CHARITABLE ESTATE GIFTS

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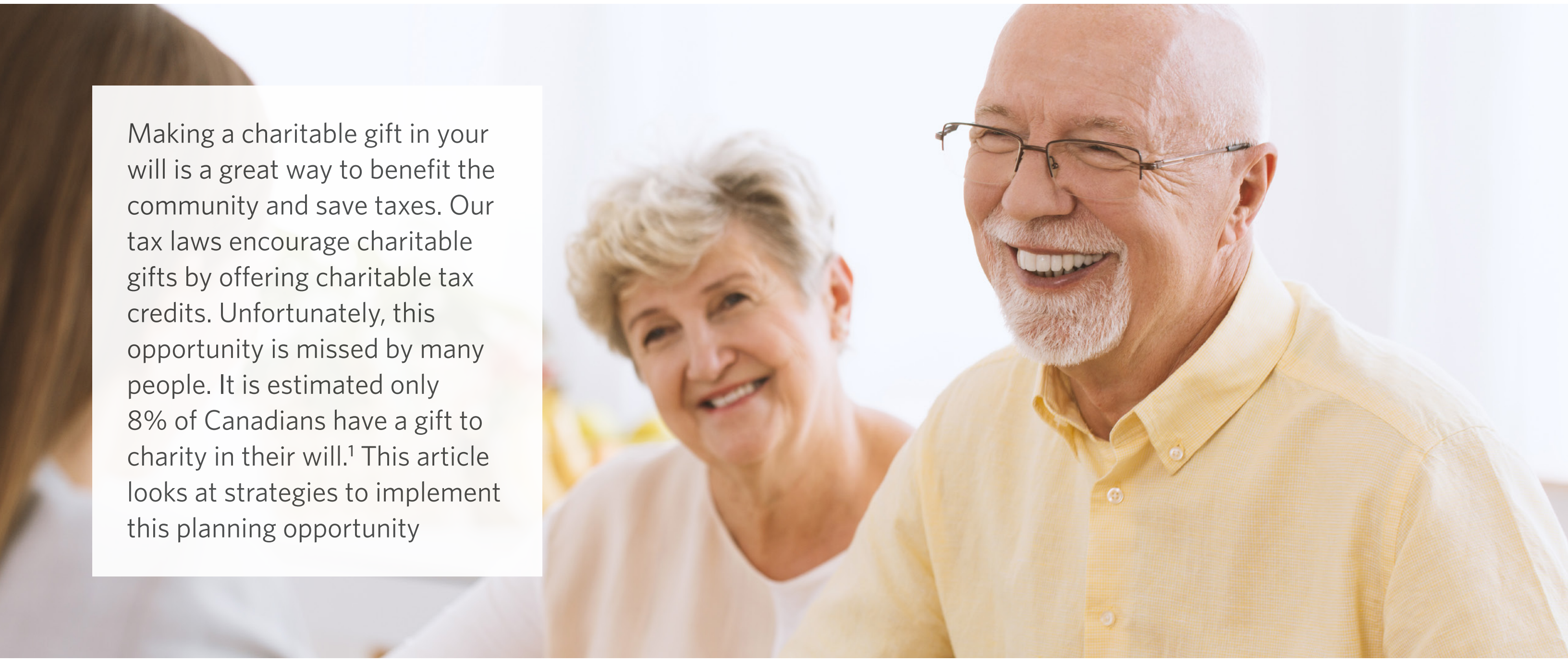

Making a charitable gift in your will is a great way to benefit the community and save taxes. Our tax laws encourage charitable gifts by offering charitable tax credits. Unfortunately, this opportunity is missed by many people. It is estimated only 8% of Canadians have a gift to charity in their will.[1] This article looks at strategies to implement this planning opportunity

Taxes on Death

In Canada, when a person dies the full value of their RRSP or RRIF as of the date of death is included in their terminal tax return. The person is also deemed to have disposed of most non-registered assets, such as stocks, bonds, mutual funds and real estate immediately before death at their fair market value. The capital gains from these deemed dispositions are included in the deceased's terminal return and are taxed at graduated personal rates.

Some of the taxes on death may be deferred if you leave property to your spouse or partner[2], or certain dependents. This will delay the tax liability until your spouse, partner or dependant sells the property or passes away.

Credits and deductions that are normally available during your lifetime can be claimed on your terminal return, including the principal residence exemption and charitable tax credits.

Make a Charitable Gift in your Estate

To make a gift to charity in your estate you need to name a registered charity in your will. Alternatively, where permitted by provincial law, you can use a beneficiary designation form or document to name a charity as a beneficiary of your registered accounts, such as an RRSP, RRIF or TFSA, or as beneficiary of a life insurance policy.[3] Your will and beneficiary designation documents are important because the executor of your estate does not have the discretion to make a charitable gift without these instructions from you.

In order to get a charitable tax credit, the gift must be given to a registered charity in Canada or another qualified donee under the *Income Tax Act*. The CRA has a searchable list of charities and qualified donees on its website at https://apps.cra-arc.gc.ca/ebci/hacc/srch/pub/dsplyBscSrch.

Registered Plans

If you have a spouse, partner or dependent child or grandchild with a disability, then it often makes sense to leave them your RRSP, RRIF, TFSA and FHSA and give other property to charities. There are special rules that allow for the deferral of tax where RRSP or RRIF assets are transferred to these relatives. Similarly, where your spouse or partner is a successor holder of your TFSA or FHSA, then the account may remain tax-exempt.[4] This can give your spouse or partner additional TFSA or FHSA room.

Note that if a charity is the beneficiary of your RRSP or RRIF, then the charity will receive the entire amount of the RRSP or RRIF. The value of the RRSP or RRIF will still be included in your income for your terminal return and the charitable tax credit may reduce tax payable, including any taxes payable from the RRSP or RRIF income inclusion.

The Tax Rules

An estate can claim a charitable tax credit against 75% of its taxable income in the year the gift is made or 5 following years.[5] In order to be able to claim the charitable tax credit against 100% of taxable income in year of death or the year prior to death, or against 75% of taxable income in the estate in a year before the gift is made, the year the gift is made or 5 years following that year, the following rules must apply:

1. The estate must be a "graduated rate estate" (GRE) or a former GRE. The estate must comply with certain restrictions and elect to be a graduated rate estate in its first tax return.
2. The gift must be made within 60 months from the date of the individual's death. The gift is made when the property is transferred to the charity. This is also the date the property is valued for the purpose of the charitable tax receipt; and
3. The gift must be from a beneficiary designation of a registered account or insurance or gifted from the estate from property that was acquired as a consequence of death or is property substituted for that property. For example, the charitable gift cannot be paid by the estate with dividends received after death or funds borrowed by the estate.

If the gift does not meet these criteria, then the estate may still be able to claim the charitable tax credit in the estate for the year the gift is made and 5 subsequent years. This may have limited impact given that the largest tax liability is usually in the terminal return.

Percentage vs. Fixed Amount

The administration of an estate takes time. It is not uncommon for a charitable gift to be made after the terminal return for the deceased is due. The charitable tax credit cannot be claimed until after the gift is made. This means that there will likely be taxes owing until the gift is made and the terminal return is amended.

One way to facilitate the charitable gift is to name a charity as a beneficiary of your registered accounts or insurance. These gifts are usually paid more quickly because they do not require probate.

Another option is to give the charity a fixed amount rather than a percentage of the estate. This is easier for the executor to gift because the amount does not need to be calculated based on the value of the entire estate.

While a fixed amount may make the charitable gift easier, it may not achieve your overall estate goals. Allocating a percentage of your estate can help make sure the gifts are allocated fairly among your beneficiaries regardless of the final value of your estate. Sometimes a fixed amount results in giving the charity too much or too little of the estate compared to your other beneficiaries.

Gift Publicly-traded Securities From the Estate

One particularly beneficial strategy is to gift publicly-traded securities in kind from the estate directly to charity. If this is done, there is no capital gains tax on the gifted shares in the terminal return or in the estate, and a charitable tax credit can be claimed for the fair market value of the securities as of the date of the transfer.

If you gift a specific dollar amount or a percentage of your estate to charity, then your executor may be able to fulfil this gift by transferring publicly-traded securities to charity depending on the wording of the will. If you are making a significant gift, then you may want to confirm with your estates lawyer that this option is available in your will. Let your executors know about the opportunity to gift securities directly from the estate for these added tax savings.

Talk to the Charity

Many charities only learn about an estate gift after someone has passed. Consider sharing information about your planned gift with the charity in advance. Charites can help plan the gift and many wish to express their gratitude to you during your lifetime.

It is important to use the charity's legal name to avoid a failed gift or potential litigation over the gift. Consider contacting the charity to confirm their legal name.

If your gift has any requirements of the charity, then the charity needs to be willing and able to carry out these requirements. For example, you may want a gift to be used for a particular program or you may want recognition of the gift on a donor wall. If you are leaving anything unusual to the charity, you should also confirm that the charity can accept the property. In these cases, it is important to include the charity in planning your gift. If the charity cannot accept the property or fulfil the requirements in your will, then your gift to charity may fail.

Conclusion

Charitable gifts in the estate are a great strategy to benefit our communities and are encouraged by tax incentives. You can make a charitable gift by naming a charity in your will or naming a charity as a beneficiary of a registered account or life insurance policy. Individuals should seek guidance from their tax and legal professionals to implement a suitable charitable gift plan.

[1] https://www.cagp-acpdp.org/en/will-power

[2] In this report, spouse refers to someone to whom you are legally married. Partner refers to a common-law partner under the Income Tax Act, which means someone who cohabits with you in a conjugal relationship, provided the two of you have cohabited for the past 12 months or are jointly parents of a child.

[3] In Quebec, you can only make beneficiary designations on registered accounts issued as an annuity of life insurance.

[4] Where your spouse or partner is named as beneficiary of your TFSA or FHSA, then there may be other options to defer tax.

[5] The 75% limit can be increased by 25 percent of any taxable capital gain or recaptured depreciation resulting from qualifying donations of capital property.

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