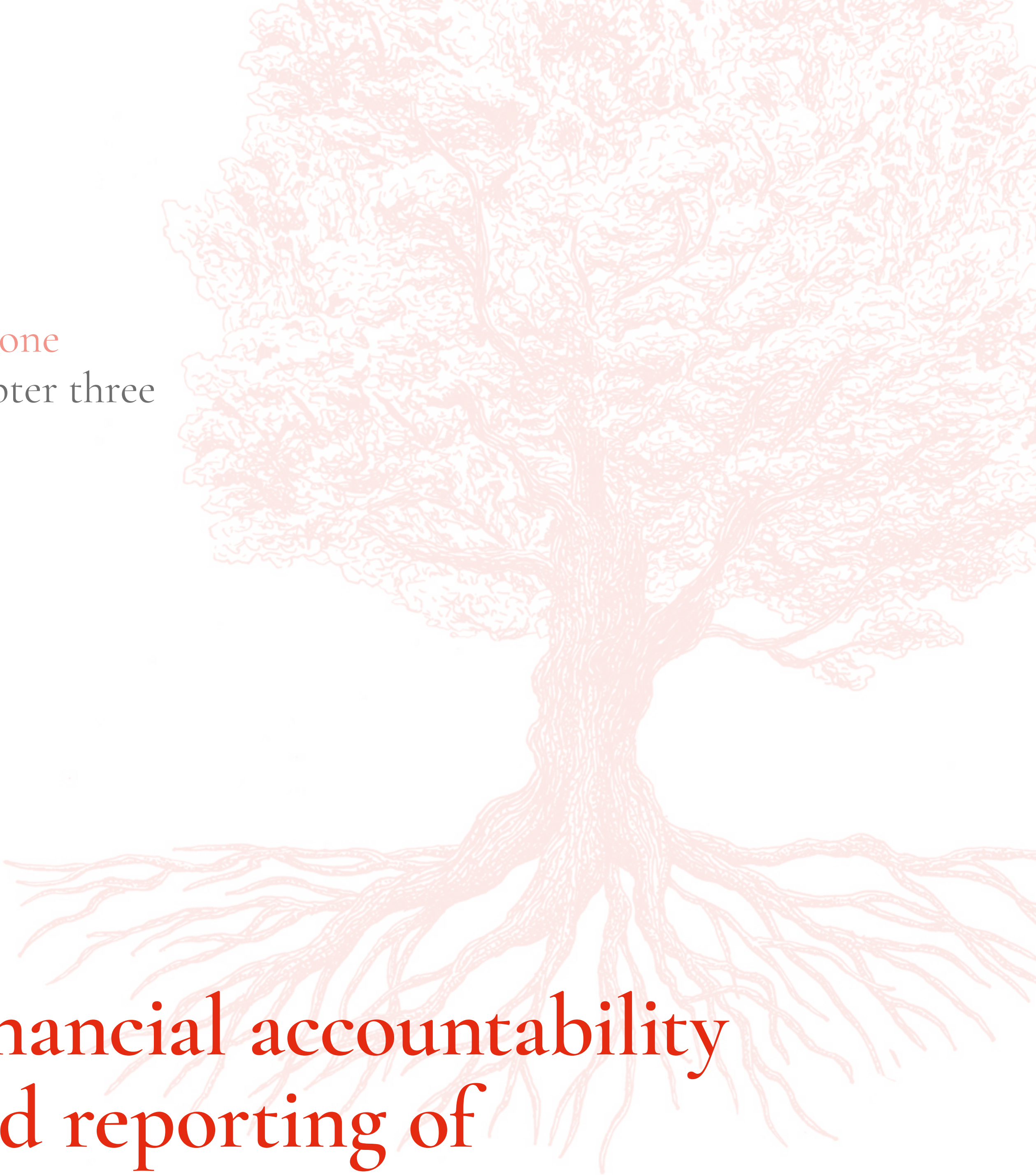


Part one
Chapter three

Financial accountability and reporting of foundations in Canada

François Brouard and Marc Pilon

Foundations operate in a complex and multifaceted environment that creates a number of organizational challenges and increased calls for accountability, among them: perception of secrecy and pursuit of private interests, reputational challenges, increased demands for support, reliance on philanthropy as a substitute of government, demands for transparency, public trust expectations, demonstration of value, increased social needs, and social divides (Johnston, 2012; Pearson, 2010; Pitt, 2018; Ravenscroft, 2017; Rourke, 2014). The general increase in public interest also brings additional accountability pressures on foundations (Dhanani & Connolly, 2015; Gates & Rourke, 2014; Shienfield, 2012).[1] And statutory bodies and the general public alike are demanding information of better quality, particularly in the wake of increased visibility of incidences of mismanagement, tax fraud, and scandals (Cordery *et al.*, 2017).

Of the various forms of accountability foundations must manage, financial accountability constitutes an important part of the overall accountability framework that foundations operate under. This conceptual paper explores the financial accountability of foundations in Canada and the ways in which it is managed through governance mechanisms and reporting. The chapter focuses on the financial accountability dimensions of foundations in Canada and the important financial accountability strategies that Canadian foundations should focus on.

From a financial perspective, financial accountability covers regulatory and legislative requirements, measurement and reporting challenges, ethical dilemmas, transparency demands, information systems, risks management and performance measurement. Financial reporting itself is defined as the "communication of information by an individual or organization to interested parties by way of financial statements and other financial data" (CICA, 1992, p.93).

1 See also Chapter 10 by Laurel Carlton and Sara Lyons on accountability.

In Canada, foundations represent an important group of actors in the nonprofit sector and philanthropic ecosystem. Many foundations may have the impression that they are able to operate outside any external scrutiny (Rourke, 2014). However, considering the fiduciary responsibilities associated with charitable foundations, multiple stakeholders are, could or should be involved in the accountability process.

The Canada Revenue Agency (CRA) (2009) describes a registered charity as an organization established and operated exclusively for charitable purposes. Foundations are a subgroup of charities that include both charitable organizations and foundations. Legally, according to the *Income Tax Act* (ITA), "Charitable foundation means a corporation or trust that is constituted and operated exclusively for charitable purposes, no part of the income of which is payable to, or is otherwise available for, the personal benefit of any proprietor, member, shareholder, trustee or settler thereof, and that is not a charitable organization" (*Income Tax Act*, section 149.1(1)).

As funding organizations, charitable foundations do not need to carry out the charitable activities themselves, although an increasing number do so. Charitable foundations are subdivided into public and private foundations. A public foundation means a foundation where more than 50% of its board operates at arm's length and no *de facto* or *de jure* control is exerted by a person who has donated more than 50% of its capital (i.e. a major donor) (ITA 149.1(1)); a "private foundation means a charitable foundation that is not a public foundation" (ITA 149.1(1)). Public foundations tend to be associated with fundraising activities, while private foundations are generally not.

In addition to their legal public and private classification, Chamberland *et al.* (2012) have also classified foundations by their form as family (e.g. Fondation Lucie et André Chagnon, The J W McConnell Family Foundation), corporate (e.g. RBC Foundation, Mastercard Foundation), community (e.g. Winnipeg Foundation, Vancouver Foundation, Community Foundation of Ottawa), governmental (e.g. The Ontario Trillium Foundation, Alberta Innovates – Health Solutions), philanthropic clubs (e.g. Rotary, Lions, Kiwanis) and specific goals foundations (Canadian Wildlife Federation, Fondation Hôpital Montfort, The Hospital for Sick Children Foundation/SickKids Foundation). Imagine Canada and Philanthropic Foundations Canada (2014) categorize foundations according to their activities: as fundraising arms (e.g. hospital foundations), fundraising intermediaries, donor-advised funds, operating foundations, nondiscretionary funders, grantmaking foundations and community foundations. The diversity of foundations, as demonstrated by their multiple classifications, may add to the accountability challenges they face, which requires a different set of potential stakeholders and standards (see also Chapter 4 by Carla Funk on types of foundations).

The remainder of the chapter is organized into six sections. The first section describes the historical context. The second section presents the concept of financial accountability and its dimensions. Governance mechanisms, both internal and external, are then explored in the third section. The fourth section then looks at and examines financial reporting. The fifth section presents possible improvements in financial accountability. And the sixth and concluding section sets out the main implications of the chapter.

The historical context

In Canada, the Voluntary Sector Roundtable commissioned a report on accountability and governance, which resulted in the release of the Broadbent Report in 1999. The Broadbent Report called for standards, best practices and guides to help regulate the sector. Subsequently, the Voluntary Sector Initiative (1999a; 1999b) had three joint tables, drawing on the work of government officials and sector leaders, on building new relationships, strengthening capacity and improving regulatory frameworks. These tables include suggestions for accountability and reporting that cover financial capacity, human resources, knowledge, information management, and legislative, institutional, administrative and funding changes. Even 20 years later, many of these suggestions remain relevant, for example: "a voice of the sector in government policy making", "being transparent, including communicating to members, stakeholders and the public, and responding appropriately to requests for information", "different reporting requirements for large and small organizations", "greater consistency in accounting practices" (Voluntary Sector Initiative, 1999a, pp. iv, vii). Some efforts have been achieved, but improvements are still needed.

The purpose of presenting the historical context is to underline the failures and challenges of accountability – mainly relating to frauds, scandals and the internal and external environment within which foundations operate – and to understand the evolution of issues over the years. The information flow between stakeholders is then presented in order to give some indication of the complexity of relationships.

Accountability failures: frauds and scandals

Recent examples of nonprofit accountability failures such as frauds and scandals – which feature regularly in the press – further highlight the troubles that the sector faces. Frauds could relate to asset misappropriation, corruption, fraudulent financial statements and misrepresentation (Chen *et al.*, 2009).

One such example is the fundraising effort for a non-existent foundation, as in the case of Wish Kids Foundation, rather than the genuine Children's Wish Foundation (Kennedy, 2014). In 2010, a 48-year-old Sudbury woman was convicted of misappropriating funds from her employer, the Northern Cancer Research Foundation, and sentenced to 10 months in prison (Vaillancourt, 2010). The employee, an executive director, defrauded the foundation of more than $50,000 over the course of at least one year, by stealing cash donations and claiming fictitious expenditures.

Such cases, sadly, are not unusual: the Ottawa police estimates that about 20% of Canadians are victims of charity fraud (Kennedy, 2014).

International examples, where a similar fraudulent fundraising scheme, or the apparent proximity fraud perpetrated by an international network, may also have a spill-over effect on Canada (*ibid.*). More recently, the Cancer Fund of America and three of its affiliates (Children's Cancer Fund of America, The Breast Cancer Society and Cancer Support Services) were dissolved in what is possibly the largest international foundation fraud of all time. The organizations were found guilty of stealing virtually all the US$187 million in donations they received over a number of years (Federal Trade Commission, 2016). The same spill-over effect may come from nonprofits in general, not just from other foundations (Chen *et al.*, 2009).

Accountability failures like these are highly visible and, while the foundations may have been victims of fraud, their financial accountability practices were less than ideal. Frauds are clearly illegal, and even the perception of accountability failures can tarnish a reputation (Sarstedt & Schloderer, 2010). Media coverage in recent years of frauds and waste has mired the sector's reputation and overall social capital (Hall *et al.*, 2003). When publicly disclosed, these scandals shine the spotlight on a foundation's management issues and point to a clear problem of accountability (Gibelman & Gelman, 2004). When the events of the fraud become public, donors lose confidence, and donations can drop significantly. These accountability failures raise concerns about the ability of organizations to manage their financial accountability and impede an organization's ability to deliver on its mission (Costa *et al.*, 2011).

Accountability failures have hurt the nonprofit sector and its foundations by reducing its credibility (Gibelman & Gelman, 2004). The accountability failures undermine citizens' trust in the sector and negatively impact its ability to solicit donations, attract members and recruit volunteers effectively. If the lack of accountability were to become so pervasive that citizens reduced their donations and volunteering, it could have serious consequences on the economy and on society. Reputational effects are especially damaging to smaller organizations, because they are more vulnerable and dependent on donations, members and volunteers (Puentes *et al.*, 2012). Therefore, accountability failures have required foundations not only to be more accountable but also to demonstrate greater accountability (Ossewaarde *et al.*, 2008).

Accountability challenges: Internal and external environment

In addition to accountability failures, accountability management is further complicated by internal and external challenges (Salm, 1999). As with many organizations and in any resource-limited sector, foundations face challenges that affect their ability to manage their accountability and achieve their objectives. Hall *et al.* (2003) distinguish between two prominent accountability challenges: internal capacity factors and external environmental factors.

Internal capacity is defined as "the human and financial resources, technology, skills, knowledge and understanding required to permit organizations to do their work and fulfil what is expected of them by stakeholders" (Broadbent Report, 1999, p.118). The external environment consists of relevant factors outside the boundaries of the organization (Duncan, 1972). Pressures on funding are growing for foundations, especially public foundations. On the demand side, an increase for their products and services required more funds to satisfy demand (Hall *et al.*, 2004; Lasby & Barr, 2014), as governments have downloaded many services to the nonprofit sector (Hall *et al.*, 2003; Smith, 2008). On the supply side, there has been a shift from stable, long-term funding to project funding (Barr *et al.*, 2006; Hall *et al.*, 2003). A study by Statistics Canada found that 98% of nonprofit organizations reported an unwillingness of funders to fund core operations (Hall *et al.*, 2004). As a result, funding has become more cyclical and uncertain, which has made it more difficult for nonprofits to do long-term planning *(ibid.)* and for foundations to fundraise. This increase in demand and a shift in revenue sources have created a lack of resources, which prior research has suggested might be a significant potential barrier to nonprofit accountability (Palmer, 2013; Yetman & Yetman, 2012).

The external environment is composed of numerous factors which can affect the organization's capacity by creating or amplifying organizational challenges (Hall *et al.*, 2003). Foundations face a competitive external environment for the attention of donors and funders (Hall *et al.*, 2003, 2004; Salm, 1999). Donations, as a percentage of GDP, continue to decrease (Emmett & Emmett, 2015), and charities are relying on a smaller proportion of taxpayers for donations (Imagine Canada, 2018). Foundations are often volunteer driven and tend to rely on a small number of key personnel, which may affect their accountability.

Imagine Canada standards program

Governance mechanisms may be used as a way to overcome accountability challenges. A practical application to overcome these challenges is an accreditation process that follows certain standards. The standards program for charities and nonprofits by Imagine Canada (*ibid.*, p.1) is a program "designed to strengthen their capacity in five fundamental areas: board governance, financial accountability & transparency, fundraising, staff management, and volunteer involvement". The program presents three levels of standards on the basis of a combination of the size of organization in term of employees (range from 10 to 50 FTE – full-time equivalent – threshold) and annual expenses (from $3 to $10 million) (*ibid.*). In its ethical code, Imagine Canada (2011) distinguishes three main areas: donor policies and public representations, fundraising practices, and financial practice and transparency. Table 1 summarizes the ethical code requirements for financial practice and transparency. Imagine Canada closed the ethical code program on December 31, 2016. Table 2 presents a summary of the standards regarding financial accountability and transparency, which will be discussed later.

Table 1 – Imagine Canada's ethical code on financial practice and transparency

	Extracts from the code on ethical requirements
C1	"The charity's financial affairs shall be conducted in a responsible manner, consistent with the ethical obligations of stewardship and all applicable laws."
C2	"All donations shall be used to support the charity's objects, as registered with CRA."
C3	"The cost-effectiveness of the charity's fundraising programs shall be reviewed regularly by the governing board. No more will be spent on administration and fundraising than is required to ensure effective management and resource development."
C4	"The charity shall accurately disclose all costs associated with its fundraising activity."
C5	"The charity shall make the following information publicly available (e.g. on its website, in its annual report, in its financial statements) within six months of its year-end: • total fundraising revenues • total fundraising expenses • total expenditures on charitable activities/programming"
C6	"Charities with over $1 million in annual revenue must have their financial statements audited by an independent licence public accountant. Charities with annual revenue between $250,000 and $1 million may have a review engagement unless required by their governing legislation to have an audit."
C7	"If the charity's investable assets surpass $1 million, an Investment Policy shall be established setting out asset allocation, procedures for investment decisions, and asset protection issues."

Source: Imagine Canada (2011)

Table 2 – Imagine Canada's standards on financial accountability & transparency

Standards summary for foundations	
Financial accountability	
B1	"Organizations must complete annual financial statement in accordance with an acceptable accounting framework as identified by [...] CPA Canada (Chartered Professional Accountants of Canada)."
B2	"Organizations with over $1 million in annual revenue must have their financial statements audited by an independent licensed public accountant. Other organizations may have a review engagement unless required by their governing legislation to have an audit."
B3	"The organization's financial statements must be received and approved by the board and released within six months of year-end"
B4	"The board has a process to ensure that an accurate Registered Charity Information Return (T3010) is filed with the CRA within six months of year-end, as required by law."
B5	"The board approves the annual budget and has a process to monitor the organization's performance in relation to the annual budget. The board or a board committee reviews actual revenues and expenses versus budget at least twice a year."
B6	"The board or a board committee receives from management, at least twice a year, assurance that all statutory remittances have been made."
B7	"The board regularly reviews the cost-effectiveness of the organization's fundraising activities. No more will be spent on administration and fundraising than is required to ensure effective management and resources development."
B8	"Organizations with investable assets over $1 million must have an investment policy setting out asset allocation, procedures for investments, and asset protection issues."
Transparency	
B10	"The organization's financial statements are publicly available. The organization makes the following information available on its website: annual reports, financial statements with opinion, names of all board members, T3010."
B11	"The organization makes information on compensation accessible to its stakeholders to at least the same level as that required by CRA in the T3010."
B12	"The organization discloses on its website details of the purpose and amount of payments for products or services to board members or companies in which a board member is an owner, partner or senior manager."
B13	"The organization accurately discloses all costs associated with its fundraising activities."

Source: Imagine Canada (2018)

Note: B9 standard on protection in electronic commerce was eliminated in 2018.

Ecosystem of information flows

To prevent failures and challenges, a large component of accountability is the exchange of information between stakeholders.[2] In a philanthropic ecosystem, many stakeholders drive accountability (Fontan & Lévesque, 2017). Among the most important stakeholders of grantmaking foundations are the government, donors, grantees, the public, media and intermediaries (Charity Commission, 2009; CICA, 2011; Connolly *et al.*, 2013).

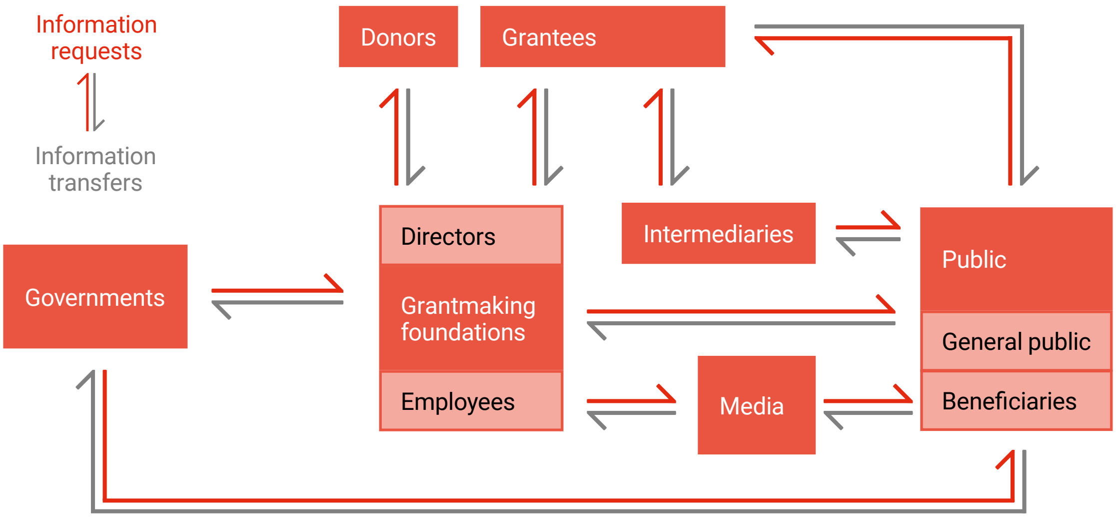
It is important to identify each of these stakeholders more closely. *Grantmaking private or public foundations* are registered charities and must therefore respond to the reporting requests set out by regulators, most notably the CRA. Directors and employees (including the management team and volunteers) are stakeholders within foundations. *Government*, as a regulator, plays a key role in the aggregation and disclosure of financial and governance reporting information (Hyndman & McMahon, 2010). For the purpose of this chapter, "government" includes all the agencies, ministries and statutory agencies such as CRA, Industry Canada, Finance Canada, and Statistics Canada. *Donors* (for public foundations) and funders (for private foundations) are considered important stakeholders (Hyndman, 2010), because without them there would be no foundation in the first place. *Grantees* are organizations or individuals who receive grants from grantmaking foundations. *The public* includes the general public and beneficiaries. *The media* includes newspapers, television, radio, and various social media. *Intermediaries* present multiple faces, which include rating agencies, the accounting profession and researchers: some are organizations that monitor the charitable sector, disseminate information and provide ratings (Gordon *et al.*, 2009; Phillips, 2013). The accounting profession is another intermediary that plays a role in the development of accounting standards applicable to foundations (Hyndman & McMahon, 2010), and auditors provide assurance on financial statements and financial information (Sinclair *et al.*, 2011). Researchers could be seen as intermediaries as well (Brouard, 2014).

Figure 1 shows the key stakeholders and main information flows connected to grantmaking foundations. The main nexus of information flows are between foundations and donors, foundations and government, foundations and grantees, foundations and the public, governments and the public, and grantees and the public. All these stakeholders operate in a web of information exchanges. Information requests and transfers represent the information inflows and outflows between stakeholders. Information flows are presented with arrows of different colours, depending on whether they are requests or transfers. Some exchanges are mediated by media and/or intermediairies. Requests for information could be mandatory (e.g. T3010) or voluntary (e.g. website content). The disclosure and accessibility of information could be public or private. Informal and private reporting may be restricted to specific foundations or available to peers. Information flows may fall between the continuum of those dimensions (disclosure/accessibility, public/private). Information disclosures could also originate from stakeholders themselves or from

2 See also Chapter 2 by Hilary Pearson for the importance of information.

other stakeholders, with or without their consent. For foundations, managing the information flows is, therefore, a critical component of accountability.

Figure 1: Ecosystem, stakeholders and information flows



Source: Brouard & Glass (2017)

The framework in Figure 1 includes networks of grantmaking foundations and government institutions because information sharing and collaboration are considered growing trends (Pearson, 2010). Information sharing occurs within a group of grantmaking foundations, especially larger ones – associations such as Community Foundations of Canada (CFC), Philanthropic Foundations Canada (PFC) – or as the result of common interest, with organizations such as the Canadian Environmental Grantmakers Network and the Circle on Philanthropy and Aboriginal Peoples in Canada (*ibid.*).

Financial accountability

A number of dilemmas could be cited to explain some of the general debates regarding accountability. From an institutional perspective, Rourke (2014) cites the distinction between public and private money, the discrepancy between more information and better information, and the difference between being transparent and demonstrating impact.

Definition and dimensions of financial accountability

Financial accountability is imposed and "prioritises formal, coercive, compliance-based forms of accountability [...] using mainly quantitative measures" (O'Dwyer and Boomsma, 2015, p. 38). There are explicit rules (Morrison & Salipante, 2007), often legal requirements to achieve at specified and regular intervals. There are many dimensions of financial accountability: ethics, regulatory and legislative requirements, information systems, transparency, risks management, measurement and reporting challenges, performance measurement, social responsibility.

The role of regulators

In Canada, the federal government regulates the charity sector and plays a key financial accountability role (Cordery & Morgan, 2013; Hyndman & McMahon, 2010). This role is assumed by CRA and the Charities Directorate. Canada is known to have a strong reporting system in comparison with others. All charities, including foundations, are required to comply, and it is possible to find T3010 information from the CRA website or on the charitydata.ca website (Brouard, 2017). With the open data movement, regulators may not control the access to information completely (Phillips, 2013). Any suggestion that the quality of data is becoming insufficient may affect the reputation of these organizations, which could bring about more regulation (Tremblay-Boire *et al.*, 2016). Forthcoming changes within the CRA on-line T3010 reporting requirements for charities are likely to improve data quality and quantity.

As registered charities, grantmaking private or public foundations must respond to the reporting requests set out by CRA and the *Income Tax Act*. The main obligations of a registered charity are to devote its resources (funds, personnel, and property) to its charitable purposes and activities, control and direct the use of all its resources, maintain its status as a legal entity, keep adequate books and records, meet its annual spending requirements (disbursement quota), make sure that official donation receipts are complete and accurate when issued, and file its annual form T3010 within six months of its fiscal year-end (Brouard, 2014).

Governance mechanisms

Governance mechanisms are used to manage the accountability demands of stakeholders and may be divided between internal and external mechanisms (Walsh & Seward, 1990). Harris *et al.* (2017, p.164) describe the importance of both internal and external governance to foundation activities: "Prior research suggests that donors value certain governance mechanisms voluntarily adopted by charities [...]. Our results provide specific reasons why donors should care – good governance reduces the likelihood that their funds will be misappropriated. Moreover, donors may also want to consider the presence of external oversight." Table 3 presents a summary of internal and external governance mechanisms, many of which, while not exclusive to grantmaking foundations, apply to foundations and should provide a helpful checklist for them. Most of these mechanisms are related to financial accountability in some way and examples are provided below. More details will be provided later for mechanisms that are more specific to financial reporting.

There is growing interest about the impact evaluation of the activity of foundations, which will continue to follow the regulations and disclose their financial statements in accordance with accounting standards and to provide an external audit report.

Table 3 – Internal and external governance mechanisms

Internal governance mechanisms	External governance mechanisms
Beliefs and values	Market
Board of directors	Shareholders/Members
Audit committee	Employees
Other board committees	Legal system
Advisory board	Disclosure requirements
Family groups and rules	Accounting profession
Remuneration plans	Results and performance
Management systems	Media pressures
Ownership structure	Societal ethics and morality

Source: Brouard (2016)

Internal governance mechanisms

Internal governance mechanisms can be grouped into the following categories: beliefs and values, board of directors, audit committee, other board committees, advisory board, family groups and rules, remuneration plans, management systems, and ownership structure (see Table 4 for details).

Table 4 – Internal governance mechanisms

Internal governance mechanism	Components
Beliefs and values	beliefs and value systems, code of values, code of conduct, code of ethics, conflict of interest rules, trust, culture, and management philosophy.
Board of directors	statutory and oversight role, size, composition, frequency of meetings per year, proportion of executive directors/non-executive directors on the board, proportion of independent directors on the board, proportion of independent directors with accounting and finance background on the board, proportion of directors external to the family on the board of directors (especially important with a family foundation), mix of inside and outside directors (the Imagine Canada (2018) standard A18 recommends five or more outside directors). Further specific aspects relating to the role of chief executive officer (CEO): e.g. whether their role is combined with or distinct from the chair of the board; their power/influence re board membership selection, terms and length of board membership. Important considerations for board composition include: reputationof executive/non-executive directors on the board, qualification of directors on the board, membership criteria for directors on the board (experience, personal characteristics, gender, independence, core competencies, availability). Criteria relating to board directors' election (age, election term, term limit, mandatory retirement), the number and kind of positions that each board director holds in other organizations, and procedures for evaluating board members.

Audit committee	The *audit committee* (one of the board of directors' committees) has a special role with regard to financial accountability (Ellwood & Garcia-Lacalle, 2016) and may be responsible for performing Imagine Canada (2018) standards B5 on budget approval and B6 on assurance. The establishment, role, size and composition of audit committees are matters for consideration, as are the membership criteria for the directors on it (experience, personal characteristics, independence, core competencies, availability, remuneration), the frequency of audit committee meetings per year, and the level of independence of the committee from the board. As far as the composition of the audit committee is concerned, some considerations may include a high proportion of independent directors, a high proportion of directors with an accounting and finance background, a high proportion of independent non-executive directors, and CEO and CFO presence.
Other board committees	*Other board committees* cover numerous aspects of organizational governance. Organizations use various names for these committees, such as governance, fundraising, nomination, management, executive, finance, remuneration and benefits, pension, environment and health, human resources, investment, risk, regulatory, compliance and government affairs, public responsibilities, technology and innovation, sustainability and ethics. Imagine Canada (2018) standard B8 on investment and asset management may be performed by an investment committee. An investment policy (asset allocation, procedures for investments, asset protection issues) is mandatory when an organization's assets are over $1 million. As with the board of directors and the audit committee, there should be clarity for each committee on its mandate; procedures; criteria about roles, size, composition; membership criteria such as experience, personal characteristics, independence, core competencies, availability, diversity; remuneration; proportion of independent directors.
Advisory board	An *advisory board* can complement an existing board of directors when terms of office make it difficult to provide the full scope of representation or long-term experience for prudent decision-making. As above, the terms of reference and scope of activity for an advisory board is important to define and enforce.
Family groups and rules	*Family groups and rules* may be relevant for family foundations. A family foundation may be regulated by family procedures and rules such as the establishment of a family assembly, the number of family assembly meetings a year, the establishment of a family council, the number of family council meetings a year, the number of meetings a year between family members, family business rules and family charter. The interconnection between the foundation and the family, especially for private foundations, may be unofficially settled at the family meetings.

Remuneration plans	*Remuneration plans* may be a source of tension between donors and the foundation. The level of remuneration for charitable organizations is often cited in the media. Among the factors to be considered here are the executive compensation structure, executive compensation level, CEO compensation, remuneration systems, and performance incentives. Imagine Canada (2018) standard A5 indicates a requirement for the board or a board committee to approve the total compensation package of the most senior staff person.
Management systems	*Management systems* include a wide variety of mechanisms such as constitution, bylaws, policies and guidelines, vision and mission, strategic plan, accounting systems, budget, business plan, rules and procedures, internal controls, internal auditor, strategic intelligence, balance scorecard, risk management system, systems for conflict resolution, whistleblower policy and tools, crisis management, continuity plan, and insurance. Imagine Canada (2018) standards in section A propose various guidelines on management systems.
Ownership structure	*Ownership structure* of a foundation may include the structure, the ownership by a family and its use for other objectives, namely control of a corporation with a transfer of shares to a foundation (McQuaig, 1987). Corporate foundations act as the philanthropic arm of a for-profit corporation (see Chapter 5).

The Imagine Canada standards program, noted above, is relatively recent, having been launched in 2012. By September 2018 it had accredited more than 200 organizations (not all foundations). Under this program (now Imagine Canada 2018), foundations are able to strengthen their financial accountability through governance and reporting. Establishing formal processes and systems are a continuous challenge, especially for smaller foundations, because they are often volunteer driven and may be unable to acquire or train key personnel to acquire the necessary managerial knowledge and expertise (Barr *et al.*, 2006). Collaboration between foundations may help them share their experience and best practices.

External governance mechanisms

The external governance mechanisms are: market, shareholders/members, employees, legal system, disclosure requirements, accounting profession, results and performance, media pressures, societal ethics and morality (see Table 5 for details).

Table 5 – External governance mechanisms

External governance mechanism	Components
The market	*The market* has fewer implications for foundations than it does for for-profit corporations. The financial market and subsequent transactions may be relevant when considering asset managements or donor transactions by donors (0% inclusion rate for taxable capital gain on gift of publicly traded securities – unless donated to a private foundation). Other market-related facets may include debt/loan market (debt covenant), labour market, managers market, goods and services market, and competition between organizations, especially for attracting donation dollars.
Shareholders/ members	*Shareholders/members* of an organization may be in a position to exercise a right to vote on, and thus influence, a variety of governance issues including board membership, by-laws, budgets and the appointment of auditors.
Employees	*Employees* may exercise a certain control over an organization, which may be increased with the presence of unions, though this is quite rare in foundations. Employees may have a say in the election of directors to the board of directors.
The legal system	*The legal system* includes corporate law, securities legislation, labour law, environmental law, access to information legislation, privacy legislation, disclosure protection legislation (whistleblowing), lobbying legislation, other laws and regulations, governance codes, and codes of best practice. Imagine Canada (2011) ethical code C1 calls for financial affairs to be conducted in a responsible manner, consistent with the ethical obligations of stewardship and all applicable laws.
Disclosure requirements	*Disclosure requirements* are a major component of demonstrating financial accountability, and include financial statements, management and discussion analysis (MD&A), annual reports, governance reports, environmental reports, social responsibility reports, governmental reports (tax return, information return – T3010), disclosures of remuneration, and voluntary disclosures. Imagine Canada (2018) standards B1, B3 and B4 require complete financial statements to be approved by the board and for there to be a process to ensure accurate and timely release of the T3010.
The accounting profession	*The accounting profession* regulates the financial disclosure and the assurance of financial statements according to the accounting standards – Generally Accepted Accounting Principles (GAAP) – and the auditing standards (GAAS). For instance, the accounting profession regulates audit engagements, including auditor independence, the presence of two auditors, and the proportion of services other than auditing offered by an auditor. Imagine Canada (2018) standards B1 and B2 require an acceptable accounting framework, as identified by CPA Canada, accompanied by an audit or review report.

External governance mechanism	Components
Results and performance	*Results and performance* could be measured in various ways beyond net income or the surplus of revenues over expenses – for example, the social impact and reputation of an organization. Imagine Canada (2018) standards A24, D9–D10 and E9 require board performance reviews, staff performance objectives and assessment, and volunteer impact and contributions evaluation. These standards do not focus on the social impact, even if some trends demonstrate a potential evolution toward such measurement.
Media pressures	*Media pressures* could play a role in the flow of information with media enquiries focusing on various aspects of an organization. For foundations, media pressures are probably the most crucial aspect of external governance, and media scrutiny of a foundation's actions continues to increase.
Societal ethics and morality	*Societal ethics and morality* provide a context for what is or is not acceptable in a society. The #metoo movement and its implications is an example of the evolution of societal ethics and morality. Debates around partnerships agreements between the Fondation Lucie et André Chagnon, the Québec government and community actors underline issues about taxation, democracy and autonomy (Fortin, 2018).

Financial reporting

Financial reporting is an important component of demonstrating accountability to external stakeholders. Financial reporting includes definition, measurement, presentation and disclosure. There is a need for reliability and consistency in the way in which charities report their finances, and for enforcement of this reporting (Breen, 2013). For our purpose, reporting is defined as the organization of information flows along a common set of characteristics and objectives.

Financial information types

Information, such as financial information, could lead to knowledge that is also a valuable resource for foundations (Schorr, 2004). Information reporting should have a good fit with the information needs of charities (Hyndman, 1991): in other words, there should be a correspondence between information requests and information transfers. There are four broad categories of financial information reporting (Brouard & Glass, 2017): tax and regulatory, performance, social, and grantmaking. Table 6 presents examples of financial information shared within the philanthropic ecosystem.

Table 6 – Examples of financial information that might be shared

	Tax and regulatory reporting	Performance reporting	Social reporting	Grantmaking reporting
Financial statements	■	■		
Audit or review report	■	■		
T3010 return for CRA – section D & schedule 6	■			
Annual Information Return for Industry Canada or provincial incorporating body	■			
Donations receipts	■			
Annual report		■	■	
Foundation reports to donors		■	■	
Foundation website		■	■	
Policies (e.g. investment)		■		
Budget information		■		
Input, outputs		■	■	
Outcomes		■	■	
Salary scales			■	
Granting policies and procedures				■
Past and current grants disbursed (amount, recipient, purpose)				■
Grantee application				■
Grantee report				■
Ratios (e.g. ratio of administration costs to total budget)		■		■

Tax and regulatory reporting is influenced by the general requirements imposed on charities by governmental agencies and specific requirements on foundations by the *Income Tax Act*, such as the T3010 Information return, and other regulatory requirements.

Performance reporting refers to financial statements and other financial information which are generally prepared internally and are mostly quantitative. Performance, which may include more than financial information, is often the responsibility of the same group of individuals.

Social reporting refers to information shared about a foundation's activities, non-financial performance and impacts. Such information can be prepared internally or by external stakeholders such as the media, government agencies or other intermediaries and can include both quantitative and qualitative measures.

Grantmaking reporting refers to information requests and disclosure between foundations and grantees and information about grants shared with other stakeholders.

Financial statements

The main vehicle for reporting financial information to internal and external stakeholders is financial statements. The five components of financial statements are the statement of operations/income statement with revenue and expenditures; the statement of financial position/balance sheet with assets, liabilities and net assets; the statement of changes in net assets; the statement of cash flows; and the notes to the financial statements. An auditor's report may accompany the financial statements to provide assurance about their preparation in accordance with generally accepted accounting principles (GAAP) (Sinclair *et al.*, 2011). Imagine Canada (2018) standards B1 and B2 require complete annual financial statements with an audit or review report. Instead of a full set of financial statements, summary or highlights of financial information are sometimes prepared and presented. Such summaries may reduce the level of details available to stakeholders, but simplify the financial information for non-experts. Providing both complete and summary financial statements, however, may present the various audiences of an organization with the level of financial information they need and increase transparency.

In the absence of research here in a Canadian context, international studies provide some guidance. According to a study of the Charity Commission for England and Wales (2017, p. 1), although three-quarters of charities provided information of acceptable quality, a "quarter of charities failed to provide this basic information and fell well short of the standard the public has every right to expect". This basic information required charities to demonstrate how they had used their resources and to provide an audit report. Among the reasons given for charities' failure to do so, the Charity Commission cited: "the accounts as a whole were inconsistent or not transparent", "the accounts did not balance or were incomplete", "a proper independent examination had not been carried out", "the annual report did not cover the charity's objectives and/or its charitable activities", "one or more of the annual report, independent scrutiny report and the accounts were missing" (Charity Commission for England and Wales, 2017, p. 4).

The accounting profession plays a role in the development of accounting and assurance standards (CPA Canada, 2018a; 2018b; 2018c) for nonprofits, charities and foundations (Hyndman and McMahon, 2010). With different types of organization and a wide range of activities, foundations face a different financial reporting and accounting context in Canada. From the CPA Canada handbooks (CPA Canada, 2018a; 2018c), foundations could choose various versions of accounting standards, such as the International Financial Reporting Standards (IFRS) (Part I), the accounting standards for private enterprises (ASPE) (Part II), the accounting standards for not-for-profit organizations (Part III), and the Public Sector Accounting standards. Charitable nonprofit organizations are part of a larger set of organizations (Crawford *et al.*, 2018). However, Imagine Canada (2018) standard B1 requires an acceptable accounting framework as identified by CPA Canada. An audit report will attest to the acceptable accounting framework used. Given the different nature of various types of foundations, those of similar type will be comparable. The development of financial reporting standards is even more complicated at the international level (Crawford *et al.*, 2018; Kilcullen *et al.*, 2007). The various standards may bring a lack of comparability and understandability of financial reporting.

Financial information in T3010 – Information return

Every registered charity in Canada is required to file a T3010 (Registered Charity Information Return) for each taxation year (ITA 149.1(14)) within six months of the year-end; not doing so may incur a revocation by CRA of the charity's charitable status. The T3010 information for all charities is publicly available through the CRA and also through the charitydata.ca websites. Executive summary of T3010 information profile could offer an efficient way to ensure public understanding of a foundation. Donors use that information to address their main concern that donations are being used efficiently and effectively. For instance, a recent survey by Imagine Canada found that 61% of donors reported that they would like charities to explain where or how their donation would be spent, 46% would like to know if too much money is spent on fundraising and 39% want charities to demonstrate the impact on the cause and community they are serving (Lasby & Barr, 2018).

On the T3010, most financial information is found in Section D (1 page) and more detailed financial information is found in Schedule 6 (2 pages). Detailed financial information is required when a charity's revenue exceeds $100,000, the amount of all property not used in charitable activities is more than $25,000, and if the charity has permission to accumulate funds during the fiscal period. Financial information includes assets, liabilities, revenues and expenditures. Schedule 3 of the T3010 requires remuneration details of the ten highest-compensated, permanent, full-time positions. Table 7 presents the content of the 2019 version of the CRA T3010 Information Return. It should be noted that the form T3010 changes regularly, generally every year.

Table 7 – Canada Revenue Agency T3010 content

Section	Description	Additional form
Section A	Identification	Schedule 1 Foundations
Section B	Directors/trustees and like officials	T1235 Directors/Trustees worksheet
Section C	Programs and general information	T1236 Qualified donees worksheet Schedule 2 Activities outside Canada Schedule 3 Compensation Schedule 4 Confidential data Schedule 5 Non-cash gifts Schedule 7 Public policy dialogue and development activities
Section D	Financial information	Schedule 6 Detailed financial information
Section E	Certification	
Section F	Confidential data	
	Privacy statement	
Schedule 1	Foundations	T2081 Excess corporate holdings worksheet for private foundations
Schedule 2	Activities outside Canada	
Schedule 3	Compensation	
Schedule 4	Confidential data	
Schedule 5	Non-cash gifts	
Schedule 6	Detailed financial information	
Schedule 7	Public policy dialogue and development activities	

Source: CRA T3010E (19) version

Annual report

In addition to the quantitative information provided in the financial statements, narrative reporting, which is usually found in the annual report and which places the financial information in the context of the organization's overall story, is considered important (CICA, 2011). Narrative reporting, for example, would include accounts of impact and volunteer contributions, items that are not usually to be found in the financial statements (Shienfield, 2012). The narrative may be helpful for donors to know the impact on the cause and community they are serving (Lasby & Barr, 2018).

According to a CICA (2011) report, key elements of reporting may include: organizational purpose, mission/vision, strategy, goals and performance, risks and opportunities, financial and non-financial highlights, fundraising methods and outcomes, outlook for the future, organizational structure and leadership, and governance. The report also gives some guiding principles of reporting to help organizations in writing their annual report, such as "focus on the mission", "tell the story", "have a strategic perspective", "account for stewardship", "meet stakeholder needs", "be fair and balanced" (*ibid.* p. 6).

Other financial information

Other financial information may include quantitative and qualitative formats (Hyndman, 1991). For example, in addition to previous years' information, future information may be included, such as budget information and service level estimates.

Social reporting may include a variety of content choices such as a statement of an organization's goals and information on problem issues or areas in need of support (Connolly & Hyndman, 2003). Mandatory public benefit reporting may be included as part of social reporting. Measurement of social impact is a developing area. Performance reporting may include the economic performance of an organization, effectiveness and efficiency measures based on input/output, outcomes, volume, quality of service (Connolly & Hyndman, 2003; 2004), and using administration and fundraising cost to total budget as a way of measuring cost-benefit ratios (Connolly & Hyndman, 2013). The content of grantmaking reporting may also include the funding application or grantee reports.

Considering all the content choices, data is a vital organizational resource. Pardy and Fritsch (2017) underline the importance of data literacy to make the most of the data. Various types of data exist, such as administrative data (e.g. accounting transactions, financial statements, T3010), program data (e.g. service level measures, operational data collected about programs) and social data (e.g. demographic trends, well-being of communities) (*ibid.*). The data could be private, shared, simple or highly complex. Big data and analytics may involve multiple datasets and require sophisticated tools and expertise, which may be available only to larger foundations.

Possible improvements in financial accountability

Financial accountability could be improved through additional transparency: relationships and trust are important to accountability (Gates & Rourke, 2014). Vinten (1997, pp. 25–8) suggests thirteen elements "to make accountability a reality" in a charity, namely: fulfilment, formality, periodic reporting, adequate detail, consistent form, accountability to all directly and indirectly responsible or properly interested parties, purposes, principles, procedure, relationships, results and outcomes, efficiency and performance, and incomes and expenditures.

It is also possible to have more transparency by having some open decision-making meetings of the charities and foundations, which will allow questions by interested stakeholders (Fiennes & Masheder, 2016). Foundations are funded by society through the benefits of the tax system on charitable donations, and therefore all stakeholders should be considered in accountability matters. Fiennes and Masheder (*ibid.*, p. 4) suggest specific examples such as "inviting the public to observe discussions and decision-making meetings", "holding open public meetings", "hold an AMA (Ask Me Anything) [...] on physical or social media", "collecting (and publishing) feedback from grantees", "publishing transcripts of all board meetings". At the Hôpital Montfort in Ottawa, for example, holding public meetings for some of the regular board of directors' meetings is a common practice, open to anyone who is interested.

Another way to improve financial accountability is to adopt standards, such as Imagine Canada (2018), sharing best practices and increasing the participation of different stakeholders (The William and Flora Hewlett Foundation, 2015). Open access to information about a foundation's assets, investment policies, and program impact could be examples of sharing best practices. Reinstating national surveys (similar to Statistics Canada (2005, 2009)) should be a key priority (Lalande & Cave, 2017), and having a more unified and strong charitable sector in Canada would enable foundations to cope better with changes and challenges as they occur (*ibid.*).

Conclusion

As the historical context shows, accountability is not a new issue. Reports in the 1990s, the conclusions of which are still relevant today, established a need for improved accountability, by improving collaboration and relationships between the sector and government institutions, by strengthening capacity and by improving the regulatory framework. The increased attention on financial accountability, however, has put additional pressures on foundations and all stakeholders to react and be proactive. The exchange of information between key stakeholders in the philanthropic ecosystem presents various information flows for requests and transfers. A clear set of policies by government and foundations is still a work in progress. In a landscape which is changing and likely to continue evolving, being vigilant is essential.

Financial accountability is a specially important part of accountability, given the need for financial sustainability in response to failures, such as frauds and scandals, and internal and external challenges. The variety of internal and external governance mechanisms offers numerous ways to manage accountability. Even if they may be imperfect and not completely foolproof, governance mechanisms may help to mitigate errors and failures in creating the appropriate accountability system.

Financial reporting is an umbrella term encompassing the financial dimension of tax and regulatory, financial, social and grantmaking reporting. Financial statements, as the primary tool, are a means to communicate the financial position and operations of a foundation. The CRA T3010 form, as a mandatory requirement, is a major driver of information requests. There is a variety of other information reporting which is valued by the different stakeholders.

The implications for foundations of the requirement to tighten accountability include the need to strengthen their accountability role by providing more variety in the content of the information communicated on their finances and their performance, but also on the general context of their actions. Better information quality on the foundations' goals and actions will help those working with foundations to understand the difficulties they are facing with limited financial and human resources. For academics with an interest in accounting, financial accountability is an open area of research with multiple ramifications.

Given the shift towards more accountability, the foundations that will thrive in the future are likely to be those that adopt greater transparency with more and better information and exercise real leadership in managing their stakeholder relationships, governance and financial reporting.

Three key takeaways

1

Financial accountability should be an important part of an organization's overall strategy. Taking financial accountability seriously can help prevent costly frauds and scandals.

2

Annual financial reporting to regulators should not be seen as a burden and a task to be completed as quickly as possible. Financial reporting requires strong attention to detail and regular monitoring throughout the year.

3

Beyond financial reporting, narrative and social reporting is an important means to gain legitimacy with important stakeholders.

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PHILANTHROPIC FOUNDATIONS IN CANADA

LANDSCAPES, INDIGENOUS PERSPECTIVES AND PATHWAYS TO CHANGE

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Dedicated to our dear
friend and colleague
Jack Quarter

1942–2019

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