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4<sup>TH</sup> NATIONAL SYMPOSIUM ON CHARITY LAW**

**Toronto - May 11, 2006**

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**WHEN IS AN ADVANTAGE NOT AN  
ADVANTAGE? – ISSUES ARISING FROM  
THE PROPOSED SPLIT RECEIPTING  
REGIME**

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**1. BACKGROUND**

- **Complex rules**
- **Both donors and charities are equally concerned with ensuring that their donations are appropriately and accurately received**

**HISTORY OF THE JULY 2005 PROPOSED  
AMENDMENTS :**

- **December 20, 2002 - draft amendments**
- **December 24, 2002 - Income Tax Technical News No. 26**
- **February 28, 2003 - Federal budget**
- **December 5, 2003 - draft amendments**
- **February 27, 2004 - revised draft technical amendments**
- **July 18, 2005 Special Release – legislative proposals relating**

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- **Subsections 248(30) to (41) introduced to allow a donor to receive a donation tax receipt even in situations where the donor or someone else receives a limited advantage as a result of the gift, i.e. “split-receipting”**
- **Some of the proposed changes also stem from the Department’s intention to curtail abusive tax shelter schemes involving charitable donations**

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- **These changes generally apply to gifts made after December 20, 2002, with a few exceptions**
- **Proposed rules are required to be followed even though they have yet to be enacted as law**  
– *See Richert v. Stewards' Charitable Foundation case*

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## **2. IMPLICATIONS**

- **First, the split-receipting rules change the definition of what constitutes a “gift” for the purposes of the Act**
- **Second, fundamentally change the calculation of the charitable tax deduction and credit**

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**a) “Gift” for the purposes of the Act**

- **The traditional common law definition of a gift requires:**
  - **the donor must have an intention to give**
  - **there must be a transfer of property**
  - **the transfer must be made voluntarily without contractual obligation; and**
  - **no consideration or advantage can be received by the donor**

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- **July 2005 draft amendments to the Act create a new concept of “gift” for tax purposes which permits a donor to receive benefit, provided that the value of the property donated exceeds the benefit received by the donor**
- **Concept is commonly referred to as “split-receipting”**
- **The July 2005 draft amendments reflect an importation of the civil law concept of gift which permits a benefit back to the donor**

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- **Charitable donation receipts must now reflect the following formula:**

$$\begin{array}{rcl} \text{Eligible Amount} & = & \text{Fair Market} \\ \text{of Gift} & & \text{Value of the} \\ & & \text{Property} \\ & & \text{Donated} \end{array} \quad - \quad \begin{array}{l} \text{Advantage} \\ \text{Received} \end{array}$$

- **Must be voluntary transfer of property with a clearly ascertainable value**

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- **Donative intent required**
- **Must have a clear donative intent by the donor to benefit the charity**
- **Donative intent will generally be presumed if the fair market value of the advantage does not exceed 80% of the value of the gift**
- **The donor may apply to the Minister for a determination of whether the transfer was made with the intention to make a gift**

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**b) Calculation of charitable tax deduction/credits**

- **Fundamentally changed the calculation of the charitable tax deduction set out in section 110.1 of the Act and the charitable tax credit set out in section 118.1 of the Act**
- **Previously both charitable tax deduction and charitable tax credit simply reflected the fair market value of the property donated to the charity**
- **Now requires a new calculation – the value of the deduction or credit is the “eligible amount of the gift”**

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**3. DEFINITION OF “ADVANTAGE” FOR THE PURPOSES OF THE SPLIT-RECEIPTING RULES**

**a) Definition**

- **The “amount of the advantage” is defined, the term “advantage” is not**
- **Canadian jurisprudence has considered what constitutes an “advantage” in other contexts**
- **Broad meaning of “advantage” from case law, e.g. *R. v. Marsh***

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- **Broad meaning of “the amount of the advantage” in proposed subsection 248(32)**
  - the total value of all property, services, compensation, use or other benefits,
  - to which the donor, or a person not dealing at arms length with the donor,
  - has received or obtained or is entitled to receive (either immediately or in the future),
  - as partial consideration of or in gratitude of the gift or that is in any other way related to the gift

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- b) **Extended legislative meaning**
  - (i) **Advantage “in respect of” what?**
    - **“The amount of the advantage in respect of a gift or monetary contribution by a taxpayer is the total of...”**
    - **The phrase “in respect of” has very broad connotation**

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- ***Nowegijick v. The Queen* : “The words “in respect of” are ... words of the widest possible scope. They import such meanings as ‘in relation to,’ ‘with reference to’ or ‘in connection with.’ The phrase ‘in respect of’ is probably the widest of any expression intended to convey some connection between two related subject matters.”**
- **Intended to apply in respect of any transaction or series of transactions having either the purpose or the effect of reducing the economic impact to a donor of a gift or contribution – i.e. very wide application**

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- (ii) **What is the value of the advantage?**
- **“... the total of all amounts other than an amount referred to in paragraph (b), each of which is the value, at the time the gift or monetary contribution is made, of ...”**
  - **“amount of the advantage” must have a calculable value that is to be determined at the time that the gift is made**
  - **The term “value” is used in describing the “amount of advantage,” while the term “fair market value” is used in describing the property donated**

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- To ensure that the CRA had a wide degree of latitude in assessing what constitutes the “value” of an “amount of advantage”
- Advantage must be clearly identified and its value ascertainable, otherwise no tax receipt
- CRA’s administrative *de minimis* threshold to allow nominal value be excluded from the “amount of advantage”, i.e. advantage of lesser of 10% of the value of the gift or \$75
- Method of valuation an issue – more than one approach may be acceptable to determine the value of the “amount of advantage” for the purposes of the *Act*

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**(iii) By what mode is the advantage to be conferred?**

**a) “any property, service, compensation, use or other benefit ...”**

– **Property is defined in subsection 248(1) of the *Act* to include:**

**property of any kind whatever whether Real or personal or corporeal or incorporeal and, without restricting the generality of the foregoing, includes a right of any kind whatever, a share or a chose in action; unless a contrary intention is evident, money; a timber resource property; and the work in progress of a business that is a profession.**

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- **“Service” means “state of being a servant; work done for and benefit conferred on another; act of kindness; ... advantage; use.” (Webster’s Dictionary)**
- **“Compensation” means “recompense; payment for some loss, injury etc.” (Webster’s Dictionary)**
- **“Use” has a wide definitional ambit, and suggests the drafters intended to include situations whereby donors are permitted to use facilities or properties without payment**

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- **“Benefit” means “advantage; profit; fruit; privilege; gain; interest” (Black’s dictionary)**
- **The courts held that the word ‘benefit’ is to be liberally interpreted and is not confined to financial benefit**
- **The broad scope of these terms are intended to catch any type of advantage that could possibly accrue to a donor upon the making of a charitable gift**
- **Care must be taken each time a gift is made to determine whether it may run afoul of these provisions**

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**(b) “... has received, obtained or enjoyed, or is entitled, either immediately or in the future and either absolutely or contingently, to receive, obtain or enjoy ...”**

- **Received, obtained or enjoyed by the donor**
- **“Enjoyed” broadened the scope of application of this clause to include advantages merely “enjoyed” by the donor, to which he or she may not have had any legal right**
- **Includes both contingent and actual advantages**

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- **Catches situations which seem far-fetched and where it would be difficult if not impossible to determine the value of the “advantage”**
  - **Also problem of valuing the amount of a remote contingent advantage**
- (c) “... (i) that is in consideration for ... (ii) in gratitude for ... or (iii) in any other way related to the gift or monetary contribution”**
- **Incredibly wide in scope**

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- **“In consideration for”**
  - **concept of “consideration” negates the requirement that the gift must be voluntary**
  - **legally enforceable rights of the donor**
- **“In gratitude for”**
  - **include advantages received, obtained or enjoyed as a result of an expression of gratitude or appreciation of the donor's gift**
  - **not legally enforceable rights**

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- **“in any other way related to the gift”**
  - **Involves advantages that are neither provided in consideration of the gift nor provided gratuitously**
  - **Suggests that it is not necessary for a causal relationship to exist between the making of the gift and the receiving of the advantage if they are “in any other way” related to one another**
  - **Linkage between the gift and the advantage? – religious school cases**

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- **Naming rights**
  - **Naming rights are not advantages if there is no prospective economic benefit associated with the naming rights**
  - **CRA advance rulings**
  - **Corporate donors - if a corporation wishes to make a donation in exchange for the promotion of its business name, an economic benefit will result**

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- **Individual donors - if a private individual wishes to make a donation in exchange for the use of a family name, no economic benefit will result**
- **What if the family name of the donor is very close to the family business?**

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**(iv) What is the timing of the valuation of the advantage?**

- **“...value, at the time the gift or monetary contribution is made, of any property, service, compensation, use or other benefit ... either immediately or in the future and either absolutely or contingently, ...”**
- **Calculated at the time that the gift is made**
- **Problem with contingent advantage – valuation issue, possibly appraisal and actuarial reports**

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**(v) By who is the Advantage to be Provided?**

- **Subsection 248(32) is silent**
- **Not necessary that the advantage be received from the charity that received the gift**
- **Could include an advantage provided by a third party, even unbeknownst to the charity issuing the receipt**

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**(vi) To whom is the advantage to be provided?**

- **“... the taxpayer, or a person or partnership who does not deal at arm's length with the taxpayer ...”**
- **The advantage may accrue to the taxpayer, or a person or partnership that does not deal at arm's length with the taxpayer**

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- **Additional onus on taxpayers and charities to ensure that advantages enjoyed by all relevant persons are properly accounted for, even those advantages of which the charity, and even the donor, may be unaware**
- **Another difficulty with this provision is the use of the arm's length concept in the charity context**

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**(vii) Additional examples of the outcome of the foregoing definition**

- **A charity receives a gift of land from a donor who has received some type of benefit from a developer who owns property adjacent to the donated property in exchange for making the gift**
- **A donor who poses for pictures with his wife, a professional model, after agreeing to make a large donation to a charity. The agreement regarding the donation is publicized, various media outlets publish the pictures, and the wife of the donor receives increased modeling work as a result**

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**(viii) What is the amount of the advantage in situations involving limited recourse debt?**

- **The proposed amendments also curtail the use of limited recourse debt, which is a form of tax shelter in which the tax-payer incurs a debt for which recourse is limited and which can reasonably be considered to be related to a charitable gifting arrangement**
- **Care should be taken, therefore, to ensure that any plan that involves the borrowing of funds to make charitable gifts is outside of the limited recourse provisions of the *Act***

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#### **4. OBLIGATIONS AND CONSEQUENCES**

- **Negative consequences to both the donors and charities if they fail to conform to the requirements of the *Act***
- **Important to consider the obligations and the consequences that may result if such obligations are not met**
- **The proposed rule: Charities issuing a receipt with an eligible amount in excess of \$5,000 would be required to make “reasonable inquiry” of the donor**

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- **Finance announced on November 22, 2005 that it is intending to repeal the above statutory requirement, but such repeal will have little practical implication, since a charity still has an obligation for due diligence purposes to determine the correct amount for the eligible amount of a receipt**
- **What happens if the charity fails to ask questions?**
  - **If a charity fails to make inquiry, this may result in an incorrect receipt and could trigger the imposition of intermediate sanctions**

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- **Disgruntled donors could take legal action**
- **The charitable status of the charity that issued the receipt may also be revoked**
- **It remains unclear whether the intermediate sanction/penalty will be applied to a charity if it has made inquiries but the donor has not provided the required information**
- **What happens if the donor fails to give information to the charity?**
  - **If a donor fails to provide any required information, whether or not the charity has made inquiries, the eligible amount of the receipt will be deemed to be nil, i.e. no credit or deduction in respect of the gift**

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- **The extent of the due diligence that a charity should undertake in any situation must generally be judged on a case-by-case basis**
  - **Understand the split-receipting rules and what information is required**
  - **Develop and use questionnaires and due diligence checklists**
  - **Request written confirmation from the donors (signed? sworn?)**
  - **Develop gift acceptance policies**

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- **Ensure detailed documentation in gift agreements**
- **May need to issue a separate receipt for each gift where multiple gifts from a donor is involved**
- **Ensure staff of the charity is aware of the rules (accountants, gift planner, fundraisers, public relations, marketing and publications staff, etc.)**

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## **5. OTHER RELATED ISSUES**

### **a) Gifts between charities and disbursement quota**

- **Will a transferor charity be considered to have made a gift to another charity (and an expenditure for disbursement quota purposes) even if it received an advantage, such as some manner of consideration, from the recipient charity as a result of the transfer**
- **It appears that there are strong arguments supporting the proposition that the new amendments governing the terms “gift” and “amount of advantage” in the *Act* are also meant to apply to inter-charity gifts.**

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**b) Multiple donations by the same donor**

- **In situations involving multiple donations, it is a question of fact whether any advantage received relates to a single donation or to the series**
- **Sometimes, it might be necessary for separate receipts be issued for multiple donations made by the same donor**
- **If the advantage relates to a series of donations, then a single receipt would need to be issued for the series of donations**
- **If the advantage relates to a single donation, then it might be necessary or beneficial to issue multiple receipts**

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**c) Different effective dates**

- **It is also necessary to note that the various components of the new split-receipting rules involving “advantage” of gifts have different effective dates**
- **See list in paper**

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## **6. CONCLUSION**

- **Raises many troubling questions and issues for charities attempting to comply with its rules**
- **The definition of what constitutes the amount of an advantage for the purposes of the *Act* and its calculation is less than clear**
- **The potential breadth of the terms used may lead to unexplained and potentially dangerous results for both charities and donors**

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- **Imposes increased due diligence obligations on charities to ensure that they are correctly receipting in circumstances where it may be impossible for them to access the information they need in order to ensure that all advantages are properly included in the calculation of the eligible amount of the gift**

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