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INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC WEALTH MANAGEMENT SERVICES



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Charitable donations of securities

Gifted shares instead of cash may enhance
your tax benefit

To encourage charitable giving, the government provides you with a tax credit when you make a personal donation to a registered charity. This donation tax credit can be used to reduce your taxes payable. This article discusses a further potential tax benefit if you donate certain securities in-kind.

Please note the strategies discussed in this article only pertain to individuals who are donating securities held on account of capital. Holding a security on account of capital means that if you were to sell the security, you would realize a capital gain or loss. If you would realize income or losses from the sale of a security, you're holding that security on account of income. If you're uncertain which pertains to your situation, it's important to seek advice from your qualified tax advisor. Further, if you report gains on the sale of securities on account of income, it's important to seek advice from your qualified tax advisor as to a donation strategy that makes sense for you.

Gifted certain types of securities

Generally, when you gift property, the property is deemed to have been disposed of at fair market value (FMV). As such, you may realize taxable capital gains if the property has increased in value since you first acquired it. The capital gains triggered when donating securities may be eliminated in some cases if you donate the securities in-kind.

In order to qualify for the elimination of capital gains, the donated securities can be:

- Shares, debt obligations or rights listed on a designated stock exchange;
- Mutual funds;
- Interests in related segregated fund trusts; or
- Government of Canada or provincial government bonds.

In addition, the donation must be made to a qualified donee. The term qualified donee refers to an organization that can issue donation receipts for the gifts they receive from individuals or corporations. Qualified donees may be charitable organizations, public foundations or private foundations. Typically, a registered charity is a qualified donee. In this article, the terms qualified donee and registered charity are used interchangeably.

The Canada Revenue Agency (CRA) maintains a list of qualified donees that may issue official donation receipts for gifts. You may check the CRA website for the current tax status of your favourite charity.

Before making a donation in-kind, it's important to contact the qualified donee and verify that they can accept in-kind donations.

Mechanics of the donation tax credit

When you make a donation to a registered charity, you can choose to claim a tax credit on your personal tax return. The donation tax credit reduces your federal and provincial income taxes in the year you make the claim.

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You do not have to claim the donation tax credit in the year you make the donation. You may carry forward unclaimed donations for up to five tax years. If you make small annual donations, you can claim the combined donations to utilize the higher credit for gifts above \$200 in one year.

The donation tax credit is non-refundable, which means the tax credit cannot reduce the amount of your tax below zero. Federally, there are three levels of tax credits that may be available to you depending on your taxable income and the amount of the donation. The following table illustrates how you calculate your donation tax credit.

	First \$200 of donations	For individuals who are not subject to the highest federal tax bracket of 33%	For individuals who are subject to the highest federal tax rate of 33%
Federal donation credit	Federal tax credit of 15%.	Any excess donation over \$200 will result in a tax credit of 29%.	33% on the lesser of: <ul style="list-style-type: none"> The amount by which the individual's total gifts for the year exceed \$200; and The amount by which the individual's taxable income exceeds the dollar threshold for the top personal rate; and 29% on the individual's total gifts for the year above \$200 that is not eligible for the 33% rate above.
Example	An individual claims \$200 in donations. This will provide them with a federal tax credit of \$30 ($200 \times 15\%$).	An individual claims a total of \$1,000 in donations. The first \$200 will generate a \$30 federal tax credit, while the remaining \$800 will generate a \$232 federal tax credit for a total of \$262 ($200 \times 15\% + 800 \times 29\%$).	An individual has taxable income of \$215,000 and makes a charitable donation of \$20,000, their tax credit would be calculated as follows: <ul style="list-style-type: none"> \$30 ($15\% \times 200$); plus \$4,950 ($33\% \times 15,000$), which is the lesser of \$19,800 ($20,000 - 200$) or \$15,000 ($215,000 - 200,000^*$); plus \$1,392 ($29\% \times 4,800$), which is calculated as $20,000 - 200 - 15,000$. Overall, this will provide them with a \$6,372 federal donation tax credit.

* In this example, it's assumed that taxable income above \$200,000 is subject to the top federal income tax rate of 33%; the actual amount is indexed annually.

In addition to the federal tax credit illustrated above, you may also receive a provincial donation tax credit. The amount of the credit will vary depending on your province of residence. If you currently live in a province that has a surtax (currently, Prince Edward Island and Ontario have a surtax), the donation tax credit will reduce your taxes payable, which will reduce your surtax payable.

Limit on donation amount

There is no limit to the amount you can donate in a year. However, for tax purposes, you can generally only claim a charitable donation of up to 75% of your net income in a taxation year. The limit is 100% of your net taxable income for Quebec. This limit is also 100% of your net income in the year of death and the preceding year.

For example, assume Jane's net income for the year is \$100,000. She received a large inheritance in the same year and decides to make a donation of \$200,000 to her favourite charity. Jane will only be able to claim a maximum of \$75,000 (75% x \$100,000) of donations for tax purposes this year. Jane can carry forward the remainder for a maximum of five years.

Combining the elimination of capital gains with donation tax credit

When you donate securities in-kind, you may benefit from the elimination of the capital gain accrued on the securities plus the donation tax credit. As such, it may cost you less to make a donation of securities than a donation of cash. The following example illustrates this point by comparing two alternatives for donating shares of a publicly traded company with a FMV of \$50,000 and an adjusted cost base (ACB) of \$10,000 to a registered charity. The donor's combined federal and provincial marginal tax rate is 46% and the donor is also entitled to a combined federal and provincial donation tax credit at a rate of 46%.

	Sell shares and donate cash	Donate shares directly
FMV of donation (a)	\$50,000	\$50,000
Adjusted cost base	\$10,000	\$10,000
Capital gain	\$40,000	\$40,000
Taxable capital gain	\$20,000	0
Tax on capital gain @46% (b)	\$9,200	0
Tax savings from donation tax credit (c)	\$23,000	\$23,000
Total cost of donation = (a) + (b) – (c)	\$36,200	\$27,000

In this example, the donor realizes savings of \$9,200 (\$36,200 – \$27,000) by donating appreciated property

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instead of selling it and donating the proceeds. The difference is a result of the eliminated capital gains tax on the donated securities.

Donate some shares to eliminate tax on sale of securities

If you sell securities with an accrued capital gain, you may trigger a tax liability. As an alternative to selling the securities, you may want to consider donating the securities to eliminate the taxable capital gain. If you plan to use some of the sale proceeds to fund lifestyle expenses or make reinvestments, you may only want to donate a portion of the securities you're planning to dispose of and sell the remainder.

You may be able use the donation tax credit on the portion of the securities you donate to eliminate the tax liability on the capital gain triggered on the disposition of the remaining portion (i.e. portion not donated). Ask your RBC advisor about a tool that can help you estimate the portion of securities you need to donate to eliminate the tax on the securities you sell.

Donating securities in-kind at death

When an individual passes away, the individual is generally deemed to have disposed of their capital property immediately before death. If the deceased owned securities discussed earlier in this article and these securities were donated in-kind by the deceased's estate, the capital gain accrued on these securities may be eliminated. The capital gain may be eliminated if the donation is made within 60 months of the individual's death and the estate is a graduated rate estate (GRE) or was a GRE that continues to meet the other requirements of a GRE, other than the 36-month time period.

Generally, a GRE of an individual is an estate that arose on and as a consequence of the individual's death for the first 36 months after death. To be considered a GRE, the estate also needs to remain a testamentary trust and be designated for its first taxation year as the deceased individual's GRE. For more information regarding donation of securities on death, ask your RBC advisor for an article on income taxes at death.

Donating depreciated securities in-kind

Donating appreciated securities is attractive for tax purposes, as you can eliminate the capital gain. However, in some cases, donating depreciated securities may also make sense. Year-end tax planning often involves tax loss selling and charitable giving as two strategies that may be used to reduce your tax bill. Combining the two strategies is possible, as an in-kind donation of depreciated securities will trigger a capital loss for tax purposes and result in a donation tax credit equal to the FMV of the security donated. The capital loss triggered is not eliminated; it is applied first against any capital gains realized in the same year. Any remaining net capital losses can then be carried back and applied against capital gains from the previous three years, or they can be carried forward and applied against capital gains realized in a future year. You should be mindful of the “superficial loss” rules if you’re planning to repurchase the same security. For more information on the superficial loss rules, please ask your RBC advisor for the article on this topic.

Gifting other types of securities

The following sections discuss other types of securities.

Donating flow-through investments

In 2011, the federal government introduced rules to limit what they saw as excessive tax benefits that resulted from the elimination of the taxable capital gains on the donation of flow-through investments. Generally, these rules tax the portion of any capital gain realized on the sale of the flow-through securities up to the original cost of the investment. As a result, a deemed capital gain may be triggered when flow-through investments are donated. These rules apply to donations of a “flow-through share class of property” made on or after March 22, 2011.

However, these rules do not apply to flow-through common shares acquired before March 22, 2011, or mutual fund corporation shares that are received in exchange for flow-through limited partnership units acquired before August 16, 2011 (no contributions to the partnership can be made on or after August 16, 2011). For more information on donating flow-through investments, please ask your RBC advisor for an article on this topic.

Donating shares acquired through employee stock options

You may benefit from favourable tax treatment when donating shares acquired through exercising employee stock options when the shares are donated to a qualified donee.

When you exercise your stock options, you receive a taxable employment benefit which is equal to the

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difference between the FMV of the shares on the day of exercise and the option exercise price. If you exercise employee stock options and donate the acquired shares to a qualified donee, part or all of the employment benefit may be eliminated. For more information, ask your RBC advisor for an article on donating shares acquired from employee stock options.

Donating exchangeable shares

As a result of a reorganization of shares or a sale of shares to a foreign acquirer, you may have acquired exchangeable securities in order to allow you to defer the capital gains on the disposition of your securities. These exchangeable shares are generally not publicly traded but they may be exchanged for publicly traded securities. When you exchange your exchangeable shares for publicly traded shares, a deemed disposition will occur and a capital gain or loss will be triggered. The capital gain triggered on the conversion will be eliminated if the converted publicly traded securities are gifted to a registered charity within 30 days of the exchange. Another requirement is that, at the time the unlisted security is issued, it must be exchangeable for the publicly traded security and the publicly traded security must be the only consideration received on exchange.

Donating registered assets versus non-registered securities in-kind

You may donate the assets in your registered account, such as your RRSP/RRIF to a qualified donee during your lifetime or upon death. However, the assets in your registered account will not benefit from the zero capital gains inclusion treatment, as the value of the securities in your registered plan is considered income on your tax return, not a capital gain. If you withdraw securities from your RRSP/RRIF, the amount you withdraw is taxable to you as income. You could choose to donate the securities after withdrawing them from your RRSP/RRIF which allows you to benefit from the donation tax credit.

Given there’s no special exemption on the donation of registered assets, if you have a registered account and a non-registered account, you may want to consider making an in-kind donation of securities with accrued capital gains rather than donating your registered assets.

Conclusion

Making charitable donations provides individuals with a chance to give back to their community and receive tax incentives at the same time. When you donate certain securities, such as publicly traded shares, in addition to getting a donation tax receipt for the FMV of the securities donated, any capital gains you've accrued on the donated securities may also be eliminated. If you plan on making a donation, have your RBC advisor review your portfolio to determine if there are any securities with large capital gains. Speak with a qualified tax advisor to determine whether it makes sense for you to donate securities with accrued capital gains.

This article may contain strategies, not all of which will apply to your particular financial circumstances. The information in this article is not intended to provide legal, tax or insurance advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified tax, legal and/or insurance advisor before acting on any of the information in this article.

If you plan on making a donation, have your RBC advisor review your portfolio to determine if there are any securities with large capital gains.



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