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THERE ARE MANY GIFTS-IN-KIND IN THE SEA

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Purple pantyhose and load of manure force nonprofits to get creative

From the AMERICAN - STATESMAN STAFF
Sunday, July 08, 2007

•A Pallet of Queen Sized Purple Pantyhose •100 right-foot boots •1967 Kaiser Jeep retrofitted as a hunting vehicle •Two prosthetic legs •A truckload of horse manure •12 boxes of Vivarin (caffeine pills) to a children's shelter	•A bag of Depends adult diapers signed by Depends spokeswoman/actress June Allyson. •Wedding dress & a giant realistic gorilla mannequin •Thong underwear, edible massage oils and liqueur-filled chocolates

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Aug. 6, 2007 – AFP eWire

•Antique Horse Drawn Hearse •Prize Winning Steer •Seal Meat •Chocolate Covered Ants •Cemetery Plots •Human Skeleton •Fake Sapphires •Several large cartons of defective pantyhose •Therapy Session	•388 bottles of sake •Live Hand Grenade •A Live Chicken •500 Hand Tied Fishing Lures •A Human Leg •Five Sheep per Year for Five Years •50 Condom Vending Machines •Burial Vaults •A one quarter interest in a bull

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A. INTRODUCTION

1. Gifts of Real Estate
2. Gifts of Personal Property
3. Ecological Gifts
4. Gifts of Cultural Property
5. Private Company Shares
6. Limited Partnership Interests

GIFTS-IN-KIND EXAMPLES – WHAT WOULD YOU DO?

- Has this or something similar occurred with your organization?
- What issues arise in these situations?
- Where would you go for answers?
- Do you have a policy that deals with these situations?

Gift-in-kind

- A donor gifts a wild animal head collection and $100K to start a museum to house the collection
- The wild animals were shot and killed by the donor over many years during hunts and safaris
- Each year the donor would add another trophy piece to the collection. Soon animal heads were everywhere
- No one can say "no more heads" to the donor because of an expected bequest but the donor will not discuss his estate plans
- Questions: does the gift fit the organizations mandate, how to evaluate gift, who should address space & bequest issues

Gift-in-kind

- A donor wants to gift 100 acres of British Columbia land to a Newfoundland charity
- The donor agrees to provide one current appraisal
- It turns out the land is in the domain of an endangered species, the Whistler Toad
- To accept the gift a $10K biological survey is required to determine if any such toads are on the property. The donor will not pay for the survey
- Questions: value of land, # of appraisals, property disposition

Gift-in-kind

- The year is 2013 and a charity recruits a board member who regrettably was convicted of stealing money from a family member four years ago. The gentleman paid back the funds including lost interest
- This board member approaches you and wishes to gift 12 bottles of 200 year old scotch to your charity with no strings attached
- Questions: board member background checks, gift valuation and disposition

GIFTS-IN-KIND

- Gift of property other than cash, e.g.
  - Capital property
  - Leasehold interest
  - Residual interest
  - A right of any kind
  - Inventory of a business
  - Certified cultural property
- Examples include, books, art work or art collections, archival documentation, works or material, equipment, software, or other property
- Does not include a gift of services
- Generally, a receipt will be issued for the FMV of the property - note CRA requires an appraisal if the value exceeds $1000

- Issues
  - Valuation and appraisal
  - CRA policies on many of these types of gifts
  - Good and marketable title - e.g. Does the donor own the property being donated?
  - Due diligence searches
  - Does the charity intend to sell the capital property or to retain the property?

- If the gift is to be sold, what is marketability of the gift? - Can the gift be easily sold to realize cash for the charity?
- Are there any types of capital property that the charity does not wish to accept? e.g.
  - Property that cannot easily be sold and the charity has no use of the property- e.g. gift of large art work that the charity has no space to display
  - Property not consistent with the mission of the charity

B. GIFTS OF REAL ESTATE

- Gifts of real estate include single family homes, condominiums, apartment buildings, commercial buildings, land, and farms
- Gifts of real estate may be outright gifts, residual interest in a property (i.e. where the donor retains the use of the property), or real property to fund a charitable remainder trust

- If a charity in Ontario, must comply with *Charities Accounting Act* (Ontario)
  – The *Charities Accounting Act* prohibits a charity from owning lands for non-charitable purposes
    - "A person who holds an interest in real or personal property for a charitable purpose shall use the property for the charitable purpose" (s.8)
  – This means you may be required to divest

- Gift of real estate will generally be considered a gift of capital property, which is usually defined as any property of value that is acquired for investment purposes or to earn income
- Gift of real estate will result in a deemed disposition of the property at FMV which may result in a capital gain. Generally, 50% of the capital gain resulting from a gift of capital property will be taxable, except if a gift of publicly-listed securities or an ecological gift

- If the donor has to include a capital gain in income as a result of a gift of capital property to a charity, the donor can increase the standard donation limit by 25% of that taxable capital gain

Example: Donating land to charity

- Several years ago, George purchased vacant land for $10,000. The land is not ecologically sensitive land. The vacant land increased in value and is currently worth $90,000. George donated this land to his favourite charity.

Property donated: vacant land						
Fair market value	Proceeds of disposition	Adjusted cost base	Expenses	Capital gain	Capital loss	Taxable capital gain
$90,000	$90,000	$10,000	$0	$80,000	$0	$40,000

- George will have to include the $40,000 taxable capital gain in income.
- The tax arising from the taxable capital gain will be more than offset by the tax credit arising from the $90,000 gift.

Consider the following:

- Valuation and appraisal
- Good and marketable title - e.g. Does the donor own the property being donated?
- Due diligence and title searches
- Title Insurance
- Discharge of mortgage on the property

- Concerns related to land ownership, e.g. environmental contaminants, oil tank leakage, conservation restrictions, use restrictions, property tax, up-to-date survey, zoning, safety, etc.
- Does the charity intend to sell the property or to retain the property?
- If the charity is to retain the property, is it to be used for charitable purpose or rented as an investment property? If for investment, possible disbursement quota issues

C. GIFTS OF PERSONAL-USE PROPERTY

- Personal-use property (PUP) are
  - items that you own primarily for the personal use or enjoyment of yourself and your family
- Includes personal and household items, such as furniture, automobiles, boats, cottages, and other similar properties
- If a donor disposes of PUP with an adjusted cost base or proceeds of disposition of more than $1000, the donor may have capital gain that will have to be reported, but no capital loss can be claimed
- If less than $1000, then no capital gain

GIFTS OF LISTED PERSONAL PROPERTY

- Personal-use property includes a special class of property called *Listed Personal Property* (LPP)
- LPP usually increases in value over time
- Includes:
  - Prints, etchings, drawings, paintings, sculptures, or other similar works of art
  - Jewellery
  - Rare folios, rare manuscripts, rare books
  - Stamps
  - Coins

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- Have the item appraised to determine its value
- Capital gain or loss from disposition of LPP item is calculated same way as for PUP
- Donor may deduct losses from any gains from disposing of other LPP

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Example: Donating personal-use properties

- Jane gave a China cabinet and boat to a local charity. The China cabinet is currently worth $900. She purchased it for $500 several years ago. The boat is currently valued at $1,200. She purchased the boat for $850 a couple years ago.

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Jane's personal-use properties in 2014					
Property donated	Proceeds of disposition	Fair market value	Adjusted cost base	Outlays and expenses	Capital gain (or loss)
Cabinet	$900	$900	$500	$0	$0
Boat	$1200	$1200	$850	$50	$0

Calculation of capital gain or loss:		
Property donated	China cabinet	Boat
Proceeds of disposition (*greater of* selling price & $1000)	$1000	$1200
Minus: Adjusted cost base (*greater of* cost & $1000) *plus* outlays and expenses	$1000	$1050 ($1000 + $50 expenses)
Capital gain (or loss)	$0	$150
Calculation	1000-1000 = 0	1200-1050 = 150

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- Personal property: the receipt may be impacted by the new deemed disposition rules:
  - Deemed FMV
    - Legislation first introduced Feb 27, 2004 - To stop "buy low-donate high" and other tax shelter gifting arrangements
    - Potential punitive tax consequences for private company shares gifts (e.g., estate freezes and other corporate reorganizations?)

- Rule:
  - Property acquired through a "gifting arrangement", in contemplation of gift or donated within 3 years of acquisition
  - Deemed fair market value- lesser of FMV and donor's cost
  - Exceptions include publicly traded shares, certified cultural property, real property in Canada, inventory and ecological gifts, and gifts on death.
  - Exception for shares subject to estate freeze arrangements

Consider the following issues:

a) Whether the gift is in reasonable condition and meets other criteria such as,
  - whether the gifted property will be displayed, stored, or used for fundraising purposes
  - whether to retain the property or sell it and apply the proceeds towards the charitable purpose of the gift
  - whether gifts of pharmaceuticals, food or other basic amenities may be used for charitable programs

b) Ready marketability of the property and the carrying costs
   - may want to consider securing own appraisal and issue a gift receipt based on it

c) Undertaking the necessary due diligence steps

d) Who will hold responsibility for costs, such as legal fees and appraisals

e) Date of the donation and fair market value of the property as the charitable donation receipts will be issued for the eligible amount of the gift on that date based on that value

D. DONATIONS OF ECOLOGICALLY SENSITIVE LAND

- The *Income Tax Act* ("ITA") provides enhanced tax incentives for donations of ecologically sensitive land
- What is ecologically sensitive land?
  - Areas or sites that presently, or in the future, could significantly contribute to the conservation of Canada's biodiversity and natural environmental heritage
- Government of Canada certifies the value of ecological gift donations for income tax purposes
- Donations must be made to eligible conservation charities, including land trusts, through Environment Canada's Ecological Gifts Program

- Prior to Budget 2014, the tax credit or deduction was limited to a 5-year carry-forward, which often results in some unused tax benefit, e.g.:
  - Lands under development pressure with significant appreciation have often been held by the same owner for decades (often farmers)
  - These owners often do not have the income to offset the tax receipt over the 5 year period
- Budget 2014 amended the definition of "total ecological gifts" in the ITA to extend this charitable deduction or credit to a 10-year carry-forward
- This amendment will apply to donations made on or after February 11, 2014

Example: Donation of a Remainder Interest

- Sue earns $75,000 as an accountant in Halifax
- She has owned 6 ha of property in Lunenburg County in an area with a planning restriction that prohibits development on lots smaller than 2 ha. The land includes a picturesque and significant stretch of coastline and has been in Sue's family for over a century
- In recent years, large areas of Nova Scotia's southern coast have been bought up by wealthy foreign visitors for homes and cottages. Sue is concerned that there may soon be little undeveloped coastal habitat left

- Sue opts to keep a life interest in the land so she may live out her days there and to donate the remainder interest to a land trust as an ecogift
- The land, originally valued at $80,000, is now worth $400,000. The remainder interest is worth $250,000. The land trust also enters into an agreement with Sue to use and care for the property

- Certified FMV of gift is $250,000 - it is generally the current appraised FMV of the gift less the value of the life interest (IT 226R)
- Taxable income is $75,000
- The entire amount of the donation may be used - not limited to 75% of her taxable income like other gifts
- Immediate donation tax credit in year of gift even though able to continue to use the property
- Remainder of the donation may be carried forward for 10 years
- No tax on the capital gain arising as a result of the disposition of the remainder interest

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E. GIFTS OF CULTURAL PROPERTY

- Property (art, sculptures, archival material, etc.) must be certified by the Canadian Cultural Property Export Review Board as being of outstanding significance and national importance
- Recipient must be a "designated institution"
- Board determines FMV
- No capital gain and may be claimed against up to 100% of taxable income

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- Currently a tax exemption applies to capital gains realized on the disposition of certified cultural property to institutions and public authorities designated by the Minister of Canadian Heritage
- When disposition is by way of a gift to those institutions of certified cultural property, the donor may claim a tax credit up to 100% of their net income
- Budget 2014 will remove, for certified cultural property acquired through a tax shelter arrangement, the exemption from the rule that deems that value of a gift to be no greater than its costs to the donor
- This provision will apply to donations made on or after February 11, 2014

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F. PRIVATE COMPANY SHARES

- Private company shares can be effective gifting tool
- However implementation and ongoing management of such gifts more complex/costly

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- Donation tax credit
  - Tax incentive for gifts of publicly traded securities not available
- Generally no charity receipt if no-qualifying securities
  - Exception - shares gifted to charitable organizations/public foundations and donor at arm's length
  - Trap - if shares → debt after gift

- RDTOH
  - Redemption of shares by charity shareholder may → refund of RDTOH

    So Donor → tax credit

    Company → RDTOH

    Charity → value of shares

- Donation receipt
  - Fair market value of shares - what is value if can't redeem for some time
- Disbursement quota issues
  - Enduring property?
  - If hold shares for some time → dividends to cover 3.5% DQ and administrative costs
- Control of corporation

G. LIMITED PARTNERSHIP INTERESTS

- Increasing requests to receive gifts of limited partnership interests
- Limited partnerships are very different from general partnerships and are usually set up by companies that invest money in other businesses or real estate

- Donation tax deduction or credit for the FMV of the interest
- 50% of any capital gain would be included in income and subject to tax, unless a publicly listed security
- CRA Position: The charity would be considered to be carrying on a business if it becomes a limited partner in a partnership and subject to possible revocation
- The fact that the principal activity of the partnership is the investment of funds did not change their view

- But, consider whether position would be the same if donation consists of limited partnership units which are publicly listed, widely held, and sold immediately upon receipt

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H. APPRAISALS

- When to obtain appraisals?
- Who pays for the appraisals?
- Which appraiser to retain? - must be qualified individuals
- How many appraisals to obtain?
- What if 2 appraisals obtained and the values are different?
- CRA's $1000 FMV appraisals threshold - valuation can be made by a staff member of the charity, provided that the staff member is knowledgeable in the field and is qualified to establish the value of the gift

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I. LESSONS

- Have property appraised if value is more than $1000
- Know your donor
- Seek legal advice for questionable gifts
- Before accepting a gift, assess its quality and value
- If receiving land, question whether the land is ecologically sensitive land
- If property is cultural property, must be certified for tax exemptions to apply
- Private company shares can be donated but consider the complexity and cost
- Be aware that donations may cause capital gains and losses which the donor may have to report

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