Philanthropy Impact

Canada

Non-profit formation

The laws governing the formation and subsequent regulation of non-profits are primarily those of the province of establishment. There is no single national prescribed legal form, although incorporation under the Canada Corporations Act is widespread. The corporation is the most common form for charitable organizations (registered operating charities), but societies and unincorporated association are also acceptable. The use of trusts is restricted to foundations and is most widespread with private foundations. As of early 2011, most Canadian jurisdictions – federal and provincial – are in the process of implementing modernized not-for-profit corporations legislation, which will be gradually implemented over a number of years. At the Federal level, the Canada Not-for-Profit Corporations Act will replace the Canada Corporation Act. Provinces are creating similar legislation, for example, the Ontario Not-For-Profit Corporations Act (2011).

Governance and charitable purposes

At the federal level, the Canada Revenue Agency (CRA) is responsible for the registration of qualifying organizations as charities, subject to the anglo-saxon common law of charity. The CRA Charities Directorate is, de facto, the primary regulator of charities, although technically jurisdiction is limited to the Income Tax Act of Canada. CRA provides information on the operation of charities, as well as handling audit and compliance activities. Registered charities are required to file the T3010 annual information return with CRA, a portion of which is available to the public. Federal registration is essential if a charity wishes to issue tax receipts to donors. (**www.cra-arc.gc.ca/chrts-gvng/**)

Registered charities are designated as one of three sub-types: a charitable organization, a public foundation, or a private foundation. Each designation is prescribed by the Income Tax Act and depends on structure, control, sources of funding, and objects/activities. Charitable organizations must devote the majority of its resources to charitable activities carried out by the organization itself. Foundations typically grant to charitable organizations. Private foundations are more heavily regulated than other types of registered charities due to control by non-arm's length trustees/directors and source of funding All registered charities must comply with the disbursement quota rules in the Income Tax Act of Canada that regulate use of charitable funds. The disbursement quota rule was simplified in 2010 to reduce the reporting requirements on charities and give more discretion to directors/trustees on deployment of resources.

Registered charities can conduct charitable activities outside Canada through agency agreements or contracts. They may also grant to foreign charities if they are qualified donees under the Income Tax Act of Canada. Foreign universities make up the majority of international qualified donees in the Canadian system. Special reciprocal rules also exist in the Canadian-U.S. Income Tax Convention for donors on both sides of the border.

Taxation of Charities

Charities are tax exempt at both federal and provincial levels. Charities are not typically exempt from local property tax, but do get relief on 50% of the federal Goods & Services Tax (GST). Recently some of the larger provinces have introduced the Harmonize Sales Tax (HST), which apply to most charity expenditures. Charities may receive a rebate of up to 82% of the provincial portion of the HST.

Philanthropy Impact

Tax Relief for Donors

A charitable gift from an individual or corporation qualifies for exemption from tax. Canada has split receipting rules, dividing the gift into an eligible portion that provides tax relief and advantage portion. The advantage can be no more than 20% of the total transaction. To be eligible for tax relief, the gift must be a voluntary, irrevocable transfer of property for which the donor receives no benefit in return, unless that benefit is nominal.

Individual donors receive a combined federal and provincial tax credit from CRA. The federal portion is equal to 15% of the first $200 given to registered charities in a tax year, and a tax credit equal to 29% for donations that exceed $200. When provincial portion is factored in the tax credit for gifts over $200 ranges from 43% to 50%, which is typically equal to the highest marginal tax rate. The tax credit is applied directly against income tax owed rather than being deducted from the donor's taxable income, which provides an extra benefit for middle income earners. Corporate donors are able to deduct gifts from their taxable income resulting in federal and provincial tax assistance.

The donation contribution limit enables individual and corporate donors to claim gifts equal to 75% of annual net income; receipts may be carried forward for five years. The contribution limit for bequests and other gifts made at death by an individual is 100% of net income in the final lifetime return and 100% in the penultimate return. In addition, to ensure tax liabilities associated with gifts of capital property can be sheltered in the year of the gift, the contribution limit can be increased by an additional 25% of the capital gain of the donated property.

Donations of capital property are considered to have been disposed of at fair market value for tax purposes, which may result in a capital gain at the 50% inclusion rate. Gifts of publicly-traded securities - defined as stocks and securities on prescribed exchanges, as well as bonds and mutual fund units/shares with regularly published values – are exempt from capital gains tax if donated in kind. All registered charities are eligible recipients of gifts of public securities subject to these rules. Similar rules also exist for public company employee stock options, cultural property of national significance, and ecologically sensitive land.

Planned Giving - Canada

Planned Giving is typically called Gift Planning in Canada. Starting in 1996, the Income Tax Act of Canada has been overhauled to introduce a series of incentives for gifts of assets, as opposed to from income. These incentives provide considerable flexibility and have supported a 115% increase in receipted giving from 1995 to 2009. This rise includes declines in giving reported on tax returns in 2008 and 2009.

Generally speaking, Canadians are taxed more heavily during life than at death. Canada does not have estate taxes on the value of the estate; instead there is a deemed disposition at death on capital property. Hence, while many of the new incentives have focused on encouraging future gifts, there has been an increase in significant inter vivos donations that require gift planning. The aforementioned incentive for gifts of publicly-traded securities has been particularly important, as have the increased contribution limits. Generous incentives also exist for donating ecologically sensitive land and art/artefacts of cultural importance. Canadian gift planning has also seen the advent of combination donation plans, such as structures that combine the purchase and donation of tax-effective resource “flow-through” shares, which are a well-established feature of the Canadian tax system.

Philanthropy Impact

Direct Designation Gifts: The Income Tax Act allows a donor to name one or more charities as the beneficiary of a registered retirement plan (RRSP or RRIF) or life insurance policy. These direct designation gifts are triggered by death and provide tax relief in the final two lifetime tax returns (same as a bequest). Capital in an RRSP or RRIF is taxed at death as income if there is no spousal rollover, but the tax savings from a gift typically provide full relief. In contrast, life insurance proceeds are tax exempt and the tax credit can be used against other income on the final two lifetime returns.

Life Income Gifts

Charitable Gift Annuity: A number of charities, primarily religious organizations, self-issue charitable gift annuities. These gifts provide regular, partially tax-free payments to the donor (or designated beneficiary) and a future gift to the charity. A receipt is issued, subject to the split receipting rules, based on amount of the gift the charity is expected to receive at life expectancy of the annuitant. Charities may also offer charitable gift annuities on a reinsured basis. Technically, reinsured annuities combine a current gift with prescribed annuity purchased by the charity from a commercial insurer, but the elements are presented to the donor as a single gift structure. The receipt is determined by subtracting the fair market value of the annuity contract from the total amount transferred to the charity. Charitable gift annuities are also structured as charitable insured annuities, which utilize a commercial annuity to pay the ongoing premiums of a charity-owned life insurance policy. The donor receives tax-effective income from the combination gift structure.

Charitable Remainder Trust (CRT): The CRA provides administrative guidelines for charitable remainder trusts, although their use is limited due to the current rules and lack of legal clarity. As in the USA, the CRT involves a donor establishing an irrevocable gift to charity in return for a discounted tax receipt and a (fully taxable) cash flow; the charity has received an irrevocable gift and upon the termination of the trust will receive the remainder. CRTs eligible for tax receipts are most likely to be an inter vivos trust. Testamentary CRTs, however, are more common in Canada and typically are not eligible for a receipt due to capital encroachment provisions.

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