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Split-receipting:
Ask Questions Before Issuing the Receipt

(Powerpoint Presentation)

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KEY POINTS TO REMEMBER

- **A gift will now permit some consideration to be received by the donor**
- **New split-receipting rules will apply**
- **New broader definition of "advantage" may reduce the eligible amount of a charitable receipt**
- **Complicated new rules to curtail tax shelter schemes may result in reduction of charitable receipts for gifts in kind**
- **Charities will need to make "reasonable inquiries" of donors for all gifts over $5,000, whether gifts in kind or cash**
- **Different proposed changes have different effective dates, some are retroactive**

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OVERVIEW OF RECENT CHANGES TO THE *INCOME TAX ACT*

Proposed Technical 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 - draft amendments**
- **July 18, 2005 – draft amendments**

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SPLIT-RECEIPTING RULES

- **The traditional common law definition of a gift requires that the donor must not receive any consideration or advantage for having made a gift**
- **New proposed changes to the *Income Tax Act* now permits a donor to receive a limited benefit**

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

Eligible Amount of gift	=	Fair market value of the property donated	-	Advantage received by donor

(1) Must be voluntary transfer of property with a clearly ascertainable value

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(2) 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**

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(3) Advantage

- **Broad definition - includes:**
  - **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 for or in gratitude for the gift or that is in any other way related to the gift**

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- **Must be clearly identified and its value ascertainable**
- **Value of advantage - the total value of any "property, service, compensation, use or other benefit" in question**
- **Timing of valuation - the time when the gift is made**

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- **Mode of the advantage - includes something that (1) is received, obtained, or enjoyed by someone or (2) someone is "entitled, either immediately or in the future and either absolutely or contingently" to receive, obtain or enjoy. The advantage could be (i) in consideration of, (ii) in gratitude of, or (iii) in any other way related to the gift**
  - **The advantage can be received prior to, at the same time as, or subsequent to the making of the gift**
  - **Not require causal relationship between the making of the gift and the receiving of the advantage, as long as the advantage is related to the gift**

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- **To whom the advantage is provided - the donor or to a person or partnership not dealing at arm's length with the donor**
- **By whom the advantage is provided – it is not necessary that the advantage be received from the charity that received the gift, i.e. the advantage could even be provided by third parties unbeknownst to the charity, which fact will necessitate that charities make inquiries of donors to determine if they have received a related benefit from anyone**
- **CRA's administrative exemption – allows a token advantage of the lesser of 10% of the value of the gift and $75 (*de minimis* threshold)**

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(4) Curtailing donation tax shelter schemes

- **Some of the proposed changes are the result of the government's attempt to curtail abusive tax shelter donation schemes by severely restricting the tax benefits from donations made under these schemes**
- **These donation programs usually involve the item in question being purchased at a substantially lower price than its purported much higher fair market value, and that a donation receipt is issued by a registered charity for the fair market value when the item is donated**

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- **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**

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(5) "Deemed fair market value"

- **Valuation of fair market value (fmv) of donated property**
- **FMV of donated property may be deemed to be the lesser of**
  - **(i) the fair market value of the property and**
  - **(ii) the cost (or the adjusted cost base where applicable) of the property to the tax-payer immediately before the gift is made**

  in the following three situations:

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- If the donor acquired the property through a "gifting arrangement"
- If the donor acquired the property less than 3 years before making the gift
- If the donor acquired the property less than 10 years before making the gift, if it was reasonable to conclude that when the donor acquired the property one of the main reasons for the acquisition was to make a gift (donor must prove that the donor did not have an expectation to make a gift when the property was acquired)

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- New provision also requires a "look-back" to see if the property had been acquired within the 3 or 10 years by a non arm's length person, and if so, the cost of the property to the donor will be deemed to be the lower of the donor's cost and the lowest cost to any such non arm's length person
- The deeming provision does not apply to inventory, real property or an immovable situated in Canada, certified cultural property, publicly traded shares and ecological gifts

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- The deeming provision also does not apply
  - (a) where the gift is made as a consequence of the donor's death
  - (b) a shareholder has transferred property to a controlled corporation in exchange for shares and the shares are donated, or a rollover transaction to a corporation for the same purpose of donating shares

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- **New rules to prevent a donor from avoiding the deeming provision by disposing of property to a charity and then donating the proceeds of disposition, rather than the donor donating the property directly to the charity ("substantive gifts")**

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(6) Reasonable Inquiry

- **The Rule: Charities issuing a receipt with an eligible amount in excess of $5,000 will be required to make "reasonable inquiry" of the donor**

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(a) What is involved?

- **The charity must make reasonable inquiry**
- **The donor must provide the requested information to the charity**
- **The information on the receipt must be accurate and reflects the fmv (or deemed fmv where applicable) of the donated property, the advantage and the eligible amount of the gift**

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(b) When to ask?

- **If the receipt reflects an eligible amount that is in excess of $5,000, the legislation imposes a positive obligation on the charity to ask questions**
- **If the receipt is less than $5,000, although the legislation does not impose a positive obligation on the charity to make reasonable inquiry, the charity still has to make sure that the amounts shown on the receipt is accurate and the charity would still need to make inquiry regarding the gift for due diligence purposes**

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- **The reasonable inquiry must be made *before* issuing the receipt, not afterwards**
- **Reasonable inquiry must be made regardless of the type of donated property, including cash and gifts in kind**
- **The obligation to make reasonable inquiries applies to gifts made after 2005**

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(c) What to ask?

- **What is "reasonable"?**
- **Due diligence required**
- **Must inquire as to the existence of any circumstances in respect of which the new split-receipting or tax shelter rules might apply to cause the eligible amount to be less than the fair market value of the property donated**

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- Very broad, includes
  - When was the property acquired?
  - What was the cost of acquisition?
  - Was there any advantage related to the gift?
  - What was the value of the advantage?
  - Does the donor have any obligation in relation to any limited recourse debt in making the gift?
  - Was the donated property acquired through a donation tax shelter gifting arrangement?

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- Was the property acquired in the last 3 years, if so, what is the donor's cost amount?
- Was the property acquired in the last 10 years, and if so, did the donor have an expectation to make a gift at the time when the donor acquired the property. If so, what was the donor's cost amount?
- Did any non arm's length person acquired the property in the past 3 or 10 years prior to making the gift, and if so, what were their cost amounts?

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(d) How to comply with the obligation to make reasonable inquiry?

- What is "reasonable"?
- Understand the split-receipting rules and what information is required, e.g.
  - A charity has to understand what is a "donation tax shelter gifting arrangement" in order to ask the donor whether the donated property was acquired through such an arrangement

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- A charity has to understand what "arm's length" means in order to ask the donor whether any non arm's length person acquired the property in the past 3 or 10 years prior to making the gift
- A charity has to understand what would constitute an "advantage" in order to ask the donor whether there was any advantage related to the gift

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- Develop and use questionnaires and due diligence checklists
- Request written confirmation from the donors (signed? sworn?)
- Develop gift acceptance policies
- Ensure detailed documentation in gift agreements
- Issue donation receipts for each gift received, where possible, rather than issuing one receipt at the end of the year for all gifts received

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- Ensure staff of the charity is aware of the split-receipting rules, e.g.
  - Accounting staff because they receive gifts and issue receipts
  - Fundraising and gift planning staff because they contact donors to solicit donations
  - Public relation, marketing and publication staff who prepare fundraising and other promotional materials that makes representation to donors

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(e) What if donors fail to give information to the charity?

- **If a donor fails to provide any of this information, whether or not the charity has made reasonable 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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(f) What if the charity fails to ask questions?

- **If a charity fails to make reasonable inquiry, this will likely result in an incorrect receipt and could trigger the imposition of intermediate sanctions**
- **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 reasonable inquiries but the donor has not provided the required information**

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