Giving Smarter

Choosing the right charitable giving strategy

If you have philanthropic goals and plan to make charitable donations during your lifetime or upon death, it is important to develop a strategy that maximizes the tax benefits that may be available to you.

Donation strategies

Beneficiary designation with registered plans

One of the easiest ways for Canadians (other than Quebec residents) to donate is to designate your preferred charity as the beneficiary of your Registered Retirement Savings Plan (RRSP), Registered Retirement Income Fund (RRIF) or Tax Free Savings Account (TFSA). This strategy allows the funds to bypass probate and be paid directly to the charity named as the beneficiary of the account. You can designate a beneficiary directly with the financial institution holding the registered account or you can designate a beneficiary in your will. If making a beneficiary designation in your will, it must be drafted carefully to ensure that the registered account remains outside of your estate and is not subject to probate tax.

Designating a charity as the beneficiary of your registered account will provide tax benefits in the year of your death. Under Canadian tax law, your executor must report any taxable income earned in the year of death which includes 100% of the value of an RRSP/RRIF. Designating a charity as the beneficiary of your RRSP/RRIF will allow your estate to claim a charitable tax credit to offset a portion of the tax payable on the value of your RRSP/RRIF. The federal charitable tax credit rate is 15% on the first $200 donated and 29% thereafter. You can claim charitable tax credits up to 100% of your net income in the year of death. Provincial charitable tax credits may also be available.

Designating a charity as the beneficiary of your registered plans has the added advantage of privacy since the funds will be transferred directly to the charity upon your death. If you make a beneficiary designation in your will and your will is probated, it becomes a public document.

Bequests

A bequest is a gift made in your will. There are many different ways to make a charitable bequest. You can choose to gift a fixed amount of money, a specific item of real or personal property, or a portion of the residue of your estate. When making a charitable bequest in your will it is important that you accurately identify the charity by including its proper legal name, address, and charity registration number. Only registered charities can issue donation tax receipts which your estate will require to claim a charitable tax credit.

Life insurance

You can designate a charity as the beneficiary of your life insurance policy. When you pass away, the charity will receive the life insurance proceeds and your estate will get a donation tax receipt for the amount of the death benefit. With this strategy, you remain the owner of the policy while you're alive. That means you can change your mind and revoke the beneficiary designation at any time.

Publicly traded securities

From a tax perspective, it can be advantageous to donate publicly held securities rather than cash, particularly when the securities have a large accrued capital gain. Normally, when you sell securities 50% of the capital gain is taxable. However, if you donate the securities to charity you don't have to pay any capital gains tax and you will receive a donation receipt for the fair market value of the securities.

Example:

> Joanna owns shares of ABC Inc., a publicly traded company, which she bought for $20,000 and are now worth $100,000. Joanna wants to donate her ABC Inc. shares to the National Gallery of Art in the most tax-efficient way. The table below shows that Joanna would realize additional tax savings of $20,000 if she donated her ABC Inc. shares directly to the charity rather than selling them first and donating the proceeds.

	Sell shares, donate proceeds to charity	Donate shares directly to charity
FMV of Donation (A)	$100,000	$100,000
Adjusted Cost Base	$20,000	$20,000
Capital Gain	$80,000	$80,000
Taxable Capital Gain	$40,000	$0
Tax Rate	50%	50%
Tax on Capital Gain (B)	$20,000	$0
Charitable Tax Credit (C)	$29,000	$29,000
Total Cost of Donation (A + B – C)	**$91,000**	**$71,000**
Net Tax Savings (C-B)	**$9,000**	**$29,000**

Specialty gifts

Specialty Gifts can include many types of property such as land or art work. You may wish to give a parcel of land or building to a charity, but before doing so, speak with the charity. Do they wish to receive property? Will the building serve a purpose for the charity? It's more likely they will prefer that this type of property be sold, and you donate the cash proceeds instead.

There are some special cases where an environmental charity would welcome the donation of **ecologically sensitive land**. In fact, such a donation can be made to the federal or provincial governments, municipalities or an approved charity. This program is administered by *Environment and Climate Change Canada*. Look online for more detailed information about this program, here: http://www.ec.gc.ca/pde-egp/

The "fair market value" of the property must then be established. Specialty gifts require a proper valuation. An accredited appraiser must be hired to provide a valuation that will be acceptable to the Canada Revenue Agency (CRA). The value of the property, and hence the eventual tax credit, should be worth the cost of hiring such an appraiser.

Perhaps you have a preference for supporting arts and culture. You may make a gift of **cultural property** to charities such as a public art gallery, museum, archives or library. To qualify for special tax treatment, the gift must be certified as having "cultural significance". Cultural significance is determined by a federal board the Cultural Property Export Review Board. The Board determines whether an item has cultural significance, and if so, its value. Information about the Board and its guidelines are available on the Board's website.

If the gift is accepted by the charity and approved by the Board, the donation will be equal to its fair market value.

With regard to receiving a taxable receipt for gifts of ecologically sensitive land or cultural property, the amount of the donation that you may claim on your tax return can be up to 100% of your net income, rather than the usual 75% limit for other types of charitable donations.

Charitable remainder trusts

A charitable remainder trust allows you to donate property to charity while retaining the use of it during your lifetime (which includes the ability to receive income from it). You receive a donation tax receipt in the year you donate the property to the trust. This strategy is most often used by donors with extensive holdings who plan to make a donation in the future, but would like to reduce income tax now.

When you transfer property to a charitable remainder trust, you make an irrevocable transfer of the property to the trust which becomes the legal owner of the property. You retain a lifetime interest to use or benefit from the property while you're alive and upon your death, the property will be transferred from the trust to the charity. For this strategy to work the trust must be "irrevocable", meaning you cannot change your mind about making the donation.

The donation tax receipt is issued to you for the fair market value of the residual interest in the property at the time the property is transferred to the trust. A proper valuation of the property should be obtained from an accredited appraiser. The transfer of property to the trust may trigger unrealized capital gains that could be offset by the charitable tax credit received. You should speak with your tax advisor to ensure you know the full implications of the transfer.

> Perhaps you have a preference for supporting arts and culture.

Finally, the property will also pass to the charity outside of your estate, so probate fees would not apply to the value of the donation, and you will benefit from the privacy of not having made the donation through your Will — a public document if probated.

Donor advised funds

Donor Advised Funds for charitable giving purposes are an alternative to establishing a private foundation. You can establish a fund, determine the name, donate cash or securities, receive a donation receipt, and decide which charities to give to.

This can be done without having to undertake the effort, cost, and fiduciary responsibility of setting up and running a private foundation. The foundations's board of directors has the fiduciary duty to ensure that it is in compliance with CRA's rules regulating charities.

The benefits of the foundation include:

- You will receive the donation tax receipt up-front.
- The funds held within the foundation are invested and tax-exempt.
- You remain actively involved in choosing the organizations and projects that receive the funds.
- You have the flexibility to make changes.
- You will be able to engage your family members, especially your children, in the decision-making, creating an opportunity to unite family members around shared values for years to come.

Finally, you will be creating a tax-effective legacy to support the causes that you care about. You can realize immediate tax benefits from donating through a Donor Advised Fund. Your contributions, as irrevocable gifts, may result in tax credits in the year you make them, or they could be carried forward for credit within five years.

Private foundation

A private foundation is a highly structured form of giving, which involves a great deal of hands-on involvement by the donor, and usually his or her family — much more than a Donor Advised Fund. Moreover, you will receive the same tax benefits as donating through a Donor Advised Fund; however, it will also mean incurring more expenses to set up and maintain.

You would normally work with a lawyer to set up your foundation as either a trust or a non-share capital corporation. If it is established as a corporation, you would need a minimum of three people as a board of directors, or a trustee if it is established as a trust an application is made to the CRA to obtain registered charitable status.

Once the foundation is established, you donate to it, and receive a donation receipt. You can donate a wide range of assets — cash, securities and life insurance — to your foundation. It can also be the beneficiary of your RRSP, RRIF, TSFA or life insurance policy. Private foundations are tax-exempt, enabling income and capital gains to accumulate tax-free. It should be noted that all gifts to private foundations are irrevocable.

The foundation has to disburse, or use for charitable purposes, a minimum of 3.5% of its average value in the previous two years, to charity and must abide by all of CRA's rules governing charities. Annual filings must be made to the CRA.

The basic tax benefits of donating

The value of a tax credit is determined by two factors:

1. The total amount of your available donations
2. Your income

These general rules apply to both the federal and provincial donation tax credits, which will have a combined impact on your tax payable.

For the provinces, generally a donation total up to $200 will result in a tax credit be multiplied by the respective province's lowest tax rate. For a donation total above $200, the tax credit will generally multiplied by the province's highest tax rate. The total credit will vary depending on the province you live in.

On the federal level, the rates are as follows:

- If the total amount of your tax donations for the year is $200 or less, you will receive a total credit multiplied by the donation, i,e., $200 x 015=$30.
- The credit will be 33% on the lesser of: the amount by which the donor's total donations for the year exceed $200 and the amount by which the donor's taxable income exceeds the dollar threshold of the top personal tax rate.
- For a donation total that is not eligible for the 33% rate, the tax credit rate will be 29%.

Three more points to keep in mind

1. Generally, the total amount of charitable donations claimed can be up to 75% of your net income. The exemption to this rule is your year of death, and the year prior to death, when the total donation amount claimed can be up to 100% of net income.
2. If your total donation amount is greater than 75% of taxable income, it can be carried forward and claimed in any of the subsequent five years.
3. You can maximize the impact of the donation tax credit in any given year in a variety of ways. For example, you could gather receipts received for donations given over a few years, combine and use them to obtain a larger credit in one year — within the five-year carry-forward limit. So you or your spouse or common-law partner, whoever has the highest income, can claim the donation and can maximize his or her tax savings.

Considerations

Planning your charitable giving and choosing which charitable giving strategies are suitable for you. With assistance from your TD advisor, identify the tax benefits that arise from the strategies you choose within the context of your overall Wealth Plan.