

UTILIZING TEN YEAR GIFTS IN CHARITABLE FUND RAISING

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A. INTRODUCTION

Ten year gifts to charities are becoming an important tool in charitable fund raising, both for charities and donors. They assist charities by being exempt from the 80% disbursement requirement that applies to donations received in the previous year. They assist donors by facilitating the giving of gifts that are to be held for a longer term, whether it be for a minimum of ten years or for longer, such as a perpetual endowment fund. However, there are many legal issues involving ten year gifts that are not well understood by charities for which the advice of lawyers should be sought. The following is a brief overview of some of those issues.

B. DOCUMENTING TEN YEAR GIFTS

Subsection 149.1(1) of the *Income Tax Act (ITA)* sets out what constitutes a ten year gift. The relevant provisions are as follows:

...a gift subject to a trust or direction to the effect that property given, or property substitutes therefore, is to be held by the foundation [charitable organizations] for a period of not less than ten years...

The fact that a ten year gift can include a directed gift as well as a charitable trust means that gifts to a charity that may not meet the requirements to create a charitable purpose trust may still constitute a ten year gift where the requirements to document a ten year gift under the *ITA* have been met.

Each ten year gift must be evidenced by a document signed by the donor. The documentation must:

- ◆ clearly identify the donee charity, including its official name and registration number;
- ◆ indicate the amount of the gift;
- ◆ set out the date the gift is made;
- ◆ set out the name and address of the donor; and
- ◆ set out the serial number of the official receipt issued to the donor for the gift.

The documentation should then be attached to the charity's duplicate copy of the receipt and retained with its other books and records.

The requirement that a ten year gift must be a trust or a direction that is executed by the donor may be problematic when dealing with a public fund raising event, such as a dinner or auction, where the proceeds are to be added to an endowment or other type of ten year gift. It is not realistic to expect that each person attending the event would be prepared to sign a direction or declaration of trust. A solution might be for the event's promotional materials to set out the requirements to establish a ten year gift and to include a reply card to buy tickets stating that the completion and signing of the card is deemed to be the execution of a ten year gift document, or alternatively to include all of the relevant information about the ten year gift on the back of the tickets provided that the purchasers sign their tickets and the charity retains a duplicate copy

C. EXPENDITURE OF INCOME BY FOUNDATIONS

Ten year gifts remain subject to the 4.5% annual disbursement quota imposed on foundations. Unless a foundation has other income to meet the 4.5% disbursement quota on ten year gifts that it holds, it is essential that the ten year document permit the income earned on the gifts to be expended each year, and also that the annual income earned on the gift be at least 4.5% of its original value plus any resulting capital gains.

Sub-section 149.1(1) requires a ten year gift to remain intact for ten years. This means that a partial disbursement of capital to meet the quota is not permitted. Therefore, before accepting a ten year gift, a foundation must be satisfied that the gift will earn sufficient income to meet the 4.5% disbursement quota. If not, the board cannot disburse a portion of the capital to meet the quota. Instead, it should not accept the ten year gift.

A related question is whether the document creating a ten year gift can authorize the expenditure of capital gains earned on the gift by defining "income" to include resulting capital gains. In this regard, CCRA has recently stated that capital gains earned from a gift are considered to be a portion of the "*property given, or property substituted therefore*" under ss.149.1(1) of the *ITA* and that no capital gain earned on a ten year gift can be disbursed for at least ten years.

As a result, it is important for charities that may have ten year gift documentation permitting the disbursement of capital gains not to exercise that option; otherwise, the charity would be in violation of the definition of a ten year gift under ss.149.1(1) of the *ITA*.

D. CONSEQUENCES OF EXPENDING CAPITAL PRIOR TO EXPIRY OF TEN YEARS

If the capital of a ten year gift, i.e. "*property given or property substituted therefore*" under ss.149.1(1) of the *ITA*, including capital gains ("Capital"), is expended within ten years of the gift being made, certain consequences would result:

- ♦ The expenditure would be a breach of trust or a violation of the donor direction creating the ten year gift.
- ♦ The portion of the Capital expended would be added to the disbursement quota of the charity for the year in which the Capital was expended in accordance with the definition of the disbursement quota under ss.149.1(1) of the *ITA*. This, in effect, would mean that the amount of the Capital expended would be added to and disbursed as part of the disbursement quota in the same year, resulting in a neutral effect upon the disbursement quota of the charity for that year.

- ◆ The more difficult question is whether the full amount of the ten year gift collapses where only a portion of the Capital is expended in any one year. This would not appear to be the case from the wording of ss.149.1(1), in that the amount added to the disbursement quota is based upon the actual amount that is expended in a particular year. As such, if only ten percent of a ten year gift were disbursed in a year, it would appear that only the ten percent actually expended would be added to the disbursement quota.
- ◆ Based upon the above, some charities have considered gradually disbursing a ten year gift over a number of years, assuming that there would be no negative impact upon meeting its disbursement quota each year. However, CCRA may see a gradual disbursement as an intentional misuse of the ten year gift, which might result in either deregistration of the charity or, alternatively, disallowance of the ten year gift in the original year in which it was claimed for the full amount of the gift that had been exempted.

E. EXPENDITURE OF TEN YEAR GIFTS AFTER EXPIRY OF TEN YEARS

The ten year gift exemption only requires that a gift be held for "*not less than ten years.*" Therefore, a trust or direction could create a ten year gift that is to be held for longer than ten years, or even in perpetuity as an endowment. In this regard, the donor could direct how the gift is to be expended after ten years. Silence on this issue by the donor would give the charity liberty to use the gift as the charity determined at the end of ten years, regardless of the donor's intentions.

Conversely, a gift listed as a ten year gift on a charity's annual return does not necessarily mean that the gift can be expended after ten years. The charity and its board of directors would need to carefully review the wording creating the gift to determine if any restrictions continue after ten years, such as the gift being held in perpetuity as an endowment.

F. MANAGING TEN YEAR GIFTS

Charities often co-mingle restricted funds in a single account for investment purposes. Although this practice may be authorized by pending regulations under the *Charities Accounting Act* of Ontario, it is prudent for charities to maintain each ten year gift in a separate account. Although administratively awkward, this practise would help to ensure the following:

- ◆ Since the Capital of a ten year gift, including any resulting capital gains, cannot be expended for at least ten years, a charity must be able to identify the original gift and the capital gains earned thereon.
- ◆ There would be less chance that the capital of the gift would be expended during the ten years in an attempt to meet the 4.5% disbursement quota.
- ◆ Since each donor may impose different terms on a ten year gift, i.e. length of time the gift must be held, or the investment powers that are to apply, maintaining separate accounts for each ten year gift would help the charity to keep track of and comply with the specific terms of each gift.