



Types of Charitable Gifts During Your Lifetime

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Cash Gifts

Cash gifts are the most common way to donate to charity. The donor receives a tax credit, rather than a tax deduction on the donated amount. The tax credit on the first \$200 donated is calculated using the lowest federal marginal tax rate (15%). The tax credit on donations in excess of \$200 is calculated using the highest federal marginal tax rate (29%). Provincial tax credits vary between provinces and territories.

Generally, the amount of charitable donations claimed cannot exceed 75% of net income. Unclaimed donations can be carried forward for up to five years. The limit increases to 100% in the year of death or in the preceding year.

Here are a few ways to increase the charitable donation tax credit:

- 1) Donate over \$200 per year up to the maximum allowable amount;
- 2) Combine accumulated charitable donations over the five-year period and claim them on a single tax return. However, the most that can be saved is \$38.22 per year of carried forward \$42 donations using Ontario tax rates;
- 3) Claim the entire amount of all charitable donations on the higher income spouse's tax return. This avoids the double-counting of the \$200 threshold. Also, the higher income spouse can take advantage of a higher limit and a possible reduction of provincial surtaxes.

Note: Generally CRA's administrative practice has been to allow spouses to combine their donation receipts. Furthermore, the CRA's website offers the following tax tip: "Combine your receipts with those of your spouse or common-law partner and claim them all on the return that will allow for the highest tax credit rate."¹

However, the Income Tax Act does not mention the transferability of the donation receipts between spouses or common-law partners (ITA 118.1). A recent court case highlighted this discrepancy. The court concluded that despite the erroneous belief, CRA's long-time administrative practice does not give legal protection and tax authorities are not bound by past practices. The judge issued the following ruling disallowing the transferability of the donation receipts: "But where there is no ambiguity in the law, and I am afraid I can find none in section 118.1, I am bound to apply the law as Parliament wrote it, and I have no alternative but to dismiss your appeal."²

If you are doing a large donation, ensure that the donation receipt is issued in the desired spouse's name.

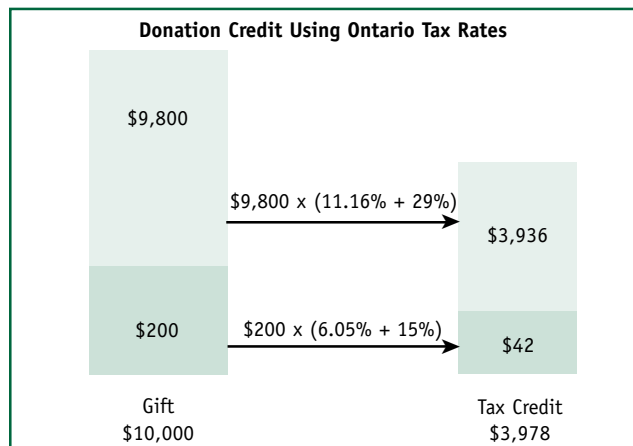
Donation of Capital Property or Depreciable Property

Most gifts of property are deemed to be disposed of at fair market value at the time of donation. This can result in capital gains, capital losses, recaptures of capital cost allowance (CCA)¹ or terminal losses. Gifts of publicly-traded securities are one of the exceptions to this rule and they are addressed later.

The 75% annual donation limit is increased by 25% of the taxable capital gain and 25% of any recapture of CCA (to a maximum of 25% of the lesser of the capital cost or the fair market value of the depreciable property) that are realized on donated assets.

If a donation of property results in a capital gain or a recapture of capital cost allowance, the tax on the income will be offset by the donation credit.

On the other hand, if a deemed disposition results in a capital or terminal loss, this could reduce net income and

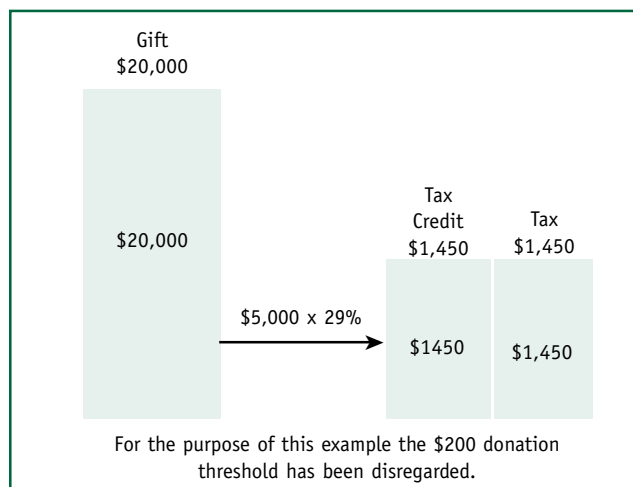


consequently a taxpayer's donation limit.

Capital Gain Example

A violin was acquired for \$10,000. It was donated at a fair market value of \$20,000, resulting in a capital gain of \$10,000. A taxable capital gain (net income) is 50% of \$10,000 = \$5,000. The maximum donation limit is \$5,000, calculated as $(\$5,000 \times 75\%) + (\$5,000 \times 25\%)$. At the top federal tax rate of 29%, the federal tax on the capital gain is \$1,450, calculated as $(\$10,000 \times 50\% \times 29\%)$. The federal donation tax credit is \$1,450, calculated as $\$5,000 \times 29\%$. As a result, the taxpayer has a net federal tax of \$0.

The excess donation of \$15,000 (total donation - maximum donation limit) or $(\$20,000 - \$5,000)$ can be claimed against other income or carried forward for up to 5 years.



Recapture of CCA Example

A commercial plane was acquired for \$100,000. CCA of \$50,000 has been deducted from income over a number of years. The plane was donated at a fair market value of \$70,000. As a result, the donor realizes a recapture of CCA of \$20,000 $(\$70,000 - [\$100,000 - \$50,000])$ and has to include it in his income. A recapture of CCA is 100% taxable.

The donor's donation limit is \$20,000, calculated as $(\$20,000 \times 75\%) + (\$20,000 \times 25\%)$. The maximum federal tax on the recapture of CCA is \$5,800 $(\$20,000 \times 29\%)$. This is offset by the maximum federal tax credit of \$5,800 $(\$20,000 \times 29\%)$.

The excess donation of \$50,000 (total donation - maximum donation limit) or $(\$70,000 - \$20,000)$ can be claimed against other income or carried forward for up to 5 years.

Gifts of Publicly-Traded Securities

Taxable capital gains realized on gifts of publicly-traded securities were eliminated on May 1, 2006.

However, allowable capital losses are still calculated as 50% of realized capital losses.

Donations of publicly-traded securities can become complicated in the event of a merger or acquisition.

Example

If the BCE deal had gone through, shareholders would have received \$42.75 per share. Many BCE shareholders acquired their shares at a much lower price so they were expecting to realize significant capital gains on their dispositions. Consequently, many of them considered donating their shares.

Unfortunately, in every potential takeover there is a risk that the deal might not be consummated. Charities cannot take on this risk by issuing a receipt for the full price of the proposed deal. In fact, many charities have a policy to sell donated shares within 24 hours of receiving them.

On the other hand, once a merger or acquisition has been completed, shareholders may be deemed to have disposed of their shares. They will have no choice but to recognize capital gains or losses on the transaction.

Therefore, individuals who are planning to donate their shares to a charity in the event of a merger or acquisition may wish to adopt a "wait and see" approach because as time gets closer to the deadline:

- More information about the likelihood of the deal will likely become available; and
- The trading price will likely approach the proposed deal price.

Employee Stock Options and Unlisted Exchangeable Securities

As per the 2006 Federal Budget, employee stock options that are exercised to purchase shares which are then gifted to an eligible charity within 30 days are also exempt from tax.

The 2008 Federal Budget introduced similar changes for unlisted exchangeable securities that are exercised for listed securities and then donated within 30 days.

Gifts of Life Insurance

Gifts of life insurance can be receipted in three ways:

1. Upon the transfer of the ownership of an existing policy to a charity, a receipt can be issued for the fair market value (usually the cash surrender value [CSV] except in special circumstances) of the policy.

However, this option has a number of drawbacks because the charity is now the policy owner:

- The charity becomes the only beneficiary;
- The charity controls the CSV; and
- The charity can make any future changes to the policy.

2. If a donor undertakes to pay the ongoing premiums or partial payments for the policy, receipts can be issued for the amount paid.

3. Life insurance proceeds payable to a charity upon the death of an insured (as designated beneficiary of the policy or as directed in the taxpayer's will) will generate a donation receipt for the full amount of the proceeds. The donation tax credits can be claimed in the taxpayer's final return. Any unused credits may be claimed in the previous year.

Gifts with Benefits Returning to the Donor

If a donor structures a gift with a benefit (advantage) returning back to the donor, split receipting rules may apply.

Example

A donor could give a lump-sum amount to charity out of which the charity is required to issue an annuity to the donor. Another possibility might be if a donor gifted a property during his/her lifetime, but had a lifetime right to use the asset.

If gifts aren't properly structured, the donation credit may be denied.

The split receipting rules, which are still in draft form although they are treated by CRA as being in effect as of December 20, 2002, are as follows:

- There must be an intention to give. The amount of the advantage returning to the donor must not exceed 80% of the fair market value of the transferred property (*ITA* subsection 248[30]).
- The amount eligible for a donation receipt = the fair market value of the property less the amount of the advantage (subsection 248[31]).
- The amount of the advantage = the fair market value of the property, service, compensation or other benefit received by the donor (subsection 248[32]).
- Anti-avoidance provisions are specified in subsections 248 (35) – (41).
- Some of the more common types of donations and related strategies have been highlighted here. There are also many different alternatives to consider.

Endnotes

¹ Canada Revenue Agency website, Frequently Asked Questions, "How can I maximize my tax credits for donations?," <http://www.cra-arc.gc.ca/tx/chrts/dnrs/fq/menu-eng.html>.

² *Douziech v. R.*, 2000 CarswellNat 1000 (T.C.C.), at para. 6 (informal procedure).

³ Most capital expenditures cannot be deducted from income in the year they are incurred. Instead, a certain percentage of the expenditure is deducted from income over a

What You Cannot Claim

These are some examples of gifts that cannot be claimed:

- Donations to charitable organizations outside of Canada (there are some exceptions to this rule),
- Gifts to individuals,
- Cost of lottery tickets purchased from charitable organizations,
- Blood donations,
- A pledge to make a donation,
- A loan to a charity,
- Services,
- Unreimbursed expenses for volunteer work, and
- Tickets to events from which you or someone else benefits.

number of years. These partial deductions are called capital cost allowances (CCA).

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Income Splitting Opportunity Not To Be Missed

In February 2002, *MoneySaver* published an article on an income splitting strategy where a "high tax bracket" spouse lends a "lower tax bracket" spouse money to invest. The objective is to transfer investment income so it is taxed in the lower tax bracket spouse's hands and, therefore, the after-tax return is increased.

To comply with income tax rules the loan must be made at Canada Revenue Agency's prescribed rate of interest. The rate of interest can be locked in for the duration of the loan. The rate back then was 3%.

Well, CRA's prescribed interest rate, for at least until March 31, 2009, is now only 2%. The income splitting strategy is now even more attractive!

If you're considering this strategy, it would be a great time to implement it. Should the lower income spouse earn more than 2% on the borrowed money, the "couple" is better off in terms of the after-tax return.

If you have an income splitting loan at a 3% or higher interest rate, you may want to arrange to have the loan paid off and a new loan arranged at 2%!

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