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**NEW DISBURSEMENT QUOTA RULES
UNDER BILL C-33**

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(Current to April 18, 2005)

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A. INTRODUCTION

The disbursement quota is a prescribed amount that registered charities must disburse each year in order to maintain their charitable registration. The purpose of the disbursement quota is “to ensure that most of a charity’s funds are used to further its charitable purposes and activities; to discourage charities from accumulating excessive funds; and to keep other expenses at a reasonable level.”¹ A good understanding of the disbursement quota rules is important not only for charities, but also for donors and their advisors. An understanding of how charities are legally required to disburse donations is fundamental to a donor’s ability to structure gifts that meet both the needs of donor and recipient charity. Donors wishing to make donations to a charity through their private foundation will be interested to know the disbursement quota implications of such a gift. Similarly a donor wishing to donate property through the establishment of an endowment will need to be advised as to how best to structure his/her gift. The source of the gift, the nature of the proposed recipient charity, the nature of the property gifted and any restrictions that may be imposed on the gift will all have a bearing on the disbursement quota consequences of the gift.

⁺ A portion of this paper is based on a paper entitled “Recent Income Tax Amendments Affecting Charities And Gift Planning,” presented at the 12th Annual National Conference of the Canadian Association of Gift Planners, April 14, 2005, *Charity Law Bulletin* No. 67 entitled “Disbursement Quota Formula Under Bill C-33” dated March 31, 2005, and *Charity Law Bulletin* No. 69 entitled “Effect of Inter-Charity Transfers on Disbursement Quota Calculation Under Bill C-33,” dated April 12, 2005, all prepared by Theresa L.M. Man and Terrance S. Carter and available at www.charitylaw.ca.

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¹ See Information Circular RC 4108, *Registered Charities and the Income Tax Act*, updated May 7, 2002, and available at <http://www.cra-arc.gc.ca/E/pub/tg/rc4108/rc4108eq.html>.

On March 23, 2004 the Department of Finance released the Federal 2004 Budget (the “March 2004 Budget”), which included significant proposed amendments to the *Income Tax Act* (the “Act”)² pertaining to the calculation of the disbursement quota. The March 2004 Budget represents a major initiative by the Federal Government in rewriting the tax rules concerning the taxation and administration of charities and reflects, to a large extent, the proposals of the Voluntary Sector Initiative’s Joint Regulatory Table contained in its report of March 2003 “Strengthening Canada’s Charitable Sector: Regulatory Reform”, particularly as it relates to intermediate taxes and sanctions. In general, these initiatives include changes to the Act in the following areas:

- New intermediate sanctions and related matters, such as the transfer of assets upon revocation of charitable status and new rules regarding the annulment of registered charities;
- Prohibitions on trading in charitable donations;
- New appeal regime for registered charities, including a new internal reconsideration process and the appeal of taxes and penalties to the Tax Court of Canada;
- Transparency and accessibility of information concerning registered charities, including release of more information to the public concerning registered charities and organizations that are denied registration, inclusion of more information on official tax receipts, and increased information on Canada Revenue Agency’s (“CRA”) website; and
- New disbursement quota rules.

Draft amendments to the Act were released on September 16, 2004 (the “September 2004 Amendments”) to implement the changes announced in the March 2004 Budget. On December 6, 2004, the September 2004 Amendments were further amended by a Notice of Ways and Means Motion tabled by the Minister of Finance in the House of Commons (the “December 2004 Amendments”). The December 2004 Amendments were introduced as Bill C-33, *A Second Act to Implement Certain Provisions of the Budget Tabled in Parliament on March 23, 2004*. Bill C-33 was passed by Parliament on February 25, 2005, and received first reading by the Senate on March 7, 2005. On April 12, 2005, the second reading of Bill C-33 was introduced in the Senate.

These initiatives represent the most significant revision of the tax rules affecting charities under the Act in the last twenty years and will affect charities for many years to come.

² R.S.C. 1985, c. 1 (5th Supp.).

This paper will focus on an aspect of these proposed changes, namely the disbursement quota rules. While Bill 33 rectifies a number of technical problems regarding disbursement quota involving charities, most of which were identified in submissions by the Charities and Not-for-Profit Law Section of the Canadian Bar Association over the last three years, it also introduces new concepts and complexities. The first part of this paper will outline the disbursement quota rules that were in place prior to Bill C-33. The second part of this paper explains the new disbursement quota rules under Bill C-33.

B. SUMMARY OF DISBURSEMENT QUOTA RULES PRIOR TO THE PROPOSED AMENDMENTS

Before examining the new disbursement quota rules under Bill C-33, it is necessary to review the disbursement quota rules that are in place prior to the proposed amendments. The disbursement quota for charitable organizations, public foundations and private foundations are different.³ Disbursement quota is defined in paragraph 149.1(1) of the Act.⁴

1. Charitable organizations

Prior to the proposed amendments, the disbursement quota for a charitable organization is the total of two figures, i.e. variables “A” and “A.1”, used in an algebraic formula contained in subsection 149.1(1) of the Act. Variable “A” is defined as 80% of the total of all amounts each of which the charity issued a donation receipt in its immediately preceding taxation year, other than the following:

- (a) a gift of capital received by way of bequest or inheritance;
- (b) a gift received subject to a trust or direction to the effect that the property given, or property substituted therefor, is to be held by the charity for a period of not less than 10 years (this is commonly known as “ten-year gifts”); and

³ For a discussion on the definitions for charitable organizations, public foundations and private foundations, please see *Disbursement Quotas: What are they and how to comply*, by M.E. Hoffstein and Adam Parachin, presented at the 2nd National Symposium on Charity Law on April 14, 2004. For a discussion on the changes to these definitions proposed by draft amendments to the Act introduced on December 20, 2002 and consolidated in draft amendments to the Act introduced on February 27, 2004, please see *Charity Law Bulletin* No. 21 dated April 30, 2003 and *Charity Law Bulletin* No. 40 dated March 29, 2004.

⁴ Although the definition for disbursement quota in paragraph 149.1(1) only makes reference to charitable foundations, this definition in effect also applies to charitable organizations – See paragraph 149.1(2)(b) and definition for “disbursement excess” in subsection 149.1(21) of the Act.

- (c) a gift received from another registered charity.

Variable “A.1” is defined as 80% of the amounts that are (1) gifts that were previously excluded from the charity’s disbursement quota when calculating variable “A” above, by virtue of being either (i) capital received by way of bequest or inheritance for taxation years that begin after 1993 or (ii) ten-year gifts whenever they were received, and (2) spent by the charity in the year.

2. Public foundations

Prior to the proposed amendments, the disbursement quota for a public foundation is set out in the following formula:

$$A + A.1 + B + \{C \times 0.045 [D - (E + F)]\} \div 365 + G$$

In other words, the disbursement quota for a public foundation is the total of the following amounts:

- (a) Variables “A” and “A.1” are the same as above in relation to the disbursement quota for charitable organizations.
- (b) Variable “B” is 80% of all amounts received from other registered charities in its immediately preceding taxation year, other than specified gifts.⁵
- (c) 4.5% of variable “D”, having first deducted variables “E” and “F” from “D” (where variable “C” in the formula is the number of days in the taxation year).
- (d) Variable “D” is the average value (i.e. the “prescribed amount”) of assets of the public foundation in the immediately preceding 24 months that was not used directly in charitable activities or administration of the foundation. Sections 3700 to 3702 of the

⁵ Summary Policy CSP – S12 dated September 3, 2003 indicates that a specified gift is “a gift from one registered charity to another, where the charities involved choose to make the transfer without affecting the disbursement quota of either charity.” A gift becomes a specified gift if the transferor charity identifies it as such in its information return for the year. Information Circular RC 4108, entitled *Registered Charities and the Income Tax Act*, explains that the transferor charity cannot use a specified gift to satisfy its own disbursement quota. If the recipient charity is a charitable foundation, specified gifts received would not increase its disbursement quota. If the recipient charity is a charitable organization, it would not benefit from receiving a specified gift because it does not have to include gifts received from other registered charities.

Income Tax Regulations provide a detailed mechanism to calculate the “prescribed amount” for purposes of calculating “D”.

- (e) Variable “E” is $\frac{5}{4}$ of the total of “A” and “A.1” for the year, i.e. 100% of the amounts included when calculating “A” and “A.1” referred to above, rather than 80%.
- (f) Variable “F” is $\frac{5}{4}$ of “B”, i.e. 100% of all amounts received from registered charities in its immediately preceding taxation year, other than specified gifts.
- (g) Variable “G” refers to a defined amount in the first 10 taxation years of a public foundation commencing after 1983, and therefore is no longer relevant today.

3. Private foundations

For a private foundation, the disbursement quota is the same as that for a public foundation, except:

- (a) When calculating variable “B”, 100% of all amounts received from a registered charity in its immediately preceding taxation year are included in the disbursement quota, rather than 80%.
- (b) Variable “F” is the same as variable “B” (i.e. 100% of all amounts received from other registered charities in its immediately preceding taxation year), rather than $\frac{5}{4}$ of “B” because 100% of the amounts has already been taken into account when calculating variable “B”.

4. Summary

Table 1 below summarizes the disbursement quota rules that are in place prior to the proposed amendments under Bill C-33.

Table 1: Calculation of Disbursement Quota Under the Rules Prior to Bill C-33

Registered Charities	Disbursement Quota = A + A.1 + B + {C x 0.045 [D – (E + F)]}+365 + G			
	“A”	“A.1”	“B”	{C x 4.5% [D – (E + F)]}+365
Charitable Organizations	80% of the all amounts each of which the charity issued a donation receipt in its immediately preceding taxation year, other than: (a) a gift of capital received by way of bequest or inheritance; (b) a ten-year gift; and (c) a gift received from another registered charity	80% of the amounts that are (1) gifts of (i) capital received by way of bequests or inheritance for taxation years that begin after 1993 and (ii) ten-year gifts whenever received, (2) have previously been excluded from the charity’s disbursement quota when calculating “A”, and (3) are spent by the charity in the year	N/A	N/A
Public Foundations	same as above	same as above	80% of all amounts received from other registered charities in its immediately preceding taxation year, other than specified gifts	4.5% of [“D” - “E” - “F”] “D” = average value of assets of the foundation in the immediately preceding 24 months that were not used directly in charitable activities or administration of the foundation “E” = 5/4 of (“A” + “A.1”) = 100% of (“A” + “A.1”) “F” = 5/4 of “B” = 100% of all amounts received from registered charities in its immediately preceding taxation year, other than specified gift
Private Foundations	same as above	same as above	Same as above, except 100%, rather than 80%	Same as above, except that “F” = “B”, not 5/4 of “B”

C. DISBURSEMENT QUOTA RULES UNDER BILL C-33

1. Proposed new disbursement quota formula

The following new algebraic formula for the disbursement quota is introduced by the September 2004 Amendments:

$$A + A.1 + A.2 + B + \{C \times 0.035 [D - (E + F)]\} / 365$$

In addition, the following changes were also introduced:

- (a) variables “A”, “A.1”, “B”, “D”, “E”, and “F” have been redefined;
- (b) new variable “A.2” has been introduced;
- (c) the 4.5% disbursement quota has been reduced to 3.5%; and
- (d) new concepts of “enduring property” and capital gains pool” have been introduced.

In December 2004, the algebraic formula for calculating the disbursement quota was revised as follows:

$$A + A.1 + B + B.1 \text{ (where } B.1 = C \times 0.035 [D - (E + F)]/365)$$

The following additional changes have been made to the formula in December 2004:

- (a) the definition for variable “A.1” is amended by inserting a new subparagraph (a)(ii) and by amending paragraph (b);
- (b) a *de minimus* threshold of \$25,000 is included for variable “D”;
- (c) the definition for variable “E” is amended;
- (d) variable “A.2” is removed; and
- (e) the formula is simplified by defining “B.1,” as being “equal to $C \times 0.035 [D - (E + F)]/365$.”

The implications of the above changes are commented upon below.

2. Reduction of disbursement quota rate

Bill C-33 proposes to reduce the 4.5% disbursement quota that applies to public and private foundations to a more manageable rate of 3.5%. Apparently, the formula that was used by the Department of Finance is based on the current real rate of return minus 20% attributable to administrative costs.

As noted in Appendix 9 of the March 2004 Budget, the 3.5% figure is intended to be “more representative of historical long-term real rates of return earned on the typical investment portfolio held by a registered charity.” The March 2004 Budget also indicates that the rate is to be reviewed periodically to ensure that it continues to be representative of long-term rates of return. However, this flexibility has not been built into the new disbursement quota formula in the Act. This would mean that changes in the economy in future may make even the 3.5% disbursement quota percentage unmanageable and would necessitate future

amendments to the Act. As such, it is regrettable that Bill 33 does not provide that the new disbursement quota percentage be prescribed by regulation rather than being written into the Act itself, as this would have accommodated future adjustments more easily.

In the event that a registered charity is not able to meet the reduced 3.5% disbursement quota, it can still apply for dispensation to reduce the disbursement quota pursuant to subsection 149.1(5) of the Act.

The reduction of the 4.5% disbursement quota to 3.5% applies to taxation years that begin after March 22, 2004.

3. Extension of 3.5% disbursement quota to charitable organizations

Prior to the proposed amendments, only public and private foundations were subject to a disbursement quota on capital assets not used in charitable activities or administration. Bill C-33 proposes that the reduced 3.5% disbursement quota on capital assets also apply to charitable organizations. The reason for this, as stated in the March 2004 Budget, is that while historically charitable foundations were the primary beneficiaries of endowments, currently both charitable organizations and foundations can and do hold capital endowments from which investment income is generated. If charitable organizations are not subject to the 3.5% disbursement quota, this investment income will not be subject to any disbursement quota obligation.

This amendment is achieved by changing the reference to “public foundation” or “charitable foundation” in the definition of disbursement quota in subsection 149.1(1) to “registered charity” and inserting references to “charitable organization” where applicable. The reduced 3.5% disbursement quota will apply to public and private foundations for taxation years beginning after March 22, 2004. For charitable organizations registered before March 23, 2004, the 3.5% disbursement quota will apply to their taxation years that begin after 2008. For charitable organizations registered after March 22, 2004, the 3.5% disbursement quota will apply to their taxation years that begin after March 22, 2004.

Paragraph 149.1(2)(b), dealing with the circumstances under which the charitable status for charitable organizations may be revoked, has also been amended to reflect that the 3.5%

disbursement quota applies to charitable organizations. Alternate wording for paragraph 149.1(2)(b) has also been introduced to deal with the transition period for charitable organizations between 2004 and 2008.⁶

However, the September 2004 Amendments failed to amend paragraph 149.1(21)(c) regarding “disbursement excess” for charitable organizations to provide a corresponding amendment (“disbursement excess” is the amount by which a registered charity’s expenditure in the year exceeds its disbursement requirements for the year). As a result, in December 2004, an amendment to paragraph 149.1(21)(c) was introduced to reflect the changes to the calculation of disbursement quota. This amendment is now contained in Bill C-33.⁷

With the removal of this key distinction between charitable organizations and foundations, there will be little functional difference between the two. The key remaining differences appear to be that (i) a charitable organization is prohibited from disbursing more than 50% of its annual income to qualified donees (i.e. it must disburse at least 50% of its annual income on its own charitable activities and (ii) foundations are restricted in their ability to incur debt.⁸ It would therefore not be surprising if the Department of Finance, as a matter of policy, eventually eliminates the distinction between charitable organizations and foundations altogether so that there would be only two categories of charities, i.e. charities and private foundations. It will be interesting to see what may transpire in this regard over the next few years.

4. De minimus threshold on the application of the 3.5% disbursement quota

One of the more significant changes brought by the September 2004 Amendments is the reduction of the 4.5% disbursement quota on investment assets of a registered charity to 3.5%, and the application of the reduced 3.5% disbursement quota to all registered charities (including charitable organizations), rather than only to charitable foundations. As a result of the application of the 3.5% disbursement quota to charitable organizations, concerns were raised in the charitable sector regarding the ramifications of the application of this requirement on small charitable organizations. In response to this concern, in December 2004, it was

⁶ See clause 35(7) of Bill C-33.

⁷ See clause 35(6) of Bill C-33 amending subsection 149.1(21) of the Act.

⁸ See subsections 149.1(2), (3) and (4).

proposed that the reduced 3.5% disbursement quota only apply to registered charities (including charitable organizations, public foundations and private foundations) if the amount of their investment assets calculated under variable “D” of the disbursement quota formula is greater than \$25,000. Where the amount of investment assets is equal to or less than \$25,000, variable “D” would be nil.

5. New concept of “enduring property”

Bill C-33 introduces a new concept of “enduring property” and proposes to amend the amount for variable “A” when calculating the disbursement quota to include 80% of the total of the eligible amounts of gifts for which the charity issued donation receipts in its immediately preceding taxation year, other than gifts that are:

- (a) enduring property; or
- (b) received from another registered charity.

The proposed definition for “enduring property” is found in subsection 149.1(1) and is defined to mean property that is:

- (a) a gift received by the charity by way of a bequest or inheritance, including a gift deemed by subsection 118.1(5.2) or (5.3) of the Act;⁹
- (b) a gift received by a charitable organization from another registered charity, where the majority of directors and trustees of the donor charity deal at arm’s length with the recipient charitable organization, provided that the gift is subject to a trust or direction requiring that the gift be utilized over a period not exceeding five years either (i) in the course of a program of charitable activities that could not reasonably be completed before the end of the first taxation year of the charity ending after the year in which the gift was received or (ii) for the purpose of acquiring a capital property to be used directly in the charitable activities (this paragraph was not included in the September 2004 Amendments, but was inserted in December 2004);

⁹ Details regarding amendments to subsections 118.1(5.2) and (5.3) of the Act concerning gifts of life insurance proceeds, registered retirement income fund and registered retirement savings plan as a result of direct beneficiary designation are explained in Section 5e) below.

- (c) a ten-year gift received by the charity (i.e. the “original recipient charity”) subject to a trust or direction that the gift, or property substituted for the gift, is to be held by the original recipient charity or by another registered charity (i.e. “transferee”) for a period of not less than 10 years from the date the original recipient charity received the gift, except that the trust or direction may permit the original recipient charity or the transferee to expend the property before the end of 10 years to the extent permitted under variable “B.1” of the definition for disbursement quota in order to meet the disbursement quota requirement (In December 2004, this paragraph was revised to clarify that paragraph (c) does not deal with gifts received from another registered charity as this is dealt with under paragraph (d) below); and
- (d) a gift received by the charity as a transferee of an enduring property under (a) or (c) above from either an original recipient charity or another transferee charity, provided that if it is an enduring property under (c), the gift is subject to the same terms and conditions under the trust or direction. (The English version of the amendments proposed in December 2004 erroneously made reference to paragraph (b) instead of (c). However, the French version is correct. It is anticipated that this error will be corrected by a technical bill to be introduced at a later time.)

The new definition applies in respect of taxation years that begin after March 22, 2004. The following are several observations regarding the new concept of “enduring property”:

- a) New broad concept

The term “enduring property” is very broad and include gifts received by way of bequest or inheritance and ten-year gifts that are included in the formula for variable “A” prior to the proposed amendments, as well as life insurance proceeds, registered retirement income funds and registered retirement savings plans as a result of direct beneficiary designation, gifts received by a charitable organization from another registered charity to be expended in the next 5 years or less in its charitable activities, and gifts received by the charity as a transferee of an enduring property that are gifts by way of bequest or inheritance and ten-year gifts from either an original recipient charity or another transferee charity, provided that if the gift is a ten-year gift, the gift is subject to the same terms and conditions under the trust or direction.

b) Gifts by way of bequest or inheritance: income vs. capital

In relation to gifts received by a charity by way of bequest or inheritance, these gifts will no longer be limited to “gifts of *capital* received by way of bequests or inheritance” [emphasis added] under the definition of disbursement quota prior to the proposed amendments. This means that a testamentary income interest received by a charity would now be included as part of an enduring property.

c) Gifts received by charitable organizations from other registered charities to be expended in the next 5 years or less

In December 2004, a new category of enduring property was included in paragraph (b) for a gift received by a charitable organization from another registered charity, where the majority of directors and trustees of the donor charity deal at arm’s length with the recipient charitable organization, provided that the gift is subject to a trust or direction requiring that the gift be utilized over a period not exceeding five years in the course of a program of charitable activities or for the purpose of acquiring a capital property to be used directly in the charitable activities. It appears that this provision is intended to provide a relief provision for charitable organizations.

d) Ten-year gifts subject to ability to encroach

The definition of “enduring property” will also permit ten-year gifts that are subject to trust or direction that may permit the original recipient charity or the transferee to expend the ten-year gifts before the end of 10 years to the extent permitted under the definition for disbursement quota in order to meet the disbursement quota requirement. Our comments concerning the limits on the encroachment is set out in Section 6 below.

e) Gifts made by way of direct designation

As a result of amendments to the Act introduced by the 2000 Federal Budget, payments of life insurance proceeds [paragraph 118.1(5.2)], registered retirement income fund or registered retirement savings plan [paragraph 118.1(5.3)] as a result of direct beneficiary designation were deemed to be gifts for the purposes of section 118.1 in respect of deaths that occur after 1998, provided that the requirements under subsections 118.1(5.1),

(5.2) and (5.3) are met. As such, upon the death of an individual, a charitable donation tax receipt can be provided to the estate and the executor can claim the donation tax credit on the deceased's terminal income tax return. However, CRA's technical interpretation document number 2002-0133545 dated January 16, 2003 confirms that "these payments have not been deemed to be gifts for purposes other [than] section 118.1, they are not gifts for purposes [of] the calculation of the disbursement quota pursuant to the definition in subsection 149.1(1) of the Act and, therefore, are not included therein."¹⁰

Bill C-33 addresses this drafting error by amending subsections 118.1(5.2) and (5.3) and the definition of enduring property, by including these gifts as enduring property, and therefore as such, they are included in the calculation of the disbursement quota. These gifts will be subject only to the 3.5% disbursement quota while they are held as capital by the charity and will then become subject to the 80% disbursement quota requirement in the year in which they are disbursed. This amendment applies in respect of deaths after 1998, which retroactivity may lead to hardship for charities that relied on the earlier position of CRA that such direct designations would not be included in the charities' disbursement quota from the enactment of subsections 118.1 (5.1) to (5.3) in 2000 to the present.

f) Transfer of ten-year gifts

Paragraph (d) of the definition for "enduring property" will permit a ten-year gift to be transferred to another registered charity during the ten-year period as if the ten-year gift had been received directly from the original donor, without the amount transferred affecting the disbursement quota for both the transferor charity and the recipient charity. This is further explained in Section 7 below concerning inter-charity transfers.

6. Encroachment on enduring property

Prior to the proposed amendments, variable "A.1" of the disbursement quota required that gifts received by a charity by way of bequest or inheritance or ten-year gifts that have previously been excluded in the calculation of disbursement quota under variable "A" be

¹⁰ See also CRA's *Registered Charities Newsletter*, dated April 2, 2003.

included in determining the disbursement quota in the year they are expended. A ten-year gift is “a donation that is made subject to a donor’s written trust or direction that the gift be held by a registered charity for 10 years or more.”¹¹ CRA took the position that if a ten-year gift, or property substituted for it, is expended in a year prior to the expiration of ten-years from the time the gift was given, then the entire ten-year gift, or property substituted for it, *may* be subject to the 80% disbursement quota in that year. This rule may apply even if only a portion of the ten-year gift, or property substituted for it, was expended. The word “may” is used here to denote the fact that the law and the administrative practices of CRA are unclear on this point. It is unclear from the wording of the new disbursement quota rules whether this difficulty has been addressed.

The March 2004 Budget explained that, since an annual disbursement quota is applied to funds held by charities, sometimes, a charity may prefer to meet its obligation to satisfy the disbursement quota by realizing capital gains rather than disbursing investment income earned from these funds, especially where the return on the investment is weighted heavily in favour of capital gains. However, “if the charity does so, . . . it must then meet an 80 per cent disbursement obligation to the extent that the proceeds of disposition are expended by the charity.”¹² This difficulty is caused by the fact that the 4.5% disbursement quota and the 80% disbursement quota applicable to the portion of a ten-year gift is expended in any year are *cumulative* disbursement quota obligations. Under the old rules, when an amount that has been subject of a ten-year gift is encroached on to satisfy the 4.5% disbursement quota, it is also brought into the 80% disbursement quota calculation.¹³

¹¹ See CRA RC 4108 “Registered Charities and the Income Tax Act,” May 7, 2002, and Summary Policy CSP – T06, dated September 3, 2003.

¹² See the March 2004 Budget.

¹³ For example, consider a gift of \$1,000 to a charitable foundation that is subject to a direction that it or property substituted therefor be held for a period of not less than ten years. Assume that due to the poor return on investment in the 12th year (i.e. after the ten year restriction has expired), no income is earned on the gift in a particular year. In order to meet the 4.5% disbursement quota, which would be equal to \$45, the foundation would be required to encroach on the capital (because no income is generated in that year in the example). However, since the 4.5% disbursement quota and the 80% disbursement quota are cumulative disbursement obligations, the foundation would be required to disburse 80% of the amount of the capital encroached upon to satisfy the 80% disbursement quota, leaving only 20% of the amount encroached upon to satisfy the \$45 disbursement obligation associated with the 4.5% disbursement quota. Consequently, although only \$45 of capital is required to satisfy the 4.5% disbursement quota, the foundation would be required to encroach upon a total of \$225 of capital (so that 80% of the \$225, i.e. \$180, would be used to satisfy the 80% disbursement quota and 20% of the \$225, i.e. \$45, would be used to satisfy the 4.5% disbursement quota).

The difficulty caused by the wording in the Act is addressed by the September 2004 Amendments by amending variable “A.1” of the disbursement quota to allow a charity to encroach on the capital gains of enduring property up to a maximum of the “capital gains pool” of the charity, which is another concept introduced by the September 2004 Amendments. In this regard, in the September 2004 Amendments, variable “A.1” is proposed to be defined to be equal to 80% of the amount by which the total amount of enduring property owned by the charity to the extent that it is expended in the year exceeds the lesser of (i) 4.375 per cent (i.e. 5/4 of 3.5%) of the amount determined for variable “D” and (ii) the capital gains pool of the charity for the taxation year. The definition for “A.1” has been amended in December 2004 by inserting a new subparagraph (a)(ii) to include the fair market value of enduring property transferred by the charity in the year by way of gift to a qualified donee. This does not include enduring property that was received by the charity as a specified gift.¹⁴ Further, paragraph (b) of “A.1” is amended to clarify that the amount calculated under subparagraph (a) is reduced by an amount “claimed by the charity” that may not exceed the lesser of 3.5% of the investment assets of the charity and the capital gains pools of the charity. The phrase “an amount claimed by the charity” in paragraph (b) in the definition for “A.1” would have the effect of permitting the charity to decide whether to encroach on the capital gains pool and, if so, how much to encroach. This amendment¹⁵ also means that the amount will also become eligible for capital gains reduction.¹⁶

As a result of these changes, what will be added to the disbursement quota obligation of a charity under variable “A.1” is the sum of 80% of enduring property expended by the charity under subparagraph (a)(i) and the full fair market value of enduring property transferred by the charity to a qualified donee under subparagraph (a)(ii) which sum will be reduced by the amount claimed by the charity under paragraph (b) that may not exceed the lesser of 3.5% of the investment assets of the charity under variable “D” and the capital gains pool of the charity.

This proposal will apply to taxation years that begin after March 22, 2004.

¹⁴ The new subparagraph (a)(ii) is the same as the definition for “A.2” that was removed in December 2004.

¹⁵ The amount was formerly determined under “A.2” in the September 2004 Amendments.

¹⁶ As well, as a result of the amendment to “A.1” and the removal of “A.2”, the definition for “E” is also similarly amended in December 2004.

It is important to note the following in relation to the new definition of variable “A.1”:

a) Limit on encroachment

This formula permits expenditure of enduring property provided that the expenditure is the amount claimed by the charity under paragraph (b) of “A.1” that may not exceed the lesser of 3.5% of the investment assets of the charity under variable “D” and the capital gains pool of the charity.

i) Calculation of variable “D”

The calculation for the amount for variable “D” remains substantially the same as the definition prior to the proposed amendments save and except the *de minimus* threshold of \$25,000 mentioned above, i.e. the average value (i.e. the “prescribed amount”) of assets of the charity in the 24 months immediately preceding that taxation year that was not used directly in charitable activities or administration of the charity if the amount of the investment assets calculated under variable “D” of the disbursement quota formula is greater than \$25,000. Where the amount of investment assets is equal to or less than \$25,000, variable “D” would be regarded as nil.¹⁷

ii) “Capital gains pool”

The new term “capital gains pool” applies for the purpose of the definition for “disbursement quota”, applicable to taxation years that begin after March 22, 2004. The original definition of “capital gains pool” in the September 2004 Amendments provided that generally, the capital gains pool of a registered charity for a taxation year is the total of all capital gain of the charity from the disposition of an enduring property after March 22, 2004, less the total disbursement requirement of the charity under variable “A.1” of the definition for disbursement quota in respect of the expenditure of such enduring properties in a preceding taxation year that began after March 22, 2004. This definition is modified in December 2004 to provide

¹⁷ It should be noted that the reference to variable “D” for purposes of calculating the limit on the encroachment does not take into account variables “E” or “F” as required when calculating the 3.5% disbursement quota under “B.1” which is described in the formula $\{C \times 0.035 [D - (E + F)]\}/365$. “B.1” essentially provides that in applying the 3.5% disbursement quota percentage, one would exclude items that have been taken into account in other parts of the disbursement quota as they are expended. Thus “E” is intended to back out expenditures of certain enduring property and expenditures of receipted donation because they are otherwise brought into the disbursement quota test and “F” backs out receipts from other charities which are otherwise included in variable “B”.

that the capital gains pool for a taxation year is the total of all capital gains of the charity from the disposition of enduring properties after March 22, 2004 and before the end of the taxation year, as declared by the charity in its T3010 Information Return for the taxation year during which the disposition occurred, that exceeds the lesser of the following two amounts set out in paragraph (b) in the definition for “capital gains pool”:

- The amount determined according to paragraph (a) of variable “A.1”, i.e. the total of 80% of certain enduring property expended by the charity¹⁸ and the full fair market value of enduring property transferred by the charity to a qualified donee other than enduring property that is a specified gift,¹⁹ and
- The amount claimed by the charity according to paragraph (b) of variable “A.1”, i.e. the amount claimed by the charity that may not exceed the lesser of 3.5% of the charity’s investment assets and its capital gains pool.

The capital gain from a disposition of a bequest or inheritance received by the charity before 1994 is not included. It is important to note that the capital gains pool only consists of capital gains realized by the disposition of enduring property, rather than accrued gains. Further, the concept of the “capital gains pool” appears to be based on a tax policy in imposing an arbitrary cap on the ability of charities to encroach on testamentary gifts and ten-year gifts in order to meet the 3.5% disbursement quota, instead of being able to encroach up to the amount required to satisfy the 3.5% disbursement quota.

The December 2004 Amendments require that the total of all capital gains of the charity from the disposition of enduring properties must be “declared by the charity” in its T3010 Information Return “for the taxation year during which the disposition occurred.” The Explanatory Notes to the December 2004 Amendments indicate that “annual calculation of additions to and deductions from the capital gains pool is voluntary; however, it may be of benefit to a charity to make this calculation if it expects to ever claim a reduction of its disbursement quota in

¹⁸ See subparagraph (a)(i).

¹⁹ See subparagraph (a)(ii).

respect of the expenditure of enduring property.” In other words, in practice, regardless of whether a charity expects to encroach on its capital gains pool in the year, it should conduct its annual calculation and declare the amount of all capital gains of the charity from the disposition of enduring properties on an annual basis and declare the same in its T3010 Information Return in order to be able to encroach on its capital gains pool if and when it is required to do so in the future.

As indicated above, the phrase “an amount claimed by the charity” in paragraph (b) in the definition for “A.1” would have the effect of permitting the charity to decide whether to encroach on the capital gains pool and, if so, how much to encroach.

As can be seen from the amended definition, the calculation of the capital gains pool is very complicated. The continuing focus on distinguishing between what is capital and what is income is interesting in the context of charities and disbursement quota calculation. This distinction is well known to trust lawyers because where there are different beneficiaries of income and capital, but there would appear to be no reason to make such a distinction in the charity area and in particular in the monitoring of charitable expenditures. Furthermore, the distinction between income and capital is difficult for charities to understand and is therefore often ignored. New investment vehicles such as mutual funds which provide blended income and capital payments do not lend themselves easily to determining what is income and what is capital and as such, the tracking of the capital gains pool by charities may prove to be challenging for charities to comply with in order to take advantage of the intended relief offered by the encroachment provision under the new rules.

b) Exclusion of certain enduring property

When calculating variable “A.1”, the following enduring properties will not be included:

- (a) enduring properties included in paragraph (a)(ii) in the definition for “A.1”;
- (b) enduring properties received by the charity as “specified gifts,” and
- (c) a bequest or an inheritance received by the charity in a taxation year that included any time before 1994.

The above exceptions in relation to enduring properties included in paragraph (a)(ii) in the definition for “A.1” and “specified gifts” are commented upon in Section 7 below concerning inter-charity transfers.

c) Gifts received and spent in the same year

Prior to the proposed amendments, long-term gifts (i.e. ten-year gifts and gifts received by way of bequest or inheritance) are subject to an 80% disbursement quota to the extent that the registered charity liquidates and spends the capital in the year following the year in which the gift is received. The rules prior to the proposed amendments, however, do not address the situation where the charity receives a long-term gift and disburses it in the same year. The December 2004 Amendments eliminate this loop-hole by removing the requirement under the calculation of variable “A.1” gifts that have previously been excluded from the charity’s disbursement quota. As such, it applies the 80% disbursement quota to gifts that are expended in the same year that they are received.

7. Inter-charity transfers

a) Gifts transferred to charitable organizations

Prior to the proposed amendments, only transfers from registered charities to public and private foundations are subject to the 80% disbursement quota, which mean that transfers from registered charities to charitable organizations are exempt from the 80% disbursement quota. The December 2004 Amendments propose that all transfers from one registered charity to another, including transfers to charitable organizations, will be subject to the 80% disbursement requirement.

The only exceptions are transfers involving specified gifts and enduring property. This is achieved by applying variable “B” to charitable organizations. Variable “B” is now defined to mean as follows:

- (a) in the case of private foundations, variable “B” is the total of all amounts received by it in its immediately preceding taxation year from a registered charity, other than specified gifts or enduring properties; and

- (b) in the case of charitable organizations and public foundations, variable “B” is the same as the case for the private foundation, except that the inclusion rate is 80%, rather than 100%.

This means that gifts of enduring property received from another registered charity will no longer be subject to the disbursement quota of the recipient charity in the year after the year in which it is received. Such gifts will be subject to the same requirements as those that apply to gifts of enduring property received from other persons. The exception for a “specified gift” will continue to apply. These changes will apply to transfers received by charitable organizations in taxation years that begin after March 22, 2004.

- b) Three categories of property transfers

Under the new disbursement quota rules, there are three categories of transfer of property between charities, namely specified gifts, enduring property (that has not been designated as specified gifts by the transferor charity) and other gifts which are neither enduring property nor specified gifts (which in the context of this paper are referred to as “ordinary gifts”²⁰). The impact of each of the three categories of transfers on the disbursement quota of the both the transferor charity and the transferee charity is explained below.

- c) Transfer of ordinary gifts

Under the new disbursement quota rules, a gift may be transferred as an “ordinary gift” between two charities. An ordinary gift is a gift of property which the transferor charity does not designate as a specified gift and where the property is not an enduring property as defined in 149.1(1) of the Act.²¹ Pursuant to the new disbursement quota rules, the transferor charity would be able to utilize the transfer of the ordinary gift to satisfy its disbursement quota obligation in the taxation year in which the transfer is made. With respect to the transferee charity, the receipt of the ordinary gift would create a disbursement quota obligation under variable “B” of the disbursement quota formula. If the transferee charity is either a charitable organization or a public foundation, the

²⁰ The term “ordinary gift” is not a term under the Act, but is used in this paper to refer to transfers of property that are neither specified gifts nor enduring property.

²¹ Transfers of specified gifts and enduring property are explained in the next two sections of this paper.

transferee charity would be required to expend in the following taxation year 80% of the ordinary gift received. If the transferee charity is a private foundation, the transferee charity would be required to expend in the following year 100% of the ordinary gift received. [See Example 1]

Example 1: Transfer of an ordinary gift between charities

Ordinary gifts (i.e. not specified gift, not enduring property)	Transferor charity		Transferee charity	
	DQ obligation	DQ satisfaction	DQ obligation	DQ satisfaction
Ordinary gift \$100 Charity A Charity B in year 1	N/A	\$100 expended can be used to satisfy DQ obligation of Charity A in year 1	<ul style="list-style-type: none"> • If Charity B is either a charitable organization or a public foundation: has to expend \$80 in year 2 • If Charity B is a private foundation: has to expend \$100 in year 2 (i.e. “B” in DQ formula) 	N/A
When Charity B spends the \$100 in year 2	N/A	N/A	N/A	\$100 expended can be used to satisfy DQ obligation in year 2 (must expend at least \$80 of the \$100 for a charitable organization or a public foundation and \$100 for a private foundation)

d) Transfer of specified gifts

A “specified gift” is defined under subsection 149.1(1) of the Act as “that portion of a gift, made in a taxation year by a registered charity that is designated as a specified gift in its information return for the year.” Under the new disbursement quota rules, a transferor charity that designates a gift to another charity as a specified gift is not permitted to utilize the transfer of the specified gift to satisfy its disbursement quota obligation for the year because a specified gift is deemed not to be an expenditure on charitable activities or a gift made to a qualified donee pursuant to paragraph 149.1(1.1)(a) of the Act and therefore is not included when calculating a charity’s disbursement quota obligation. With respect to the transferee charity, the transfer does not create any disbursement quota obligation because specified gifts are excluded under variables “A.1” and “B” of the disbursement quota formula. When the transferee charity

subsequently expends the specified gift it received, it would be able to utilize the expenditure of the specified gift to satisfy its disbursement quota obligation. [See Example 2]

Example 2: Transfer of a specified gift between charities.

Specified gifts (includes enduring property received as specified gifts)	Transferor charity		Transferee charity	
	DQ obligation	DQ satisfaction	DQ obligation	DQ satisfaction
Specified gift \$100 Charity A Charity B in year 1	N/A	--- Charity A cannot use the \$100 to satisfy its DQ obligation in year 1 (b/c 149.1(1.1)(a) exclusion of specified gifts)	--- Charity B is not obligated to expend any of the \$100 in year 2 (b/c specified gifts are excluded from A.1 and B of DQ formula)	N/A
When Charity B spends the \$100 in a subsequent year	N/A	N/A	N/A	\$100 expended can be used to satisfy DQ obligation in the year when the gift is expended

e) Transfer of enduring property

Bill C-33 introduced a new concept of “enduring property,” which is explained in Section C5 above. Due to a drafting error in the definition of the disbursement quota in the Act prior to the proposed amendments, if a charity transferred a ten-year gift to another charity, the transferee charity had to expend 80% of the ten-year gift in the year following the transfer of the gift. In order to avoid this result, the recipient charity would be required to recognize the amount received as a specified gift. However, in order for the amount transferred to be recognized as a specified gift, the amount had to be designated as such by the transferor charity. The disposition of the property as a specified gift by the transferor charity means that the transferor charity was not permitted to include the amount transferred in meeting its disbursement quota obligation created by the transfer itself. To overcome this difficulty, the transferor charity or the transferee charity would have to obtain relief from CRA by applying for dispensation from the application of the disbursement quota under subsection 149.1(5) of the Act.

In order to address this anomaly, the September 2004 Amendments proposed to exempt the transfer of enduring property from variable “B”. The effect of this would be that a gift of enduring property received by a charity would not need to be included in the

disbursement quota of the transferee charity. This exemption, therefore, would not require the enduring property received be expended in the following year by the transferee charity. With respect to the transferor charity, in December 2004, and a new subparagraph (a)(ii) was inserted in the definition for “A.1” to include the fair market value of enduring property transferred by the charity in the year by way of gift to a qualified donee (which does not include enduring property that was received by the charity as a specified gift).²² In addition, the effect of this amendment also means that this amount will become eligible for capital gains reduction claimed under “A.1(b)” explained in Section C6 of this paper. In this regard, the Explanatory Notes indicate that a different disbursement requirement applies for an enduring property that is expended by way of gift to a qualified donee. The charity must disburse 100% of such an amount (which requirement is satisfied by the gift itself). This means that the transferor charity would be able to include the amount of enduring property it transfers to a qualified donee in order to meet its disbursement quota obligation, which would off-set the increase in disbursement quota of the transferor charity as a result of disposing of the enduring property to the qualified donee. This proposal also applies to taxation years after March 22, 2004.

Under the new disbursement quota rules, when a charity transfers an enduring property to another charity (and does not designate the enduring property as a specified gift), the transfer would create a disbursement quota obligation on the transferor charity to expend 100% of the value of the property in the year of the transfer under variable “A.1(a)(ii)” of the disbursement quota formula. This disbursement quota obligation on the transferor charity would be satisfied by the transfer itself, i.e. the transferor charity would include this transfer in satisfying its disbursement quota obligation for the year. With respect to the transferee charity, the receipt of the enduring property would not create a disbursement quota obligation on the charity, because enduring property is not included in variable “B” in the disbursement quota formula. Upon the subsequent expenditure of the enduring property by the transferee charity, the expenditure will create a disbursement quota obligation on the charity so that it is required to expend 80% of the

²² In the September 2004 Amendments, a new variable “A.2” inserted, which was defined in paragraph 149.1(1) to mean the fair market value (at the time of the transfer) of enduring property (other than enduring property that was received by the charity as a specified gift) transferred by a charity in the taxation year by way of a gift to a qualified donee. Variable A.2 was replaced in December 2004 by the insertion of a new subparagraph (a)(ii) in the definition for variable “A.1.”

enduring property in the year under variable “A.1(a)(i)” of the disbursement quota formula. The expenditure itself would be utilized to satisfy the disbursement quota obligation of the charity in the year. [See Example 3]

Example 3: Transfer of an enduring property between charities

Enduring property	Transferor charity		Transferee charity	
	DQ obligation	DQ satisfaction	DQ obligation	DQ satisfaction
Enduring property \$100 Charity A Charity B (provided that the property was not received as a specified gift)	Charity A will be required to expend 100% of the fmv of the enduring property (i.e. \$100 in this case) in year 1 under A.1(a)(ii) in DQ formula,	\$100 expended can be used to satisfy DQ obligation in year 1 (which would in and of itself satisfy the DQ obligation created by making the gift under A.1(a)(ii) in DQ formula	--- no effect on DQ (b/c EP is exempt from B in DQ formula)	--- no effect on DQ until such time as Charity B expends the gift
	Net effect = DQ neutral for transferor charity			
When Charity B expends the \$100 in a subsequent year	N/A	N/A	When Charity B expends the gift in a subsequent year, Charity B will be required to expend at least \$80 in the year when the gift is expended (i.e. A.1(a)(i) in DQ formula)	\$100 expended can be used to satisfy the DQ obligation in the year when the gift is expended (which would in and of itself satisfy the DQ obligation created by making the gift under A.1(a)(i) 2), in DQ formula (must expend at least \$80 of the \$100)

If the enduring property being transferred was designated by the transferor charity, either inadvertently or purposefully, as a specified gift, such a designation would not cause any negative effect on the disbursement quota of the transferee charity because variables “A.1” and “B” exempt specified gifts received from being included in the transferee charity’s disbursement quota. However, the transfer itself would create a disbursement quota obligation on the transferor charity in the year of the transfer under variable “A.1(a)(ii)” of the disbursement quota formula, because the expenditure of a specified gift is not exempt from variable “A.1(a)(ii).” However, the transferor charity would not be able to use the transfer itself to satisfy the disbursement quota obligation, including the disbursement quota obligation created by this transfer, because it is transferred as a specified gift.²³ This means that the transferor charity would need to utilize other expenditures in the year to satisfy both the disbursement quota obligation created by this transfer and its other disbursement quota obligation. The effect of these

²³ See explanation above concerning transfers of specified gifts.

rules is that there does not appear to be any reason for the transferor charity to transfer an enduring property as a specified gift, in fact it may be dangerous to do so for the transferor charity. The situation where a transferor charity may agree to designate a gift of enduring property to another charity as a specified gift is where the transferor charity has sufficient disbursement excess from previous year(s) that it could utilize to satisfy the disbursement quota obligation created by such a transfer and there may be some benefit to the recipient charity on receiving the gift as a specified gift so that the transfer would not ever impact its disbursement quota obligation. [See Example 4]

Example 4: Transfer of an enduring property designated as a specified gift between charities

Enduring property	Transferor charity		Transferee charity	
	DQ obligation	DQ satisfaction	DQ obligation	DQ satisfaction
Enduring property \$100 If Charity A Charity B but Charity A designates it as specified gift	Charity A will be required to expend \$100 in year 1 under A.1(a)(ii) in DQ formula	---	---	N/A
	By designating the transfer as a specified gift, Charity A will have to meet the A.1 DQ obligation created by this transfer with other expenditure	Charity A cannot use the \$100 to satisfy its DQ obligation in year 1 (b/c 149.1(1.1)(a) exclusion of specified gifts)	Charity B is not obligated to expend any of the \$100 in year 2 (b/c specified gifts are excluded from A.1 and B of DQ formula)	
When Charity B spends the \$100 in a subsequent year	N/A	N/A	N/A	\$100 expended can be used to satisfy DQ obligation in the year when the gift is expended

f) Factors to consider in determining how to categorize inter-charity transfers

Since different categories of transfer impact on the disbursement quota obligation and disbursement quota satisfaction of the transferor charity and the transferee charity differently, in deciding how to categorize a transfer of assets from one charity to another charity, the following questions would need to be asked:

Question (1) Is the property an enduring property?

Question (2) Does the transferor charity require the disbursement to satisfy its disbursement quota obligation for the year and/or disbursement quota shortfall from prior years?

If the answer to question (1) above is “no,” and if the answer to question (2) is “yes,” then the transferor charity would want to transfer the property as an ordinary gift, not as a specified gift, in order to be able to utilize the transfer to satisfy its disbursement quota obligation. However, the transferee charity would need to include the transfer in its disbursement quota obligation for the following year. If, however, the transferor charity transfers the property as a specified gift, the transferor charity cannot use the transfer to satisfy its disbursement quota obligation for the year and the transfer does not create any disbursement quota obligation for the transferee charity.

If the answers to both questions (1) and (2) above are “no,” then the transferor charity may choose to transfer the property either as an ordinary gift or as a specified gift. If the property is transferred as an ordinary gift, and since the transferor charity does not need to include the transfer in order to satisfy its disbursement quota obligation for the year, the transfer will lead to a disbursement quota excess for the transferor charity for use in future years. The transferee charity would need to include the transfer in its disbursement quota obligation for the following year. If the property is transferred as a specified gift, the transferor charity cannot use the transfer to satisfy its disbursement quota obligation for the year, which is not problematic for the transferor charity since its response to (2) is “no.” The transfer would not create any disbursement quota obligation for the transferee charity.

If the answer to question (1) above is “yes” and if the transferor charity transfers the enduring property to the transferee charity, the transfer would create a disbursement quota obligation on the transferor charity, which disbursement quota obligation will be satisfied by the transfer itself. If the answer to question (2) is “yes,” the transfer would not be of benefit to the transferor charity in relation to the satisfaction of its other disbursement quota obligation because the transfer would be utilized to satisfy the disbursement quota obligation by the transfer itself. In relation to the transferee charity, the transfer would not affect its disbursement quota obligation until it is expended by the transferee charity.

If the answer to question (1) above is “yes” and if the transferor charity transfers the enduring property as a specified gift to the transferee charity, the transfer itself would

create a disbursement quota obligation on the transferor charity in the year of the transfer and the transferor charity would not be able to use the transfer itself to satisfy the disbursement quota obligation created by this transfer or any other disbursement quota obligation of the transferor charity (i.e. if the answer to question (2) is “yes”). This means that the transferor charity would need to use other expenditure in the year to satisfy both the disbursement quota obligation created by this transfer and its other disbursement quota obligation. The transfer does not create any disbursement quota obligation for the transferee charity.

g) Transfer as a result of penalty

Subsection 149.1(1.1) of the Act provides that a gift or expenditure made by a registered charity will not be considered in determining whether it has met its annual disbursement quota if the gift is made by way of a specified gift or if the expenditure is on political activities. Subsection 149.1(1) will be amended by the September 2004 Amendments, consequential to the amendment of Part V of the Act in respect of taxes and penalties for which the charity is liable under subsection 188(1.1) or section 188.1 of the Act. Now paragraph 149.1(1.1)(c) provides that a transfer to another registered charity under that Part does not qualify as an expenditure for the purposes of calculating the transferor’s disbursement quota. This amendment will apply in respect of notices of intention to revoke the registration of a charity and to notices of assessment issued by the Minister after the day that is 30 days after Royal Assent.

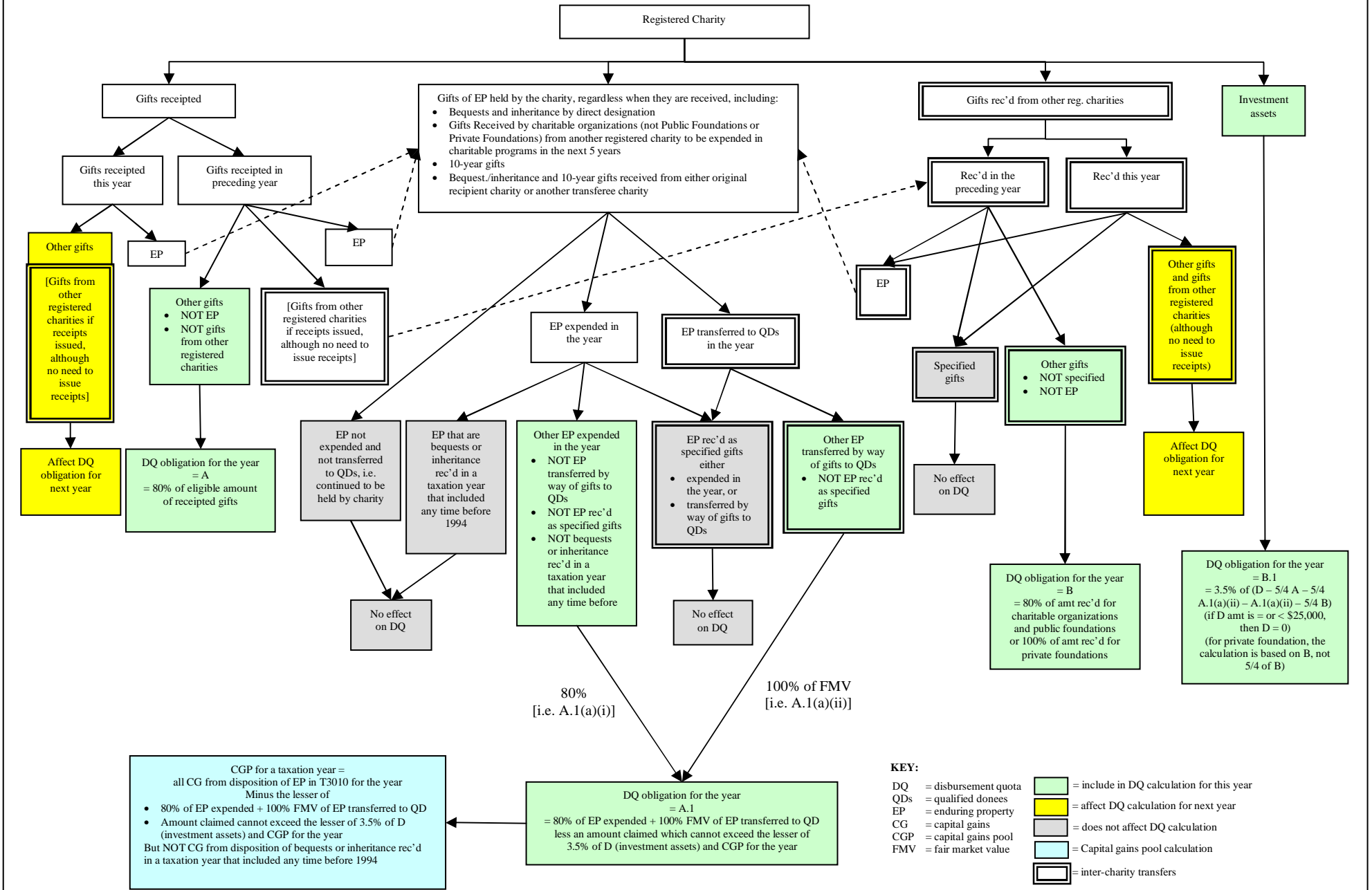
8. Summary of the proposed new disbursement quota rules

Set out below are a table [see Table 2] and a flow chart summarizing the calculation of the disbursement quota in order to assist charities and their advisors in developing a better understanding of the new rules. For ease of reference, the flow chart has been color coded to reflect the effect of gifts of different types of property and property transfers between charities on the disbursement quota calculation. Both the table and flow chart are intended to be self-explanatory.

Table 2: Calculation of Disbursement Quota Under Bill C-33

Registered Charities	Proposed Disbursement Quota = A + A.1 + B + B.1			
	"A"	"A.1"	"B"	"B.1"
Charitable Organizations and Public Foundations	<p>80% of all eligible amount of gifts for which the charity issued donation receipts in its immediately preceding taxation year, other than:</p> <p>(a) gifts of enduring property;</p> <p>(b) gifts received from other registered charities.</p> <p>"Enduring properties" include properties that are:</p> <p>(a) gifts of bequest or inheritance, including life insurance proceeds, RRSPs, and RRIFs by direct beneficiary designation</p> <p>(b) gifts received by a charitable organization from another registered charity, where the majority of directors and trustees of the donor charity deal at arm's length with the recipient charitable organization, provided that the gift is subject to a trust or direction requiring that the gift be utilized over a period not exceeding five years in the course of a program of charitable activities or for the purpose of acquiring capital property to be used directly in the charitable activities (Note that this paragraph does not apply to gifts received by public foundations)</p> <p>(c) ten-year gifts</p> <p>(d) gifts received by the charity as a transferee of enduring property that are gifts of bequest or inheritance and ten-year gifts from either an original recipient charity or another transferee charity, provided that if the gifts are ten-year gifts, the gifts are subject to the same terms and conditions under the trust or direction</p>	<p>The amount by which</p> <p>(a) the total of</p> <p>(i) 80% of the amount by which the total amount of enduring property owned by the charity to the extent that they are expended in the year, and</p> <p>(ii) the fair market value (at the time of the transfer) of enduring property (other than enduring property that was received by the charity as a specified gift) transferred by the charity in the taxation year by way of gift to qualified donees</p> <p>exceeds</p> <p>(b) the amount claimed by the charity that may not exceed the lesser of</p> <p>(i) 3.5% of the amount determined for "D" and</p> <p>(ii) the capital gains pool of the charity for the taxation year (defined in the note to the table)</p> <p>NOTE:</p> <p>"Enduring property" not included in subparagraph (a)(i) of "A.1" =</p> <p>(a) enduring properties described in subparagraph (a)(ii) of "A.1" ;</p> <p>(b) enduring properties received by the charity as "specified gifts"; and</p> <p>(c) bequests or inheritance received by the charity in a taxation year that included any time before 1994</p>	<p>80% of all amounts received from other registered charities in its immediately preceding taxation year, other than specified gifts and enduring property</p>	<p>$B.1 = C \times 0.035 [D - (E + F)] / 365$</p> <p>"C" = number of days in the taxation year</p> <p>"D" =</p> <p>(a) average value of the charity's assets in the 24 months immediately preceding the taxation year that were not used directly in charitable activities or administration of the charity, if that amount is greater than 25,000</p> <p>(b) in any other case, it is nil</p> <p>"E" = "A.1"(a)(ii) + 5/4 of ("A" + "A.1"(a)(i))</p> <p>"F" = 5/4 of "B" which is = 100% of all amounts received from registered charities in its immediately preceding taxation year</p>
Private Foundations	same as above	same as above	Same as above, except 100%, rather than 80%	Same as above, except that "F" = "B", not 5/4 of "B"
<p>NOTE: "Capital gains pool" of a registered charity for a taxation year = the total of all capital gains of the charity from the disposition of enduring properties after March 22, 2004 that are declared by the charity in its T3010 Information Return for the taxation year during which the disposition occurred, that exceeds the lesser of the following two amounts:</p> <ul style="list-style-type: none"> The amount determined according to paragraph (a) of variable "A.1", i.e. the total of 80% of enduring property expended by the charity under subparagraph (a)(i) and the full fair market value of enduring property transferred by the charity to a qualified donee under subparagraph (a)(ii). The amount claimed by the charity according to paragraph (b) of variable "A.1", i.e. the amount claimed by the charity that may not exceed the lesser of 3.5% of the charity's investment assets and its capital gains pool. <p>However, the capital gain from the disposition of a bequest or inheritance received by the charity before 1994 is not included.</p>				

Calculation of Disbursement Quota under Bill C-33



D. CONCLUSION

The above is a summary of the proposed new rules regarding disbursement quota for charities. Although many aspects of the proposed new rules reflect a bona fide attempt by the Department of Finance to address a number of problems facing charities involving the disbursement quota, the complexities introduced by the new disbursement quota rules are such as to make them difficult, if not impossible, for the average charity to understand, let alone comply with. Even with a more detailed Disbursement Quota Worksheet for the Registered Charity Information Return - T3010A to assist in the annual calculation of the disbursement quota, charities will still be left in a vulnerable position. This is because charities not only need to be able to compute the disbursement quota at their fiscal year end for purposes of completing their T3010A, they also need to have a good working knowledge of the computation of the disbursement quota that they are required to satisfy in order to enable them to make informed decisions when planning their receipt and disbursement of funds throughout the year so that their decisions will not negatively impact their ability to meet their disbursement quota requirements.

In addition, there are concerns about the application of the proposed 3.5% disbursement quota being extended from charitable foundations to charitable organizations and the removal of the exemption of transfers of capital to charitable organizations from other registered charities. This is a major change in tax policy by the Department of Finance that would blur the line between public foundations and charitable organizations to the point that the need for the separate category of public foundations may be eliminated all together, leaving only charitable organizations and private foundations. The new disbursement rules are very complex and may leave many registered charities, as well as their advisors, confused about how to implement the new provisions on both a day-to-day basis and in completing their T3010 Information Returns.