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**Carters/Fasken Healthcare
Philanthropy Webinar
February 13, 2024**

**Donors Advised Funds for
Healthcare Charities**

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INTRODUCTION & OVERVIEW

- There continues to be considerable interest in donor-advised funds (“DAFs”) throughout the charitable sector - given this, healthcare charities may want to review if DAFs could be a giving vehicle to add to their “arsenal”
- If so, then it is important for DAFs to be properly set up and managed from the outset, with clear understanding of what they are at law and their current issues
- More information is set out in the paper, “Primer on Donor Advised Funds and Current Issues – Revisited”, May 15, 2023
<https://www.carters.ca/pub/seminar/charity/2023/Paper-Primer-on-Donor-Advised-Funds-and-Current-Issues-Revisited-2023-05-12.pdf>
- This presentation will review:
 - What are DAFs and Why are They so Popular?
 - What a DAF is at Law, including Recent Case Law?
 - Survey of Current Legal Issues Related to DAFs
 - Practical Considerations when Working with DAFs

A. CONTEXT OF DAFS – WHAT IS A DAF?

- A DAF is a type of charitable giving vehicle, established when a fund is created by a donor through an initial donation to a registered charity (“DAF Holding Charity”), and the fund’s capital and/or income is then used to make gifts to registered charities, including healthcare charities
- The gifts by the donor (usually a single person or family) to the DAF are irrevocable, and charitable donation receipts are issued for the gifts by the DAF Holding Charity
- The DAF Holding Charity itself then gifts amounts from a DAF (from capital if the DAF is not perpetually endowed, as well as from income) to either:
 - Qualified donees (e.g. registered charities), or
 - Grantee organizations (subject to the new qualifying disbursement rules)
- For a healthcare-related DAF Holding Charity, the gifts from the DAFs could be directed either to different healthcare charities or possibly to different program areas within a dedicated healthcare charity beneficiary

- In a DAF, the donor is given the unique role of making non-binding suggestions to the DAF Holding Charity regarding the distribution of assets from the DAF to qualified donees or grantee organizations
- However, despite this donor advice, all administrative, operational and governance matters (including compliance with *Income Tax Act* [“ITA”] and CRA policies) are the **sole responsibility** of the DAF Holding Charity
 - This is because DAFs are the property of the DAF Holding Charity alone, **not** the donor
- Failure by a DAF Holding Charity to properly hold and maintain DAFs in compliance with tax/trust law could erode donor confidence and result in potential liability and credibility damage for the Charity

B. WHY ARE DAFs SO POPULAR NOW?

- DAFs are a practical and appealing alternative for donors who do not have the ability, interest or time to operate their own private foundations
- Relatively inexpensive to establish a DAF with a DAF Holding Charity versus operating a private foundation
- More anonymity and flexibility in structuring for donors

Some DAF Holding Charities do not impose minimum initial donations, or they can be as low as \$5,000, with ongoing fees also being moderate

Private foundations (unless established to facilitate flow through donations to qualified donees) are generally established with at least a \$1-\$2 million capital asset base, with ongoing annual operational costs

C. WHAT IS A DAF AT LAW?

1. It Is a Charitable Gift

- A voluntary transfer of property owned by a donor to a donee, for which the donor receives no consideration

2. It Could Also Be a Donor Restricted Charitable Gift

- Unrestricted charitable gifts must be applied to a charity's charitable purposes, but there are no other donor restrictions
- Restricted charitable gifts are subject to restrictions imposed by the donor from the outset, which constrains or limits a charity's use of the gift in the future, such as use in health care capital projects, for the purchase of equipment or carrying out a particular health care program/area of care

3. It Can Be a Gift for Income Tax Purposes

- CRA accepts the common law definition
- A gift meeting all ITA requirements can be receipted

D. HOW DOES THIS ALL RELATE TO A DAF?

- Original gift from the donor establishing a DAF in a DAF Holding Charity could be unrestricted or be subject to one or more donor restrictions, e.g. how long capital to be held, how income is to be used, how investment is to be done, etc.
- DAFs will then have a donor-advised “feature” added to the gift, providing the original donor (and possible successor “fund advisors”) with the ability to offer ongoing advice to the DAF Holding Charity
 - This advice can be on various aspects of the DAF, but usually relates to the gifts to be made
 - Often the donor advice is provided annually but it could be more frequently depending on the specific fund agreement’s terms
 - However, this donor advised feature does not impose a legal obligation on the DAF Holding Charity to act as the donor directs, although there is a moral obligation for the Charity to consider these donor suggestions

- A DAF Holding Charity must clearly inform its donors from the outset that their advice/input/suggestions are advisory only and that all decisions related to the DAF are ultimately to be made by the Charity
 - This is imperative to do in order that all donations by donors to DAFs are true gifts at law and can be properly receipted under ITA
 - This reflects that the DAFs are the Charity’s own charitable property over which it must exercise ongoing direction and control
 - If there is excessive ongoing control by the donor over the gifted property to a DAF, then it may lead to the CRA considering the gift to be a “directed gift”, which could then be defeated or negated
 - This could lead to issues with any charitable donation receipt issued for a defeated gift – for the charity and the donor - and should be avoided as much as possible

The Joseph Lebovic Charitable Foundation v Jewish Foundation,
2022 ONSC 4012 (“Lebovic Case”)

- This decision of the Ontario Superior Court confirmed that while a donor is free to make recommendations to a DAF Holding Charity on how monies in their DAF are to be granted, the DAF Holding Charity is under no obligation to follow those recommendations
- In this case, after the death of the original DAF donor, the donor’s brother assumed responsibility as the DAF’s fund advisor with the Jewish Foundation of Greater Toronto (“JFGT”)
- Brother brought motion to prevent JFGT from spending a small portion of funds from the DAF contrary to his requests
- Court found the brother lacked grounds for his motion – stating that unless restrictions are imposed by a donor at the time a gift is made, the donor (or any future fund advisor) is not able to later direct how any charitable gifts are spent by the DAF Holding Charity

E. CURRENT ISSUES ASSOCIATED WITH DAFs

1. Disbursement-Related Issues – “Languishing” Assets in DAFs

- The 2019 Report of the Special Senate Committee on the Charitable Sector recommended that consideration be given to:
 - “means of ensuring that donations do not languish in donor-advised funds, but are instead used to fund charitable activities in a timely fashion.”
- This recommendation has been criticized as conflating DAFs in Canada with certain features of US DAFs
- DAFs in the US can be used as a loophole for private foundations to avoid minimum payout requirements

- However, in Canada, there are:
 - Annual disbursement quota requirements, being the minimum calculated amount that a registered charity is required to spend each year (please see next slide)
 - Inter-charity transfer rules which prohibit transfers between non-arm’s length charities for the purpose of avoiding minimum payout obligations
- Given these requirements, it is not clear why specific concerns about DAFs languishing are being raised in the Canadian context
- By way of comparison, endowments and other restricted gift funds provide donors with immediate tax benefits through donation receipts while the asset distribution from these types of restricted funds takes place over time, but without the same level of criticism as is directed towards DAFs

2. Disbursement Quota (“DQ”) Increase for Tax Years on/after January 1, 2023

	Property* in excess of \$25,000 (foundations) or \$100,000 (charitable orgs) up to \$1 million	Property* in excess of \$1 million
DQ Rate	3.5%	5%

- A DAF Holding Charity meets its DQ obligations in any given year on a **global calculation basis on all charity assets**, not on a **specific fund-by-fund** basis
- Some have questioned if individual DAFs should be required to disburse sufficient income each year
- Meeting the new 5% DQ could be challenge for charities with endowments or other funds with restrictions on how/when capital can be expended – they may need costly and time consuming court orders authorizing encroachment on capital or realized capital gains in order to cover increased DQ obligation
- See “The Ins and Outs of the Increased Disbursement Quota” presentation by Theresa Man for more details

* “Property” refers to the average value of a charity’s property in the preceding 24 months not used directly in charitable activities or administration

- In Canada, it is estimated that only 10% of DAFs hold assets over \$1 million

- So, if a DQ were in theory imposed at an individual DAF level (not on global calculation basis), a DAF Holding Charity would have lower overall DQ obligation given 3.5% DQ rate for assets under \$1 million, but could have additional administrative costs

- Average granting rate from DAFs in 2021 was 9.8% of assets, which is well in excess of the 5% DQ imposed on amounts above \$1 million (2023 CAGP Report) and many DAF Holding Charities impose own internal DQ on each DAF

- Bill C-32 also provides that (1) administrative and management expenses are deemed to not satisfy DQ obligations and (2) charities can apply for reduction in DQ obligations but these applications could be made public by the CRA
- T3010s have recently been amended by the CRA to gather more DAF-related information (please see next slide)

3. New Version of T3010 Form

- CRA released version 24 of the T3010 on January 8, 2024 - it reflects anticipated changes set out in Budget 2022 aimed at improving collection of information from charities on their investments and DAFs

- Which version is to be used?

- Version 23 - For charities with fiscal periods ending **on or before Dec. 30, 2023**

- Version 24 – For charities with fiscal periods ending **on or after Dec. 31, 2023**

- Key changes in version 24 include:

- New set of questions for charities holding DAFs, need to provide: (1) total number of DAFs held at end of the fiscal period (“FP”); (2) DAFs’ total value at end of the FP; (3) total value of donations to DAFs received during the FP; and (4) total value of qualifying disbursements made from DAFs during the FP

- New question C17 on the DQ– if charity meets DQ threshold question, then must complete the new Schedule 8 on DQ calculation and reporting

- Question C2 about Programs and the Activities outside of Canada schedule have been changed to add qualifying disbursements

4. Qualifying Disbursements – Gifts to Grantee Organizations

- ITA was amended effective June 2022 to allow registered charities to make qualifying disbursements to grantee organizations if 3 requirements are met:
 - a) the disbursement furthers one of its charitable purposes
 - b) the disbursement is exclusively applied to charitable activities to further its own charitable purposes
 - c) documentation is maintained to demonstrate (a) and (b)
- DAF Holding Charities with sole charitable purpose of making gifts to qualified donees cannot make gifts to grantee organizations
- Instead new charitable purpose(s) of an active nature will be required to be added, which will take time and money to put in place as well as CRA approval
- Final CRA Guidance released on December 19, 2023
- It continues to impose additional requirements to carry out qualifying disbursements: (1) focus on risk matrix and (2) accountability tools
- See “The New Qualifying Disbursement Regime and Healthcare Charities” presentation by Terrance Carter for more details

5. Anti-Directed Giving Provision

- Paragraph 168(1)(f) of the ITA states that a registered charity that accepts a gift “the granting of which was expressly or implicitly conditional” on it making a gift to “another person, club, society, association or organization other than a qualified donee” may have its registered charitable status revoked
- Not clear what is meant by “implicitly conditional”
- Could a donation to a DAF followed by a donor request that a gift be made from the DAF to a local non-profit organization as a qualifying disbursement trigger this provision?
- Charitable sector had hoped for clarity in the CRA Final Guidance
- While some clarity was provided on “expressly conditional” gifts, “implicitly conditional” gifts remains unclear and is of potential concern for charities
- See “The New Qualifying Disbursement Regime and Healthcare Charities” presentation by Terrance Carter for more details

6. Impact of Alternative Minimum Tax

- Budget 2023 proposed alternative minimum tax (“AMT”) changes – AMT is the alternative method to calculate income tax liability for high-income individuals so that they pay higher tax than would be paid under the “regular” tax rules – with these changes to take effect for tax years after 2023
- Key proposed changes: (1) 30% of capital gains on donations of publicly listed securities to be included in the AMT (currently not included) (2) 50% of donation tax credits (among others) will not reduce the AMT payable
- In August 2023, draft legislation to implement these changes was released and concerns were raised by various stakeholders during the consultation period – to date, these proposals remain under development since they were not included in Bill C-59 (related to the Fall Economic Statement) tabled on November 30, 2023
- If changes become law, they could impact high net-worth donors’ giving patterns, e.g. significant donations to DAFs following special events, such as property or business sales with substantial capital gains

7. Clarity Finally on Trust Reporting by Charities

- Depending on how is set up, a DAF (and all donations made to it) may be donor-restricted charitable gifts held in trust by the DAF Holding Charity
- Earlier amendments to the ITA raised concerns that some DAFs might constitute internal express trusts of a charity and, as a result, “T3s” may need to be filed
- While CRA’s long-standing administrative policy has been to not require charities to obtain separate charitable status for their internal express trusts, the charitable sector called for clarity on this issue
- This clarity from CRA finally came on November 10, 2023, when it confirmed that registered charities are not required to file “T3s” for internal trusts – this includes DAFs held by DAF Holding Charities
- Instead registered charities will continue to file T3010s, which must include aggregate information about a charity’s property, including any internal trusts

8. Importance of Granting Policies

- Need to ensure gifts from DAFs over to qualified donees are not offside of the ITA – if they are, then could result in complaints, audits, penalties and/or sanctions
- Some DAF Holding Charities place limitations on the type of qualified donees able to receive gifts from their DAFs, *e.g.* geographic, religious, cultural/philosophical or program-based
 - Need to make all of these restrictions clear to donors in granting policy or guidelines, which should then be cross-referenced in the DAF agreement itself
- Granting policy should also make clear that DAF gifts cannot result in any private benefit for the donor/their family, such as paying for charity-related membership fees/dues, tuition fees, or tickets or goods purchased for charitable fundraising
- But it is not enough to have such a granting policy - there also needs to be ongoing monitoring and enforcement by the DAF Holding Charity

9. Successor Fund Advisors of DAFs

- A DAF Holding Charity may receive recommendations about gifts to be made from a DAF from a successor fund advisor(s)
- Where the DAF agreement is silent, a donor's attorney (under power of attorney) or executor may have ability to act as the successor fund advisor
- The DAF agreement (or cross-referenced policies in the agreement) should address various scenarios:

– Can the donor appoint a fund advisor and how?

– What to do if donor does not designate a successor fund advisor?

– How many successor fund advisors can be appointed?

– How to deal with multiple successors giving contrary recommendations?

– Whether successor fund advisors must only be individuals, *e.g.* not a corporation or a group of unrelated people?

10. Impact of “Anonymous” Donations from DAFs

It is possible for a donor to a DAF to remain anonymous when the DAF Holding Charity subsequently makes a gift to a charity out of that DAF

The recipient charity may find it difficult to keep the donor informed about the effectiveness of the DAF gift

The recipient charity may also not have the information it needs to determine if it should decline the gift (e.g. because of concerns about foreign interference or conflicts of interest)

F. PRACTICAL ADVICE FOR HEALTHCARE CHARITIES WITH DAFs

- **Do your homework**
 - Do due diligence so that your healthcare charity knows how to establish and then manage DAFs correctly based on trust/tax law
- **Create templates**
 - Develop and implement written gift acceptance and granting policies for DAFs and other gifting vehicles
 - Prepare template DAF agreements of various kinds
- **Ensure your charity runs the process**
 - Your healthcare charity – not the donor or their legal counsel – should be in control in establishing DAFs, utilizing consistent procedures as set out in the original gift agreements and all related policies

- **Be vigilant**

- Avoid language suggesting that (1) DAFs belong to the donors (2) donors are “clients” with “accounts” with your charity and (3) a DAF is a donor’s own private foundation

- **Identify opportunities**

- DAFs represent opportunities for healthcare charities to have ongoing connection and engagement with their donors
- DAFs could also be a new way for healthcare charities to attract more gifts and potentially larger ones from donors
- Donors may appreciate the flexibility of DAFs
- A DAF could be structured so that the donor advice could be to request gifts be made to different programs within the healthcare charity beneficiary from one year to the next
- However, healthcare charities need to be mindful of the additional administrative work associated with DAFs – including whether they have sufficient staff available to work with donors providing DAF-related advice on an ongoing basis



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