

Gifts

Why not use your hard-earned money to make a difference, by helping out the people you care for the most, or your favourite charity? Meanwhile, you benefit from the opportunity to reduce your taxes. Gifting can be done during your lifetime, in contemplation of your death, or after your death through a will. This InfoPage will discuss the tax rules and other considerations involved in gifting – and may inspire you to consider how you want to gift some of your own accumulated wealth, for the benefit of both yourself and others.

Charities

The donation credit

Donations to a registered charity in Canada are eligible for a tax credit. The first \$200 you donate is eligible for a federal tax credit of 15.25% (2006, to be increased to 15.5% for 2007 and subsequent taxation years) of the donation amount. Depending on where you live, you can also claim an additional provincial tax credit of 6% to 11%. On average, this adds up to a combined rate of 25%, or a refund of about \$50.

If your donations exceed \$200 you can claim a federal tax credit of 29%, while the provincial credit ranges from 11% to 18%. On average, you'll receive a refund of 45% of your donation. Note that the donation tax credit reduces the amount of tax you owe, rather than your taxable income. This means that the credits are generally worth the same for Canadians of every income level.

If your annual charitable donations don't amount to much more than \$200, consider saving your receipts until you accumulate a larger amount and can take advantage of the higher tax credits. You may also combine your receipts with your spouse – usually the spouse with the higher income makes the claim.

You are allowed to carry your donations forward for five years. As well, during your lifetime you may claim donations up to 75% of your net income annually. In the year of death, and the year prior, donations can be as much as 100% of your net income. Donations made through your will are treated as though they were made immediately prior to your death and can be deducted on the final return.

Keep in mind that “buy low, donate high” charitable gifting schemes are no longer permitted by the Canada Revenue Agency (CRA). In these arrangements, donations generated a receipt higher in value than the actual cost of the donated property. The value of a gift you make to charity is now limited to your own cost of the property.

Donating property in-kind

If you have mutual funds or other securities that have increased in value, consider donating them in-kind. The May 2, 2006 federal budget eliminated the taxation of capital gains on in-kind transfers of publicly traded securities and mutual funds that occur on or after May 2, 2006. And you will still receive a donation receipt for the fair market value of the securities on the date of the transfer.

If you decide to transfer your securities in-kind, you will need to coordinate the transfer with your chosen charity. If the charity does not have an existing account with your financial institution, it will be required to submit an account application form along with its corporate resolution. In addition, it may provide a request to redeem the securities immediately.

This is just in case the securities drop in value after the date of transfer – the charity is still required to issue a charitable receipt for the full value as of the date of transfer. Then when you complete your Schedule 3 at tax time, you will also need to attach CRA Form T1170, *Capital gains on gifts of certain capital property*.

Publicly-listed securities acquired with employee stock options can similarly be gifted to a registered charity. Your employment benefit that is included in your taxable income is reduced similarly to 0%, as a result of the May 2, 2006 federal budget.

The following is an example of Michael and Sharon, showing the difference in the tax treatment of a cash donation compared to an in-kind donation. The example is based on a marginal tax rate of 45%.

If we compare the fictitious stories of Michael and Sharon, below, the difference in the tax treatment is apparent. For this example, assume Michael and Sharon each earn over \$120,000 annually; therefore they are both in the 45% tax bracket.

	Michael <small>(Cash donation)</small>	Sharon <small>(In-kind donation)</small>
Market value donation	\$100,000	\$100,000
Adjusted cost base	(20,000)	(20,000)
Capital gain	\$ 80,000	\$ 80,000
Taxable gain (50% vs. 0%)	\$ 40,000	\$ 0
Tax on capital gain (at 45%)(A)	(\$ 18,000)	(\$ 0)
Tax benefit on gift (at 45%)(B)	\$ 45,000	\$ 45,000
Net tax benefit (A + B)	\$ 27,000	\$ 45,000
Tax saving from donating shares instead of cash		\$ 18,000

Gifts to benefit individuals

There are many reasons for giving money or other assets to your family or friends during your lifetime – for example, to help your children with their tuition, or with purchasing their first home. You might want to help a family member reduce their debt or start up a small business. If the gift is substantial it is wise to put your intentions in writing. The gift could later be considered an early testamentary gift, and that individual's gift in your will may be reduced accordingly.

You may make a gift directly to your intended beneficiary or through a trust. Using a trust may allow you to benefit from a reduction of your future taxable income or capital gains, and reduce the future probate tax paid by your estate. At the same time, it is important not to give away too much of your property. Care in your later years can be quite costly, and you may have unexpected expenses.

Tax consequences of gifting

Gifts have immediate tax consequences that you will need to consider before transferring your gift to a registered charity or individual. For example, if you are gifting an asset other than cash, you will have an immediate taxable capital gain, but will not be taxed on future capital gains.

In addition, if you transfer assets to family members, you must consider the attribution rules. For example, if you transfer assets to your spouse, any capital gains or income will attribute back to you. Gifts to minor children will result in the attribution of the income only.

Gifts of life insurance

Another common method of gifting is through a life insurance policy. There are several different ways of using a policy to benefit a charity. One way is to purchase a new policy in the name of the charity, based on your life expectancy, with the charity as the beneficiary. You pay the premiums during your lifetime, for which you receive an annual donation receipt.

An existing or paid-up policy can also be transferred to the charity. The amount of the donation is the cash surrender value of the policy, and any premiums that you continue to pay.

You can also simply name a charity as the beneficiary of a policy you hold in your name. Upon your death, the death benefit of the policy will be paid to

For more information on the attribution rules please see our Tax & Estate InfoPage, *Income-splitting opportunities and the income attribution rules that may prevent them.*

the charity, and your estate will receive a tax credit. Alternatively, you could name your estate as the beneficiary of the life insurance policy, with a bequest of the proceeds to the charity in your will.

Gifting your RRIF

You may find yourself in the enviable position of not requiring the income from your RRIF in your retirement years. Instead, if you decide you'd rather help your favorite charity, you can reduce your tax at the same time. If you donate the annual income from your RRIF to a charity, you'll receive a donation receipt in return. In addition, you can name the charity as the beneficiary of the RRIF, so that upon your death the charity will receive the proceeds of your plan. The designation can be made directly on the plan, not just through a will. Keep in mind that the date of death value of your RRIF will be included on your final income tax return.

It is also possible to name a charity as the direct beneficiary of your RRSP. As with a RRIF, the charity will receive the entire proceeds of the RRSP upon your death, and the date-of-death value of the RRSP will be taxable on your final return. When naming a charity as beneficiary, make sure to indicate the proper name of the charity, to avoid confusion.

Advanced strategies

There are several strategies that are somewhat more complex that you may wish to consider, especially if you have a sizeable amount to donate. The explanations below are somewhat simplified. In order to properly implement these strategies you should obtain professional advice.

Charitable gift annuities. Your donation is used to purchase an annuity that generates a guaranteed annuity payment based on your life expectancy. Many major charities offer these. The benefit is that you still receive income from the amount you donate.

Residual interest in real property. Perhaps you would like to make a substantial gift to charity but your only major asset is your home. You could donate the residual interest in your home to your chosen charity but continue to have the use and enjoyment of it for as long as you live. When you make the transfer to charity, you will receive a tax receipt for

Example: Gift annuity

Tony, who has a current life expectancy of eight years, donates \$100,000 to his favourite charity. The charity uses it to purchase a gift annuity. The insurance company calculates that the cost of the annuity will be \$50,000. Tony will receive a tax receipt for \$50,000 (\$100,000 minus \$50,000) for the year of donation. He will receive \$80,000 in annuity payments over the next eight years, of which \$30,000 will be included in his income during that time.

the residual value of the home. (This should be calculated by an actuary.) You must deduct the tax credit within five years. If the home is a principal residence, there will be no capital gain upon the transfer, due to the principal residence exemption. Your home does not form part of your estate and therefore probate tax will not be applied.

Charitable remainder trust. In this strategy, you establish an *inter vivos* trust and make the charity the ultimate beneficiary. The income from the trust is payable to you as the donor during your lifetime. Real property or personal property such as stocks or paintings can be transferred to the trust, with the charity as the ultimate beneficiary. At the time of transfer, the ownership of the property will vest with the charity and you receive a donation receipt. Again, an actuary would need to calculate the residual interest.

For more information on *inter vivos* trusts please see our Tax & Estate InfoPage, *Tax planning using alter ego and joint partner trusts*.

What are your best options?

Gift planning is an important part of estate planning, but it should also be considered along with effective tax planning and other general estate planning priorities. As every individual's situation is unique, it is important to consult with your advisor, lawyer and/or tax advisor to determine your best options. It is wise to review your plan from time to time, or as your circumstances change.

For more information about this topic, contact your advisor,
call us at **1.800.874.6275** or visit our website at **www.aimtrimark.com**.

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