

# Financial Planning

## STRATEGIES FOR CHARITABLE DONATIONS

### How to give possessions away but still use them

By **KAREN J. COOPER**  
and **THERESA L.M. MAN**

Planned giving generally involves making a charitable gift in a way that maximizes tax and other financial benefits for your clients.

For most clients, planned giving will involve identifying select charities to receive bequests in order to offset certain tax consequences on death, perhaps determining the optimal annual giving amount to avoid a shift to a higher tax bracket.

Or in some instances, the idea may be to structure a more significant one-time donation to offset a particular tax event, such as a transaction that will trigger substantial unsheltered taxable capital gains.

For high net worth clients, planned giving can become more complex. Beginning with the fairly straightforward considerations involved in taking advantage of the recent elimination of taxable capital gains on donations of publicly listed shares, including flow-through shares, and ecological gifts, gift planning for the high net worth client can sometimes progress to more complex structures involving charitable remainder trusts and gifts by wills. Finally, for clients wishing to follow in the path of recent high-profile philanthropists, establishing a private foundation may be the preferred option.

In the 2006 budget, the federal government eliminated the capital gains tax on certain gifts of publicly listed securities and ecologically sensitive land to charitable organizations and public foundations.

As a result, donors are no longer taxed on any of the capital gain

accrued on donated property and receive the full benefit of the donation tax credit.

For example, a donation of publicly traded shares or an ecological gift with an adjusted cost base of \$100 and a full market value of \$1,000 will result in no taxable capital gain, and the entire amount of the donation tax credit of \$262 will be available to reduce tax on other sources of income.

As a result, the tax benefit arising from a gift of publicly traded securities or ecologically sensitive land is now the same as if it were a gift of cash. However, it is much more cost-effective to donate securities than cash, since the securities only cost \$100.

The tax benefits of donating publicly traded securities increase even further if the securities being donated are flow-through shares. The current tax rules related to such securities effectively permit corporations to renounce or “flow-through” income tax deductions associated with certain expenditures in the oil and gas or mining sectors to investors.

The expenditures deducted on a current basis by the investor reduce the cost base of the shares held. Once the exploration is complete, investors typically exchange the flow-through shares for normal securities of the issuer (on a tax deferred basis).

Since flow-through shares are generally deemed to have a cost of nil, a significant capital gain would otherwise occur if the securities were sold, but would not be subject to tax if donated.

**Charitable remainder trusts**



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In general terms, a charitable remainder trust is created by a donor who gifts a residual (or remainder) interest in property to an irrevocable trust for the benefit of a charity, while retaining the right to use and enjoy the property, including the right to receive income from the property, for a specified period (usually the donor's life).

The donor has a present “life interest” in the property, which will expire upon the death of the donor, and the charity receives a future interest in the trust consisting of the remainder of the property available when the life interest expires. In an *Interpretation Bulletin* (IT-226R) currently under review, the Canada Revenue Agency (CRA) has indicated it will accept the immediate issuance of a donation tax receipt to the donor for the present value of the gift of the residual interest in certain limited circumstances, thus enabling the donor to obtain the tax benefit of the gift even though the charity may not actually receive the property until the death of the donor.

The main advantage of a chari-

table remainder trust as a planned giving tool is the ability of the donor to immediately claim a donation tax credit in respect of a deferred gift, while continuing to enjoy the property or receive income. This is particularly attractive for individuals wishing to make a significant donation of property during their lifetime, but who still require the use of the property or a guaranteed income stream. In addition, property transferred to a chari-

table remainder trust during the donor's lifetime will not form part of the donor's estate, and will not be subject to probate fees or provincial dependant's relief legislation.

#### Charitable donations in wills

While the *Income Tax Act* provides some tax relief to a donor for charitable gifts made during his or her lifetime, the tax relief is greater

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## Beyond 'dangerous' thinking

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changed. The entire financial services industry is slowly offering tax services, yet the public accounting industry almost refuses to expand personal planning services,” Rosentreter said.

“Most CAs in public practice are still more comfortable with the traditional services and even fear offering financial planning. That's dangerous thinking in my opinion.”

He added that he regularly works with accounting firms to help sustain their client base, but he also feels the modern business sector is setting up accounting firms to lose clients, an important

issue that he thinks needs to be addressed.

“The world of financial services is changing—banks, insurance companies, and law firms are all offering broader services to help their clients in more ways. I see obtaining a CFP and offering planning services as the way for an accountant to compete in the same way,” Rosentreter said. “Plus the additional revenue from financial planning services can easily reach six figures annually in an accounting firm.”

Although it seems clear that designated CAs will benefit as professionals by expanding the breadth and depth of the services they offer, the importance of

being a sound financial planner is becoming more crucial and necessary than ever before in terms of attracting and retaining clients.

“CAs have for a long time seen the synergy between accounting and financial planning. As CAs have continued to branch out beyond the traditional aspects of accounting over the past decade, the provision of personal financial advice – financial planning in particular – has become more and more important,” Forristal said. “Chartered accountants are appropriately positioned and well equipped to take on this challenge by furthering their education and validating their expertise through CFP certification.”

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# Financial Planning

## CREATIVE ALTERNATIVES ARE AVAILABLE Use RESPs for a developmentally delayed child



**MERRICK  
WEALTH**

By  
**Peter  
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As parents, we do our best to help open doors, which will provide our children with opportunities to continue learning. Children with developmental difficulties may not be interested in or able to attend university or college, however this does not preclude them from developing other interests and skills through post-secondary educational opportunities.

Registered Education Savings Plans provide a method of saving for post-secondary learning by allowing you to earn investment income in a tax-deferred environment.

Individual plans can be set up for the benefit of an individual beneficiary while family plans accept contributions for more than one beneficiary.

The maximum annual contribution to an RESP is \$4,000 for each beneficiary. These contributions are

not tax deductible. The federal government provides a grant of 20 cents for each dollar contributed, up to a maximum of \$400 each year and a lifetime limit of \$7,200.

Recently they have announced that there will be an additional grant for families with an income below \$70,000. The grant on the first \$500 contributed will be 40 per cent for families with incomes below \$35,000 and 30 per cent for families with incomes between \$35,000 and \$70,000. Contributions can be made for a period of 21 years and the maximum contributions for each beneficiary are limited to \$42,000.

An RESP must be terminated by the end of the year that includes the 25<sup>th</sup> anniversary of the plan. Parents have always had the assurance that if their child decides not to pursue post-secondary education, their capital contributions to the savings plan would be returned to them tax-free. They now have the additional assurance that up to \$50,000 of the income that accumulates in the RESP can be transferred into their RRSPs, to the extent that they have unused contribution room available.

Alternatively, parents can withdraw the RESP income and pay tax at their marginal rate plus an additional 20 per cent, to offset the interest earned on the grant. The grant portion is returned to the federal government.

It is now also possible to roll

over the educational assistance payments, without tax implications, to another family member, so long as the beneficiary is under 21 years of age and is related by blood or adoption. In the case of an RESP in the family plan format, educational assistance payments can be paid out to another family member as long as the same qualifying criteria are followed.

To disburse the funds from the RESP the education facility must be a "designated educational institution", with a "qualifying educational program" The school must qualify under the Canada Student Loans program or be certified by the minister of human resources as an educational institution that will provide courses that will develop or improve skills in an occupation or vocation.

A "qualifying educational program" is not less than three consecutive weeks and provides that each student spend not less than 10 hours per week on courses or work in the program. The in-class portion of a recognized apprenticeship can also be included.

There are a huge variety of courses offered at post secondary schools, which meet these qualifications. Lawyer Kenneth C. Pope, one of the most experienced legal practitioners in Ontario providing legal services to families with a member who has a disability, says

"courses can be created specifically to meet the special needs of adult children. For example, a group of families in Ottawa arranged for a program of classes designed for their 25 children at Algonquin College. The course curriculum was created for their continuing education and interest, after leaving high school at 21. This is an approved post-secondary program. A little creativity goes a long way." To explore options for courses of study visit [www.canlearn.ca](http://www.canlearn.ca)

In order to make post secondary studies more attainable, students with disabilities now have the option to attend school on a part-time basis, they can access distance education courses through correspondence, take part in online learning opportunities, or they can learn through a variety of apprenticeship programs.

Once the money from the RESP has been distributed to the beneficiary, the income earned in the plan, plus the amount of federal contributions, are taxed as income of the beneficiary. As a student your child will probably not have much other taxable income and will be eligible for the tuition and education tax credits, therefore he or she will have little to pay in taxes.

While in pursuit of post secondary education, Ontario Disability Support Payments, (ODSP) continue to be received by the child.

These payments cover the cost of accommodation and food and are considered non-taxable income. RESP funds are used for tuition and books. It is very important that if there is a residential or meal plan component, this not be paid with RESP funds. Separate paperwork should be kept in order, otherwise there would be a deemed overpayment of ODSP and a surprise claw back of 'overpayments' due to simple misapplication of funds for the wrong use according.

Although students with developmental difficulties face a number of challenges, most post-secondary learning facilities offer exceptional services for students with disabilities.

Registered Education Savings Plans are a practical tool, which can be utilized for systematically saving funds to provide for a wide variety of possible post-secondary learning experiences, both for able students and for those who face a variety of developmental and cognitive challenges.

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## Make sure limits of private foundations understood

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for gifts that are made as a result of the donor's death. Pursuant to subsection 118.1(5), a donation tax credit for a gift made through an individual's will can be claimed in the individual's terminal tax return, or in the year immediately prior to death for up to 100 per cent of the deceased's income in those years.

If a gift does not satisfy the requirements of subsection 118.1(5), the estate may only be entitled to a credit of 75 per cent of income. Also, a gift made through a testamentary trust may sometimes be treated as a distribution in satisfaction of the charity's income or capital interest in the trust and not a gift.

There is little case law dealing with what would constitute a gift made by will pursuant to subsection 118.1(5). Therefore, it is important for estate planners and solicitors to take into consideration CRA's interpretation of this sub-

section when drafting wills and gift planning.

Since 2001, CRA has relaxed its previously strict views in a number of respects, including allowing trustees to have discretion in determining the amount to be given to charities listed in the will and accepting the use of a formula to calculate the residue of the estate in order to determine the gift to be made from the residue.

In order for a gift made through a testamentary trust to qualify as a gift made by will, all of the criteria concerning outright gifts must be satisfied, failing which the trust may be not be entitled to claim the donation tax credit.

When a payment is made from the income of a testamentary trust, it is sometimes permissible for such payment to be recognized as a distribution in satisfaction of the charity's income interest in the trust, depending on whether it is dealing with a testamentary trust or an alter ego trust, although the test

to be applied by CRA in this regard is not clear.

### Use of private foundations

The effective use of a private foundation could be a very useful and flexible planned giving tool for an individual, providing many benefits that are not available by using other gift planning vehicles: the donor can retain control over the assets donated to the private foundation, while maintaining the donor's privacy in his or her personal affairs; other family members may be involved in the private foundation; the timing of a donation to a private foundation may be controlled to meet the donor's estate and tax planning needs, while providing the foundation and the donor with time to decide how the donated property should be used.

While there are many benefits in utilizing a private foundation, there are also limitations which might not make it a suitable planning tool for everyone in all circumstances. For

example, a private foundation is subject to many restrictions under the act in relation to its operations, including prohibitions on carrying on any business activities and acquiring control of another corporation.

Private foundations are subject to the provincial statutes that apply to charities, such as the *Charities Accounting Act*, the *Charitable Gifts Act*, and the *Trustee Act* in Ontario. The elimination of capital gains tax on gifts publicly listed securities or ecologically sensitive land explained above does not apply if such gifts are made to a private foundation and a donation of "non-qualifying securities" to private foundations is also subject to serious restrictions.

In addition, other issues that would need to be carefully addressed before establishing a private foundation include the types of charitable causes that the foundation would support, whether the foundation would be established as

a trust or a corporation, the jurisdiction under which the foundation would be incorporated, and how the foundation would be structured.

Other structures that this article does not deal with, but which should be considered for high net worth clients include gifts of life insurance, charitable annuities, and using joint partner trust or alter ego trusts as will substitutes.

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