



Canada Revenue
Agency

Agence du revenu
du Canada

Auditing Charities

If you need more information after you read this pamphlet, either about the audit process or about charities in general, **please write to us at:**

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Canada Revenue Agency
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You can reach the Charities Directorate at the following telephone numbers:

- (613) 954-0410 for local Ottawa calls
- 1-800-267-2384 for toll-free, long-distance calls
- 1-800-665-0354 for toll-free service for hearing-impaired people

Internet access

If you have access, you can find many of our publications on our Web site at www.cra.gc.ca/charities.

Visually impaired persons can get our publications in braille, large print, or etext (computer diskette), or on audio cassette by visiting our Web site at www.cra.gc.ca/alternate or by calling **1-800-267-1267** weekdays from 8:15 a.m. to 5:00 p.m. (Eastern Time).

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Introduction

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

The CRA is responsible for monitoring the operations of registered charities to make sure they comply with registration requirements. The audit is an important element of this process.

Being audited can be a source of great concern for registered charities because of the potential tax consequences. In some cases, a registered charity can lose its registered status because of the results of an audit. When it loses its registered status, the charity:

- is no longer exempt from tax, unless it qualifies as a non-profit organization;
- cannot issue official donation receipts for income tax purposes; and
- may be subject to a tax equivalent to the full value of its remaining assets (revocation tax).

When an audit reveals a problem, the charity is notified and is given an opportunity to be heard. The problem is often straightforward and can be resolved. We also give advice about how to better comply with the law.

Why does the Canada Revenue Agency audit charities?

In the *Income Tax Act*, the provisions for registered charities support the basic philosophy that they must use all their resources, including financial, human, and physical, **for charitable purposes**.

The CRA's role is to make sure a charity is complying with the law and applying its resources to charitable purposes. To do so, we usually look at the information a charity provides on its annual returns, financial statements, and other documents we have on file.

Occasionally, we need to confirm or clarify some of the information in that file. The easiest way to do this is to examine the charity's books and records on-site. This is called an audit.

As we do with all our clients, we keep the private information we obtain through an audit confidential. In addition, the administrative procedures we follow ensure that we treat charities fairly, impartially, and consistently throughout the audit process.

You will find more details about these procedures in the section called "What happens when the audit report is complete?" on page 6 of this booklet.

What triggers a charity audit?

The following reasons are those most frequently used to select a charity for audit:

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

Occasionally, we will also make an on-site visit to gather information to help us understand the purposes and activities of an organization that is applying for registered charity status.

How do we conduct an audit?

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

We conduct this examination, called a "field audit," on the charity's premises. It can last from a few hours to several weeks. How long the review lasts depends on whether the audit is general or specific in nature, and how large and complex the charity's operations are.

Either a single auditor or a team of auditors conducts the audit. These auditors are either departmental employees or agents working on behalf of the CRA (e.g., employees of Consulting and Audit Canada).

The Charities Directorate of the CRA directs the nature and scope of the audit, as well as provides advice. The audit process usually includes examining the charity's ledgers, journals, bank accounts, expense accounts, investments, agreements, contracts, annual reports, minutes or other records of board and staff meetings, and other documents that relate to the charity's activities.

The field audit

Auditors contact the charity in advance to arrange a mutually convenient date to begin the audit. Before then, the auditors thoroughly review all the information we have in our files about the charity.

The auditors may want to discuss with the charity's representatives some of the information they obtained from reviewing the files. This discussion helps the auditors understand the charity's activities and operations before they begin examining the books and records. The auditors may also need additional information and help from the charity's representatives during the audit itself.

When they arrive on the charity's premises, the auditors show a departmental identification card. Before examining the books and records, the auditors may also want to tour the premises to better understand the transactions recorded in the books, and to observe the charity's programs and activities.

If the charity's representatives co-operate at all stages of the examination, the audit advances more quickly and efficiently. This kind of co-operation benefits both the charity and the CRA.

A formal requirement may be made by the CRA to those who fail to provide the required information or documents.

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

Reviewing the audit findings

The field auditors then give their completed audit report to the Charities Directorate, Compliance Section. If we need more clarification or information, either the field auditor or an audit advisor from the Charities Directorate, Compliance Section will contact the charity.

Although it usually takes only one or two weeks to complete the field audit, it may take longer to complete the audit review. In order to ensure that we analyze the audit findings and apply the law uniformly, we have to take the time to carefully consider and resolve the more complex or contentious issues.

What happens when the audit report is complete?

During the final stage of the audit process, we write to the charity to formally advise it of the audit results. If the charity's operations and activities appear to comply with all the requirements of the *Income Tax Act*, the letter confirms that we are satisfied with the results of the audit.

In cases where the audit results have raised concerns, we specify our concerns in the letter, and we usually offer the charity an opportunity to address them. **Generally, our approach is to explain the requirements of the law to the charity's representatives, and to suggest the appropriate steps they can take to correct the problems found during the audit.**

In most cases, the problems we identify during an audit are straightforward. The charity can usually resolve them by correcting the problems.

However, in cases where we find a **clear contravention** of the *Income Tax Act*, we might have to consider revoking the charity's registered status. To determine whether or not such action is necessary, we may take into account the following questions:

- Were the inappropriate actions intentional or inadvertent?
- How significant are the inappropriate actions when they are compared to the charity's stated goals?
- Is the charity willing and able to change its practices to comply with the law?
- What is the impact of the charity's inappropriate actions on its donors and beneficiaries, and on the community as a whole?
- How much money is involved?
- Is this a repeat offence?

We also consider the operational realities that often make it difficult to run a charity (e.g., depending heavily on volunteers).

If the inappropriate action is more serious, or if a charity is unwilling or unable to resolve it, we notify the charity of our concerns. In this notice, we also explain that, in our view, the concerns are grounds for revoking the charity's registered status. At that time, we give the charity the opportunity to present its case as to why we should not revoke its registration.

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

According to the law, the charity can appeal this intended loss of charitable status to the Federal Court of Appeal up to 30 days after we mail the notice, or within any extended period the Court specifies.

Points to remember about an audit

You may want to keep these points in mind in the event we select the charity for an audit review:

- we generally notify charities ahead of time to agree on a mutually convenient time for the audit;
- to make sure audits proceed efficiently and quickly, we encourage mutual co-operation;
- when we audit a charity, we inspect both its books and records and the charity's activities;

- we always inform a charity about the findings of the audit;
- we will counsel the charity, if necessary, on how to comply with the requirements of the law; and
- before we make any decision on what action we should take, we always give the charity the opportunity to address our concerns.

Do you have any comments on the audit?

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

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

Please send your comments to:

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