s own purposes) is not sufficient to be a legitimate grant under the Qualifying Disbursement Regime
- As such, before a charity can make grants to Non-QDs, the charity will first need to review and possibly even amend its charitable purposes, with any amended purposes to be first approved by the CRA

3.2: Assess the grant’s risk level

- The Final Guidance sets out a risk matrix of low, medium and high risk that is intended to help as a guideline to explain risk factors a charity should consider, although the listed factors are described as “non-exhaustive”
- However, if there is a significant change in grant conditions, then the charity should assess whether the grant’s overall risk level has changed, and work with the grantee to adjust the grant’s terms accordingly

- The factors set out in the risk matrix include: (1) the charity’s experience, (2) the grantee’s experience, (3) purposes and governing documents of the grantee organization, (4) governance structure of the grantee organization, (5) the grantee’s regulation and oversight, (6) private benefit concerns, (7) grant activity, (8) grant amount, (9) nature of resources granted, and (10) grant duration

3.3: Determine how much due diligence the charity needs to apply through accountability tools based on the risk level

- The Final Guidance provides another risk matrix which contains guidelines to help a charity determine whether the use of accountability tools can be limited where there is a low risk, moderate where there is a medium risk, or extensive in a high risk situation
- These accountability/risk assessment tools in the matrix include, amongst others, (1) assess and review of grantee (such as grantee’s staff and reputation of the grantee), (2) description of grant activity, (3) written agreement, (4) reporting plan, (5) transfer schedule, and (6) separately tracked funds

3.4: Apply the accountability tools in collaboration with grantee

- Charities are encouraged to work together with grantees to ensure that the accountability requirements set out in the Final Guidance are met

3.5: Document the charity's due diligence over the grant's duration

- Charities are reminded that they are required under the ITA to keep adequate books and records, which contain sufficient information to allow CRA to determine whether they are operating in accordance with all applicable legal requirements
- For grants, a charity's books and records must allow CRA to check whether:
 - The charity's grants meet the accountability requirements,
 - The grantee's use of the charity's resources can be verified through appropriate supporting documentation, and
 - The grantee continues to use the granted resources for the purposes and activities set out in the grant's terms
- A charity making grants which does not keep adequate books and records could be subject to possible CRA audit and compliance measures

5. Section 4: Special Topics

The last section of the Final Guidance goes over several "special topics" that are related to grant making, consisting of:

- Qualifying Disbursement Limit for Charitable Organizations
- Directed Gifts and Acting as a Conduit (commented on below)
- Reporting Grants in the T3010 Registered Charity Information Return (commented on below)
- Pooled Grants with Multiple Organizations (commented on below)
- Granting Charitable Goods (commented on below)
- Granting of Real Property (e.g., land and buildings) – this is considered high risk and the charity should implement adequate documentation to ensure that property will be used only for charitable activities that further its charitable purposes
- Anti-terrorism Considerations – charity must not support terrorist activities by making a grant to an individual or group engaged in or supporting terrorist activities (but see also the humanitarian exemption and authorization regime in the *Criminal Code*) – refers to [CRA Checklist for charities avoiding terrorist abuse](#)

D. ISSUES TO CONSIDER WHEN MAKING QUALIFYING DISBURSEMENTS

1. Defined Terms of “Grants” & “Grant Making” Not in the ITA

- The Final Guidance states that it focuses “on making grants to grantees”, but the terminology of “grants” and “grant making” are not terms that are used in the ITA
- The ITA uses the terms “qualifying disbursement” and “grantee organizations”

Language in ITA	Language in Final Guidance
<p>qualifying disbursement means a disbursement by a charity, by way of <u>a gift</u> or by <u>otherwise making resources available</u> to a qualified donee, or a grantee organization</p>	<p>“grant” refers to a “<u>qualifying disbursement</u>” made to a “grantee organization”, as defined in the ITA. A grant can include both <u>cash and non-cash resources</u>. While the term “grant” is commonly applied to other arrangements within the charitable sector, <u>this guidance uses the term “grant” in relation to the ITA requirements</u> for making a “qualifying disbursement” to a “grantee organization”</p>

- Courts expect charities to comply with legislation as opposed to a CRA guidance, so these differences are important to keep in mind, as they could have significance on a CRA audit that was subsequently reviewed by a court

2. Need to Review Charitable Purposes of the Charity

- A qualifying disbursement is about furthering the charitable purpose of the transferor charity and cannot be done if it is outside of the transferor charity’s own charitable purposes

- Therefore, it is essential to review the charitable purposes of the transferor charity before considering making a qualifying disbursement

- Foundations that have only a single purpose of making gifts to QDs will not be able to make qualifying disbursements to grantee organizations, e.g. Non-QDs, since grantee organizations are not QDs

- As such, foundations with a single purpose of only making gifts to QDs will need to review and expand their charitable purposes if they are intending to make qualifying disbursements to Non-QDs

3. The Imposition of Additional Requirements Not in the ITA

“Risk” is mentioned **31 times** in the Final Guidance (down from 62 times in the Draft Guidance) but is not mentioned at all in s. 149.1 of the ITA

Use of a risk matrix is very similar to onerous Financial Action Task Force (FATF) and US Treasury Risk Matrix for purpose of anti-terrorist financing avoidance

Significant Focus
on Risk and Due
Diligence

Risk matrix says that grants outside Canada and over \$50,000 are high risk but no explanation is provided to explain why \$50,000 is a high risk threshold

While CRA recommends using the “due diligence model”, “due diligence” is not mentioned in s.149.1 of the ITA

Extensive Accountability Requirements

- “Accountability” is mentioned **66 times** in the Final Guidance, up from 46 times in the Draft Guidance, but is not mentioned at all in section 149.1 of the ITA
- “Accountability requirements” and “accountability tools” have been defined in the Final Guidance as referenced on slide 10 above
- Suggested accountability tools are similar to the requirements for “expenditure responsibility” for US private foundations and as such are complicated
- The accountability tools are similar to the requirements that were in the proposed ITA regulations but were removed from Bill C-19 when adopted
- The accountability requirements of the Qualifying Disbursement Regime are more onerous than the direction and control requirements of the Own Activities Regime

Pooled Grants with Multiple Organizations

- Before a charity can make a pooled grant with one or more Non-QDs, the Final Guidance recommends the charity must sign onto at least one written agreement with all parties (“ideally”, or if not feasible, then other accountability arrangements may be acceptable), along with interim and final reports
- Otherwise, the Draft Guidance recommends approaching pooled grants cautiously
- In light of this, charities may be hesitant to make pooled grants because of the complexity and risk involved

Charitable Goods

- Charitable goods (*i.e.* goods that can only reasonably be used for charitable purposes, such as medical supplies) will be subject to specific “accountability tools”, including written agreements and final reports on how goods were used
- These requirements are more onerous than for “charitable goods” under the direction and control regime in CRA’s CG-002 Guidance, [Canadian registered charities carrying on activities outside Canada](#)

4. Unclear Explanation of “Otherwise Making Resources Available”

- The ITA clearly indicates that a charity can make “gifts” to Non-QDs as well as “otherwise making resources available” to Non-QDs but does not explain what the phrase “otherwise making resources available” means in practice
- The Final Guidance does not mention “otherwise making resources available” except when setting out the definition of “qualifying disbursement” in the ITA
- There are two possible interpretations for what the phrase “otherwise making resources available” could mean in practice
 - The charity is gifting monetary and non-monetary resources to a Non-QD or
 - The charity is making available monetary and non-monetary resources to a Non-QD, such as use of space, staff, administration services, volunteers, directors, use of branding, and loans of funds including impact investing
- The latter interpretation is likely correct but this question will be important to consider when preparing agreements that go beyond gifting funds, such as one between a hospital and a hospital foundation for space and administrative services when calculating how to meet the disbursement quota (see below)

5. Some Qualifying Disbursements Do Not Meet Disbursement Quota (“DQ”) Obligations

- The Final Guidance mentions that “[f]or reporting purposes, and to help the charity meet its disbursement quota, the charity must be able to determine the fair market value of non-cash grants”
- However, the Final Guidance does not provide an explanation of what this determination process would involve
- Only qualifying disbursements that are gifts to QDs and Non-QDs can be used to meet the DQ obligations of the granting charity
 - Many charities may find this confusing to track or difficult to comply with in light of the increased DQ of 5% for investment property in excess of \$1 million
- Qualifying disbursements made by “otherwise making resources available” to either QDs or Non-QDs will not be counted towards the DQ, which means that making space, staff and volunteers available, as well as engaging in micro-finance loans and other types of impact investing are not DQable

6. Does Not Reflect The Wording in ITA About Directed Gifts

- New paragraph 168(1)(f) of the ITA states that CRA can revoke a charity’s charitable registration if it accepts a gift “the granting of which was expressly or implicitly conditional on the charity [...] making a gift to another person, club, society, association or organization other than a qualified donee”
 - e.g. Charity A accepting a gift that is “expressly or implicitly conditional” on Charity A making a gift to Non-Charity B
- The Final Guidance states that paragraph 168(1)(f) of the ITA is intended “to prevent organizations from acting as conduits in the making of a directed gift” to a Non-QD, and refers to the Explanatory Notes from Finance
- However, there is no explanation concerning what a “conduit” is or what “acting as conduits” mean other than to recommend that a charity should retain “authority over the use of its resources, and clearly communicate this to the donors”, for example communicating that:
 - Ultimate authority over the donation rests with the charity
 - If donor preference for the gift is not met, charity will not return the gift

- Conditional gifts, though, have a particular meaning at common law that is not explained in the Final Guidance
- The Final Guidance uses an example to explain what “expressly conditional” gifts are, which correctly includes the right of reversion to the donor if the condition is not fulfilled
- However, the Final Guidance is not clear what an “implicitly conditional” gift is when it gives as an example a charity that has the name of a Non-QD in its name, purposes, or other formal documents but no right of reversion
- The interpretation of directed gift in the Final Guidance could limit the fundraising abilities of healthcare charities involved in grants to Non-QDs
- The Final Guidance, though, states that the directed gift provision does not apply to a charity carrying out its own activities through an intermediary under the charity’s direction and control, presumably because it does not involve making a “gift”
- This could result in charities being reluctant to use the Qualified Disbursement Regime when public fundraising is required

E. REPORTING QUALIFYING DISBURSEMENTS

- Regulations under the ITA state that a charity that makes a qualifying disbursement to a grantee will need to include on its annual return (*i.e.* Form T3010) the following information for each grantee organization that receives in excess of \$5,000 in the taxation year:
 - a) The name of the grantee organization;
 - b) The purpose of each qualifying disbursement; and
 - c) The total amount disbursed by the charity to each grantee organization
- The charity must be able to determine the fair market value of non-cash “disbursements” (e.g. “property, such as land, artwork, equipment, and pharmaceuticals”) that are made to grantees on its Form T3010
- In May 2023, the CRA updated the T3010 Registered Charity Information Return by adding the new T1441 Qualifying Disbursements: Grants to Non-Qualified Donees requiring detailed information about grants
- These Forms were further updated on January 8, 2024 and charities must ensure that the correct version of Form T3010 is filed depending on its fiscal year end – for a more detailed commentary, see Charity & NFP Law Bulletin No. 525

- Form T3010 asks:

- If the charity has made qualifying disbursements via grants to Non-QDs
- If any of these grants totaled more than \$5,000 in cash and non-cash grants in one fiscal period
- The number of grantees receiving grants totaling \$5,000 or less
- Total amount paid to grantees totaling \$5,000 or less in a fiscal period
- The new Form T3010 (v. 24) also asked for the total value of qualifying disbursements from donor advised funds in a fiscal period

- Form T1441, which records all grants individually, must include

- The number of grantees that received grants totaling more than \$5,000
- Report each grant separately, even if it's to the same grantee
- The name of the grantee
- The purpose of the grant
- The total amount of cash and non-cash disbursements separately
- The country and country code of where grant activities were carried out, (unless permission is obtained due to safety concerns)
- CRA has updated [T4033 Completing the Registered Charity Information Return](#) to assist charities

F. COMPARING THE QUALIFYING DISBURSEMENT REGIME TO THE OWN ACTIVITIES REGIME

- Since registered charities can now choose between two regimes when working with Non-QDs, what are the differences?

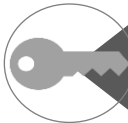
Own Activities Regime	Qualifying Disbursement Regime
1. Focus on the charity being the <u>directing mind</u> with an intermediary <u>carrying out instructions</u> received from the charity	1. Focus on <u>supporting the activities of the grantee organization</u> but only in furthering a charitable purpose of the donor charity
2. More of a <u>hierarchical top down</u> relationship	2. More of a <u>collaborative relationship</u>
3. The funds or resources are <u>not gifted</u> , instead they are transferred to an intermediary as an <u>extension of the charity</u> by means of a contractual agreement	3. The funds or resources are <u>either gifted or are otherwise made available</u> to the grantee, allowing the grantee autonomy to carry on its programs as an independent party
4. The applicable <u>regulatory due diligence</u> is in the form of <u>ongoing direction and control</u> by the charity over the activities of the intermediary	4. The applicable <u>regulatory due diligence</u> is in the form of <u>applying risk matrices</u> and following <u>extensive accountability requirements</u> rather than providing ongoing direction and control

Own Activities Regime	Qualifying Disbursement Regime
5. An <u>agreement is needed</u> to reflect <u>direction and control</u> over own activities of the charity e.g. contract for service or co-operative participation	5. For qualifying disbursements <u>above \$5,000 (or below but expected to be made on an ongoing basis)</u> , a <u>grant agreement is recommended</u> to address a significant degree of risk assessment and accountability requirements
6. As the intermediary is acting as an <u>extension of the charity</u> under the direction and control of the charity, the charity <u>may be exposed to liability</u> by the intermediary	6. Grant arrangement could <u>avoid the unintended consequences</u> for a charity carrying on its <u>own activities through an intermediary</u> , such as incurring liability to third parties under an agency relationship
7. Charitable programs done through an intermediary <u>will count toward the disbursement quota</u> of the charity	7. Qualifying disbursements in the form of " <u>otherwise making resources available</u> " <u>will not count towards the disbursement quota</u> of the charity
8. Contracting with an intermediary to allow the intermediary <u>to purchase land</u> is subject to <u>significant restrictions</u>	8. <u>Gifting of real estate</u> should be carefully documented but is generally <u>less restrictive</u>
9. Contracting with an intermediary in Canada " <u>may</u> " attract HST/GST (need expert HST advice)	9. Making a qualifying disbursement to a grantee in Canada <u>will not attract HST/GST</u> (need expert HST advice)
10. <u>Less onerous</u> reporting requirements in Form T3010	10. <u>More onerous</u> reporting requirements in Form T3010 and Form T1441

G. KEY TAKEAWAYS



The new Qualifying Disbursement Regime is an important new option for registered charities to consider



However, there are complexities and significant due diligence requirements that must be carefully reviewed before deciding to make a qualifying disbursement to a grantee organization



Whether or not a registered charity should embark on making a qualifying disbursement to a grantee organization or choose to continue with the Own Activities Regime is a decision that should be carefully reviewed with legal counsel for the registered charity



It is important to stay up to date for any changes that the CRA may implement to the reporting requirements in Form T3010 and possible updates from the CRA on the Final Guidance, as the Final Guidance is intended to be an "evergreen" document



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