

A close-up photograph of a computer keyboard with several keys visible, including the number 5, 3, and 0 keys, which are slightly out of focus compared to the central key.

Planned charitable giving

When you donate to your favourite charity, you can make a meaningful difference in people's lives while also gaining the opportunity to reduce your taxes. That's charitable giving.

Planned giving is a strategic approach to charitable giving that makes optimal use of financial structures and tax rules for the mutual benefit of both you and the charity. It can be done during your lifetime, or at your death through a Will or certain beneficiary designations.

This InfoPage discusses the tax rules and other considerations involved in charitable giving and planned giving.

The donation credit

Donations to a registered charity in Canada are eligible for a tax credit. The first \$200 you donate is eligible for a federal tax credit of 15% of the donation amount. Depending on where you live, you can also claim an additional provincial tax credit of 4% to 20%. On average, this adds up to a combined rate of 25%, or a refund of about \$50 on your \$200 donation.

If your donations exceed \$200 you can claim a federal tax credit of 29%, while the provincial credit ranges from 11% to 24%. On average, you'll receive a refund of 45% of your donation.

Note that the donation tax credit reduces the amount of tax you owe, rather than your taxable income. This means that the credits are generally worth the same for Canadians of every income level.

If your annual charitable donations don't amount to much more than \$200, consider saving your receipts until you accumulate a larger amount and can take advantage of the higher tax credits. You may also combine your receipts with those of your spouse.

You are allowed to carry your donations forward for five years. As well, during your lifetime, you may claim donations of up to 75% of your net income annually. In the year of death, donations can be as much as 100% of your net income, and any excess donations can be carried back to offset as much as 100% of the preceding year's income. Donations made through your will are treated as though they were made immediately prior to your death and can be deducted on the final return, again with the capability of being carried back to the preceding year.

Keep in mind that the Canada Revenue Agency (CRA) has been denying charitable tax credits in "buy-low, donate-high" schemes. In these arrangements, a donor received a receipt higher in value than the actual cost of the donated property. The value of a gift you make to charity is now limited to your own cost of the property.

Donating securities in-kind

If you have mutual funds or other securities that have increased in value, consider donating them in-kind. The 2006 Federal Budget eliminated the taxation of capital gains on in-kind transfers of publicly traded securities and mutual funds that occur on or after May 2, 2006 (the 2006 budget applied to registered charities, and the rules were extended to registered private foundations in the 2007 budget.) You will still receive a donation receipt for the fair market value of the securities on the date of the transfer.

To see the effect of this capital gains rule, compare the tax treatment of Michael and Sharon below. Both are at an assumed top marginal tax bracket rate of 45%.

	Michael (Cash donation)	Sharon (In-kind donation)
Market value of donation	\$ 100,000	\$ 100,000
Adjusted cost base	<u>(20,000)</u>	<u>(20,000)</u>
Capital gain	\$ 80,000	\$ 80,000
Taxable gain (50% vs. 0%)	\$ 40,000	\$ 0
Tax on capital gain (at 45%)(A)	(\$ 18,000)	(\$ 0)
Tax benefit on gift (at 45%)(B)	<u>\$ 45,000</u>	<u>\$ 45,000</u>
Net tax benefit (A + B)	\$ 27,000	\$ 45,000
Tax saving from donating shares instead of cash		\$ 18,000

If you decide to transfer your securities in-kind, you will need to coordinate the transfer with your chosen charity. If the charity does not have an existing account with your financial institution, it will be required to

submit an account application form along with its corporate resolution. In addition, it may provide a request to redeem the securities immediately. This is just in case the securities drop in value after the date of transfer. The charity is still required to issue a charitable receipt for the full value as of the date of transfer. Then when you complete your Schedule 3 at tax time, you will also need to attach CRA Form T1170, Capital Gains on Gifts of Certain Capital Property.

Publicly listed securities acquired with employee stock options can similarly be gifted to a registered charity. Your employment benefit that is included in your taxable income is reduced similarly to 0% as a result of the 2006 Federal Budget.

Note that the 2011 Federal Budget requires a capital gain to be recognized when donating newly acquired flow-through shares. The rules will apply where a taxpayer acquired flow-through shares on or after March 22, 2011, without regard to the charitable donation in-kind capital gain exemption.

Tax consequences of gifting

Gifting may have immediate tax consequences that you will need to consider before transferring your gift to a registered charity. For example, if you are gifting an asset other than cash or in-kind securities, you will have an immediate taxable capital gain, but will not be taxed on future capital gains.

Gifts of life insurance

Another common method of gifting is through a life insurance policy. There are several different ways of using a policy to benefit a charity. One way is to purchase a new policy to be owned by the charity, based on your life expectancy, with the charity as the beneficiary. You pay the premiums during your lifetime, for which you receive an annual donation receipt.

An existing policy can also be transferred to the charity. The amount of the donation is the cash surrender value of the policy in the year of transfer, and subsequent premiums will generate donation receipts in the later years. Be aware that the policy is deemed disposed on transfer and tax may be due at that time. (These policies do not benefit from the special rules for in-kind securities.)

You can also simply name a charity as the beneficiary of a policy you hold in your name. Upon death, the death benefit of the policy will be paid to the charity, and your estate will receive a tax credit. This will qualify as a donation made in the terminal year, allowing for the 100% offset of net income and potential carry-back to the prior year detailed above.

Alternatively, you could name your estate as the beneficiary of the life insurance policy, with a bequest of the proceeds to the charity in your Will. You may wish to do the latter if the proceeds will first be used to pay final expenses. Again, the carry-back rules to terminal year will generally apply. If however the executor has been given discretion in the amount of the donation, the CRA may deem this to be the estate's donation and disallow any carry-back. Accordingly, the desired effect should be clearly discussed with the lawyer drafting the Will.

Gifting your RRIF

You may find yourself in the enviable position of not requiring the income from your RRIF in your retirement years. Instead, if you decide you'd rather help your favourite charity, you can reduce your tax at the same time. If you donate the annual income from your RRIF to a charity, you'll receive a donation receipt in return.

In addition, you can name the charity as the beneficiary of the RRIF or RRSP, so that upon your death the charity will receive the proceeds of your plan. The designation can be made directly on the plan, or through a Will. Keep in mind that the date of death value of your RRIF or RRSP will be included on your final income tax return.

When naming a charity as beneficiary, make sure to indicate the proper name of the charity, to avoid confusion.

Advanced strategies

There are several strategies that are somewhat more complex that you may wish to consider, especially if you have a sizable amount to donate. The explanations below are somewhat simplified. In order to properly implement these strategies you should obtain professional advice.

Charitable gift annuities. Your donation is used to purchase an annuity that generates a guaranteed annuity payment to you based on your life expectancy, with part of each payment being taxable as interest and with the remaining part of the payment being a tax-free return of capital.

Residual interest in real property. Perhaps you would like to make a substantial gift to charity but your only major asset is your home. You could donate the residual interest in your home to your chosen charity but continue to have the use and enjoyment of it for as long as you live. When you make the transfer to charity, you will receive a tax receipt for the residual value of the home. (This should be calculated by an actuary.) You must deduct the tax credit within five years. If the home is a principal residence, there will be no capital gain upon the transfer, due to the principal residence exemption. As well, because your home does not form part of your estate, probate tax will not be applied.

Charitable remainder trust. In this strategy, you establish an inter vivos trust and make the charity the capital beneficiary. The income from the trust is payable to you as the donor during your lifetime. Real property or personal property such as stocks or paintings can be transferred to the trust, with the charity as the capital beneficiary. At the time of transfer, the ownership of the property will vest with the charity and you will receive a donation receipt. Again, an actuary would need to calculate the value of the residual interest.

What are your best options?

Charitable giving and planned giving in particular, are considerations in estate planning. These should be considered along with effective tax planning and other general estate planning priorities. As every individual's situation is unique, it is important to consult with your advisor, lawyer and/or tax advisor to determine your best options. It is wise to review your plan from time to time, or as your circumstances change.

For more information about this topic, contact your advisor, call us at 1.800.874.6275 or visit our website at www.invesco.ca.

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