Laird Hunter

I'm A Fiscal Agent: Can I Borrow Your Charity Number?

Our daily life is truly spent in the global village. The Internet connects us immediately to everywhere. Far away is right here and the long-standing tendency to incorporate ideas borrowed from other places increases at an amazing pace. A similar bent exists in the charitable world. To the many notions taken from voluntary experience in other parts of the world can now be added the useful financial concept of fiscal agent. Except that it can't. Taken from US experience, the idea is both misunderstood in its origins and misapplied in the Canadian context. In this column, we review the notion of fiscal agent as it has developed in United States and comment on its application and misapplication in this country.

But We'll Just Borrow Their Number

Imagine overhearing the following conversation.

Last week the executive director and I had a couple of long discussions and developed a proposal for Our Charity to become the fiscal agent for NP Org and to work with it as a pilot project. Our Charity will issue receipts for money raised by NP Org's fundraising efforts and by cheque each month we will transfer that money to NP Org so that it can keep up with the various projects it determines are important to it.

The concept of the fiscal agent is often expressed in this way. While some of the agency aspects used in this conversation are correct, the application to charities is not.

In legal terms, an agent is a person appointed by someone else with the power to do some specified thing for the person making the appointment, the principal. Or an agent can be appointed with general powers. In both cases the agent operates on instructions from the principal. The agent is responsible to the principal for any mistakes made in doing the principal's bidding and the principal can be liable for the wrongdoings of the agent. In the typical agency relationship, the agent is required to account to the principal for how money is spent, to keep records, and generally to be the eyes and ears of the principal at a distance. It is no different in the context of the charitable arrangement. The charity, the principal, appoints an agent to deal

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with some of its affairs. That agent is then authorized to spend money and carry on activities as if the charity were doing so directly. But, and this is a very important qualification, the agent has no more authority than does the principal. It cannot do things that the charity itself is not legally entitled to do.

For example, if a charity should appoint an agent to carry out its direct work, that agent cannot make a grant of money in a way that the charity itself is prohibited to do and not without the direct express permission of the charity. The notion of agency is a common one for charities operating overseas and the Charities Directorate of CCRA requires that the Canadian charity have a written agency agreement with its foreign associates.

In a typical arrangement, the non-exempt organization solicits grants or donations, donors make out their cheques to the tax-exempt sponsor, and the sponsor pays expenses on behalf of, or makes a grant to, the non-exempt organization,… ●

In Canada, often when people speak about charities and fiscal agents, they reverse the relationship, as in the example above. The charity is referred to as the agent, as in *"we'll get the Foundation to be our fiscal agent"*. The reason for wanting to have that relationship is that the non-profit, – not being a registered charity – needs to cloak itself with charitable status to satisfy funders and potential donors. The non-profit wants to be able to tell the Foundation to issue receipts and send it the money. The non-profit wants the charity to be its agent so that the non-profit can control the money raised. It is the non-profit that wants control. And control is the key – but to comply with requirements of the *Income Tax Act* related to charitable purposes that authority must rest with the charity.

US Origins of the Fiscal Agent

In a 1969 ruling the Internal Revenue Service held that a 501(c)(3) organization (the US version of our registered charities) could distribute funds to organizations which had not, themselves, received IRS recognition of 501(c)(3) status. But, and this is often the forgotten point, this distribution was possible only if certain steps were taken to insure that the distributed funds were only used for charitable, educational, or other 501(c)(3) purposes. Based on this ruling, many 501(c)(3) organizations have sponsored other, non-exempt organizations or projects. These arrangements are called by many names — umbrella, fiscal agent, fiscal sponsorship.

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In a typical arrangement, the non-exempt organization solicits grants or donations, donors make out their cheques to the tax-exempt sponsor, and the sponsor pays expenses on behalf of, or makes a grant to, the non-exempt organization, sometimes taking a percentage of the donation as a fee. In the US, the sponsor

may also take care of reporting for the non-exempt organization's employees, allow the use of its bulk mailing permit, provide office space, or allow the use of office equipment or clerical help.

Many of these arrangements go far beyond the scope of what is allowed in Canada as described in Revenue Ruling 68- 489. While these arrangements are not necessarily illegal in the US, commentators regularly observe that these kinds of arrangements can be risky, precisely because they are carried on within a gray area of the law. Only a few clear guidelines are set forth in the ruling:

- funds must be used for specific projects in furtherance of the sponsor's own exempt purposes
- the sponsoring organization must retain control and discretion as to the use of the funds
- the sponsoring organization must maintain records establishing that the funds were used for its purposes.

What About in Canada?

Whatever fiscal agent or sponsorship has evolved to mean in practice – both in the US and here – the fundamental legal requirement is clear: a charity explicitly instructs another organization to carry out some of the charity's work, consistent with the charity's charitable purposes. In Canada, at a minimum, a charity offering to act as a fiscal sponsor should adopt a written internal policy governing sponsorship arrangements, require written proposals from those seeking funding, enter into formal sponsorship agreements with them, and establish on-going oversight and follow-up procedures. All of this is merely the means by which the charity ensures that its charitable purposes – and not non-charitable activities – are clearly advanced by its agent. This last element should be the central part of the written document signed by the charity and the agent. The opening words of one American fiscal sponsorship agreement are an example of the quality that should determine the arrangement:

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"The Sponsor has decided that financial support for the purposes described in the attached proposal will further the Sponsor's tax-exempt purposes. With regard to the selection of the Agent or any other beneficiary to conduct the project, the Sponsor has exercised and retains full discretion and control over the selection process, acting completely independently of the Agent or any other funding source. The Sponsor has created a restricted fund designated for the project and has decided to grant all amounts that it may receive and deposit to that fund (less any administrative charge set forth below) to the Agent, subject always to the following express terms and conditions."

This language is reminiscent of wording commonly found in agency agreements used by Canadian charities overseas and reflects the legal requirement that the charity must maintain control so that their charitable purposes – and only those purposes – are the objects of spending. Charities that are asked or want to have arrangements where others do some of the charity's work under direction – whether in Canada or overseas – are well advised to understand their responsibilities as sponsors.

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