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It is better to give and receive

The tax benefits of charitable giving explained

During this season it is good to know that Canadians continue to be generous. According to a recent BMO report, 71% are planning charitable donations equal to or greater than last year and 61% feel they have a good or strong understanding of the tax benefits of charitable giving. These are encouraging statistics, however it's important to remember that philanthropy can be managed to enhance benefits for both charity and donor.

Canadians choosing a Charitable Giving or Donor Advised Fund have an endowment set up wherein they make an irrevocable gift of cash and other assets, which are invested to maximize the worth of the contribution and increase its value. Donors make grant recommendations on which registered charities receive donations, and these have an immediate tax benefit that can be carried forward up to five years.

To ensure enduring legacy, the charitable foundation can be named beneficiary of the registered plans and successors can be named to assume the advisory role. After passing, the plans' assets are transferred directly to the foundation and the estate receives a tax credit for the value on disposition. This can offset tax on income and effectively bypass probate, further benefiting the estate.

With gifts of life insurance, the charity is named as beneficiary in a permanent life insurance policy. When the donor passes, the charity receives the policy's cash surrender value plus any net accumulated dividends and interest. The executors receive a tax credit for the value of the donation, which can be applied to a final tax return with a provision to carry back any unused portion to the preceding tax year.

If the charity is designated as owner of the policy, all premiums paid to the policy after donation generate ongoing tax credits, providing a more immediate tax benefit, but no further tax credits accrue to the estate.

A Charitable Remainder Trust best benefits older donors who wish to donate to charity but still require income from their investment. The charity will receive the capital on death, but the donor gets an immediate tax benefit and continues to receive income during their lifetime.

Donating securities is a tax efficient method of financing philanthropy. The donations are exempt from capital gains, and the donor receives a charitable tax receipt for the full market value of the donated securities.

Consider an investor with a $100,000 stock position originally purchased for $20,000. There are two options: donating the cash after selling the shares, or donating the shares directly to charity.

If the investor sells and donates the proceeds to charity, capital gains taxation has an impact.

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Assuming a 44% marginal tax rate, the investor is left with $82,400 net proceeds to donate. The tax credit generated by the donation would be $35,600.

If the investor donates the shares directly to a charity, both are better off. By donating the shares directly, the investor is not subject to capital gains tax. This means the charity receives $100,000 worth of shares and the investor gets a $43,200 tax credit. The extra value to the investor of donating shares is $7,600. This strategy applies to all publicly traded securities, including stocks, bonds, and mutual fund investments.

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