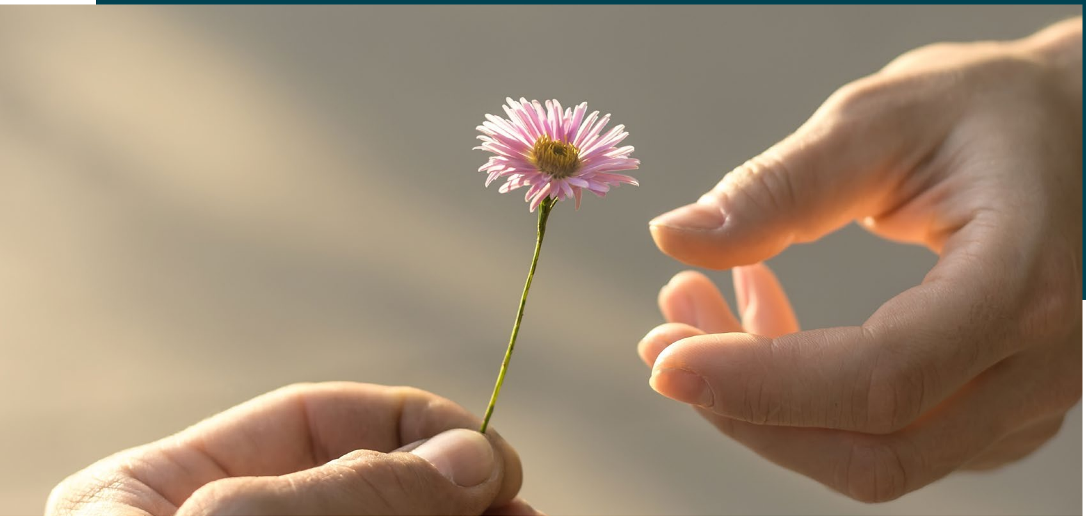
Planning Matters



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Four Ways of Charitable Giving

In the words of steel baron and progressive philanthropist, Andrew Carnegie, "it is more difficult to give money away intelligently than to earn it in the first place".

People support charities for a variety of reasons, with the types of charities and the amount and frequency of gifts dependent on each person's financial and personal circumstances. When you add in the complexity of the various ways to donate and relevant tax and non-tax considerations for each method, it can quickly become challenging to figure out which charities to benefit, the way in which to donate, the timing of donations, and the level of control to retain over those donations.

As a starting point, it is helpful to understand the tax advantages of making donations. When you make a donation to an eligible charity, you will get charitable tax credits which can be used to reduce your federal and provincial or territorial income taxes.

There are charitable tax credit rates for both federal and provincial or territorial taxes. A person may claim these charitable tax credits in his her or annual income tax return for total gifts in a year up to 75% of his or her net income, subject to certain exceptions. The charitable tax credit can be carried forward for up to five years. In the year of death, the limit for using the charitable tax credit is increased from 75% to 100% of net income. Any unused charitable tax credits in the year of death can be carried back one year. This article provides a high-level overview of four ways of charitable giving and some of the pros and cons of each.

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- Andrew Carnegie

Foundations

Charitable foundations are structures for long-term, flexible, and customized philanthropy. Both private and public foundations enable donors to make long-term gifts and offer various benefits, which include the tax benefits outlined above, creating a lasting legacy, and involving family members in the giving process. These structures may be attractive for donors who are interested in creating gifts that will have a lasting impact on charitable causes which are important to a donor and his or her family.

Public Foundations

A donor-advised fund (commonly referred to as a "DAF") is a fund established with a public foundation. A public foundation is comprised of DAFs from multiple donors, and a donor can contribute to an existing DAF or establish his or her own. There are over 180 various community foundations across Canada. As well, it is possible to set up a fund at many financial institutions.

Advantages:

- The public foundation is responsible for the administration, investment, and maintenance of the various DAFs.
- The donor can choose to be as involved as he or she desires.
- The donor does not have any direct tax compliance obligations.

Disadvantages:

- The donor can advise on the charities that he or she wishes to support, but the public foundation has the ultimate control over the distribution of funds.
- Annual administrative fees.

Example: Thomas is interested in setting up a long-term giving structure. He is semi-retired and is on the board for various public companies and travels frequently. He does not feel he has the time to devote to manage a foundation. Thomas could start a DAF and be involved as much or as little as he chooses. He can also provide input on the donation policy.

Private Foundations

A private foundation is established by a donor, generally with the help of professional advisors. A charitable trust or corporation is established or created and then an application for charitable status is made to the Canada Revenue Agency.

Advantages:

- The donor retains control over decision-making for the private foundation, including how foundation assets are invested, which charities are supported, amounts, and timing of distributions.
- The donor can be more involved in the operations of the private foundation (if established while he or she is alive).

Disadvantages:

- The donor is responsible for set-up and ongoing maintenance costs, as well as ongoing administration and tax compliance.
- Although there is no minimum, there should be enough funds contributed to the private foundation to justify the costs and also to meet the annual disbursement quota of 3.5% without having to encroach on capital (typically, at a minimum $1,000,000).

Example: Nathan and Taylor donate annually to a number of local charities. They want to engage in more structured giving and want to involve their children. They want to have full control of a foundation and have a strong role in the decision-making *process with regard to the use of donations. They have the time and professional advisors around them to attend to the necessary set-up, administration, compliance and investment management.*

Charitable Remainder Trusts

A charitable remainder trust is established by the donor transferring cash or other property to an irrevocable trust. The donor would receive income from the property during a stated period, such as his or her lifetime, and would appoint one or more charities as capital beneficiaries entitled to share the property remaining in the trust on the death of the donor.

Advantages:

- The donor would be entitled to an immediate charitable tax receipt on the transfer of property to the trust, which can be carried forward for up to five years. There is a mechanism for valuing the gift.
- Because trust assets are not held by the donor at the time of his or her death, the trust assets pass outside of the estate and are not subject to probate tax.

Disadvantages:

- The donor needs to ensure he or she has financial security outside of the income of the trust for the remainder of his or her life. The trust is irrevocable and the donor cannot have the right to encroach on the capital.
- Subject to limited exceptions, transferring property into a trust with significant appreciated capital gains will trigger a disposition for income tax purposes.
- A charitable remainder trust established under a will does not have favourable tax treatment as a result of the Graduated Rate Estate regime (which came into effect in 2016).

Example: William is an active philanthropist and wants to make a large charitable donation. He would benefit from a tax donation credit today, but does not want to lose the income stream from part of his investments. He is in his late 80s and has excess assets for his needs at this stage. A charitable remainder trust may be desirable in his case.

Gifts of Securities

People may also choose to make gifts of cash or other property directly to certain charities, either during their lifetime or in their will, or to use other means for gifting such as designating a charity as the beneficiary of proceeds of a life insurance policy or retirement plan. Donating securities in-kind to a charity instead of cash can have certain tax benefits.

Advantages:

- Elimination of the taxable capital gain on the appreciated value of the securities.
- The donor is issued a tax receipt for the fair market value of the securities at the time of the donation.

Disadvantages:

- Loss of income generated from the securities. The donor would need to feel comfortable that he or she is not personally relying on the income stream generated by the securities.
- Some charities may not accept in-kind donations, so it is important to contact the charity to confirm they will accept the intended gift.

Example: Claire wishes to donate $5,000 to a charity. She owns shares in Netflix worth $5,000 with a cost base of $1,000. She could sell the securities, pay tax on the $4,000 gain, donate the smaller net amount, and claim that smaller amount as a deduction on her tax return. Her alternative is to donate the $5,000 of securities in-kind. In this case, the charity would get the full $5,000 and Claire would get a tax receipt for the same. As a not-for-profit, if the charity should choose to sell the Netflix shares, there would be no tax payable.

The type of charitable giving will be different for each person and will depend on the person's personal and family objectives, financial circumstances, and desired level of engagement and control. When considering your philanthropic objectives, it's important to understand the different options available, including the tax and non-tax benefits, and how it fits into your overall giving plan.

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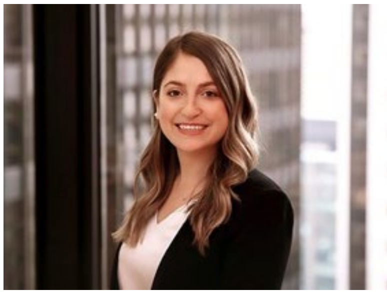

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NOTE: *The contents of this article are not intended to represent legal or tax advice. Please consult your adviser before employing any strategies discussed here.*

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