# The Impact of Taxation on Charitable Giving: Some Very Personal Views*

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## 1. The Long-Term Decline in Charitable Giving

I suggest that the real problem which Canada faces in relation to charities is the decline in charitable giving by the public generally which has occurred over the last 20 to 30 years. The stark reality of this decline has now been very carefully documented by J.F. Deeg, Chairman, Statistical Studies, of The Canadian Centre for Philanthropy, in an article which appeared in the Winter 1984 issue of *The Philanthropist.* Let me recapitulate what I consider to be his most important findings.

The percentage of Canadian taxpayers claiming itemized charitable donations, rather than the $100 standard deduction, in 1980 was significantly lower in all income categories than it was in 1961. In 1961, 25 per cent of all taxpayers claimed itemized deductions but by 1980 this figure had dropped to 10 per cent.

Let us consider the principal income categories. Among those earning between $10,000 and $25,000, the percentage claiming itemized donations declined in this 20-year period from 65 per cent to 12 per cent. In the $25,000-to-$50,000 income category the decline was from 84 per cent to 24.5 per cent and for the top income category, those with incomes of $50,000 or more, the decline was from 89 per cent to 49 per cent. The figures for the over-$50,000 income group are particularly startling when it is realized that the average income of these individuals in 1980 was $82,000.

When adjusted for inflation, the average charitable contribution per donor claiming itemized donations, in the $25,000 to $50,000 income category, declined by more than half in the period 1970 to 1980, from $756 per donor to $356 per donor. In the $50,000-and-over category the inflation-adjusted contributions of those claiming itemized deductions declined by 57 per cent, from $1,973 per donor to $840.

During the 34-year period, 1946 to 1980, inclusive, the average disposable after-tax personal income of Canadians, adjusted for inflation, increased by a factor of 2.3, that is, we were more than twice as well off in real terms. However, the average charitable contribution per person, also adjusted for inflation, remained virtually constant. As a percentage of inflation-adjusted income, charitable contributions dropped from 1.3 per cent to 0.6 per cent.

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These startling figures, derived primarily from taxation statistics, are confirmed by other statistics relating to family incomes and expenditures. Between 1969 and 1976 average disposable family income more than doubled but charitable donations increased by only 25 per cent. When the amount is adjusted for inflation, there has been a decline in per-family charitable donations, both absolutely and relative to income, from $87 per family in 1969 to $61 per family in 1978.

Some estimates have been made of the amount of charitable contributions made by persons claiming the standard $100 deduction, now happily of only historical interest. In 1969 this figure was estimated to be $43 per person but by 1978 it had declined by 75 per cent to only $13 per person.

This appalling situation is paralleled by corporate donations which, as a percentage of corporate profits after tax, declined more than 50 per cent between 1960 and 1980, from 1.7 per cent to 0.8 per cent.

**2. Can Changing the Tax System Reverse This Decline?**

It would be reassuring to believe that this situation could be remedied by changing the tax system as it affects charitable donations. However, I suspect that most aspects of the problem are not really affected at all by the tax system. Can we really believe that a person decides whether he or she will give a total of only $100 per year to all charities because a deduction from income is, or is not, available for tax purposes? I suggest that charitable giving reflects upbringing, cultural and religious background, and personal experience to a far greater extent than it reflects tax factors.

With one significant exception, our tax system does not permit a person to be better off financially through making a gift to charity. In the ordinary case, a person in a 50-per-cent tax bracket who gives $1,000 to charity will be out-of-pocket $500, just as if he had laid out $1,000 for some expense item which is deductible for income tax purposes. No one would suggest that a taxpayer would be prepared to lay out $1,000 for such an expense item merely because the payment was deductible for tax purposes. Why, then, should anyone think that a taxpayer would make a charitable contribution, merely to take advantage of its deductibility?

The exception to which I have alluded arises under the *Cultural Property Export and Import Act*, under which the fair market value of gifts of qualified cultural property to a designated institution are fully deductible from income under paragraph 110(1)(b.1) of the *Income Tax Act*. If such gifts are of capital property whose fair market value exceeds their adjusted cost base, this appreciation in value is not regarded as a capital gain under paragraph 69(1)(b) by reason of the exception in paragraph 39(1)(i.1). If, for example, an individual in a 50-per-cent tax bracket purchased a painting for $10,000 in 1972 and if he gives it to a public gallery in 1984, when it is worth $100,000, he receives a tax deduction worth $50,000 to him, which covers his $10,000 cost and gives him a cash profit of $40,000. This is probably as it should be, since it must not be forgotten that he has parted with something that really is worth $100,000. It seems unreasonable to subject him to the full rigours of paragraph 69(1)(b), so that he winds up, at best, with a net tax reduction of only $2,500, after he has made a gift of a $100,000 painting to a charity.

However, the possibilities for abuse under the *Cultural Property Export and Import Act* should give us concern. Of course, it is obviously fraudulent for a cultural institution and a donor of cultural property to obtain a grossly inflated valuation from an unethical appraiser and to use this valuation as the basis for claiming a deduction for income tax purposes. Such a practice cannot be condoned and people have been prosecuted and even sent to jail in this country for such behaviour. I am almost as concerned about another, much more subtle, problem. Suppose an individual is approached by a cultural institution which tells him that it knows of a valuable artifact which is available for immediate purchase for $50,000 from a collector who is under great financial pressure to dispose of it. The institution would like to acquire this artifact but it doesn't have any funds with which to do so. The individual is told that if he purchases the artifact and gives it immediately to the institution he will receive an appraisal showing that it is worth $150,000 and he will be able to claim a deduction from income of this amount. In his 50-per-cent tax bracket, this deduction is worth $75,000, with the result that after paying $50,000 for the artifact, he will have $25,000 more in his pocket than he started with.

I must emphasize that such a situation need not be, and will usually not be, fraudulent. "Fair market value" is defined as the highest price which would be negotiated by a willing, knowledgeable vendor, who is under no obligation to sell, and a willing, knowledgeable purchaser, who is under no obligation to buy, in conditions which allow for adequate time to expose the item in the market. A vendor who is under financial pressure to sell immediately, in order to pay his creditors, may be forced to sell at much below fair market value, if the market for the item is limited. Accordingly, it is by no means impossible, under present law, for the individual in my example to buy the artifact for $50,000 and to claim that its fair market value, even at the time of purchase, is $150,000. On this basis, he is, as I have stated, in a position to wind up with $25,000 more in his pocket than he started with. Such a situation disturbs me, even though I regard it as perfectly legal. In my view, cultural institutions which enjoy special tax status have a moral obligation to the taxpaying public not to engage in such transactions but instead, in these circumstances, simply to solicit a cash donation for the direct purchase of the artifact or other cultural object by the institution.

### 3. Tax Penalties on Charitable Giving of Appreciated Property

As I have suggested, in general, the tax system is relatively neutral as regards charitable giving, permitting a deduction from income only to the extent that the individual's net worth, the best measure of his capacity to pay taxes, has actually been reduced by the making of the gift. However, there are sometimes serious tax problems which inhibit charitable giving, particularly, although not exclusively, in respect of gifts of shares which have appreciated in value.

Imagine a businessman who has built up an incorporated business which was worth $1,000,000 on Valuation Day but which is today worth $10,000,000. He would like to contribute 10 per cent of his shares of his company, now worth $1,000,000, to a charitable foundation. However, if he does so, he will be deemed to have realized a capital gain of $900,000, one-half of which, or $450,000, will be included in his income in the year of gift. His annual income from other sources is $100,000 per year. In the year of the gift his income for tax purposes will rise to $550,000 but he will be entitled to a deduction of only 20 per cent of that amount, or $110,000, in that year for his charitable donation. If he makes no other charitable donations during the next five years, he will be entitled to deduct a further $20,000 per year. His total charitable deductions over the six-year period will therefore be $210,000, whereas the total inclusion in his income was $450,000. Even if we ignore the problem of the timing of his tax payments, the net inclusion in income will be $240,000. If he is in a 50-per-cent tax bracket, his generous gift to charity will cost him $120,000 out-of-pocket, in addition to his having parted with 10 per cent of his company.

He can improve this situation to some extent if he sells 10 per cent of his shares to the foundation for $1,000,000, payable at the rate of $100,000 per year over 10 years, without interest and if he then forgives $100,000 per year as a gift to the foundation. In that event, the $450,000 taxable capital gain will be spread over five years, at the rate of $90,000 per year, bringing his income for tax purposes to $190,000 per year for five years. As a result, he will be entitled to deduct $38,000 per year for five years and $20,000 per year for the next 10 years, a total of $390,000. The net inclusion in his income as a result of the making of this gift will be reduced to $60,000 and the tax cost to him of making this gift will be reduced to $30,000, if he is in a 50-per-cent tax bracket.

If this individual is prepared to sell those shares to the foundation for $1,000,000, payable at the rate of $50,000 per year for 20 years, and if he makes gifts of $50,000 per year to the foundation for 20 years by way of forgiveness of this indebtedness, the tax situation can be somewhat improved. He will be entitled to deductions of $38,000 per year for the first five years and $20,000 per year for the next 20 years, a total of $590,000, as compared with the inclusion of $450,000 of taxable capital gains in his income. That is, if he can spread his gift over a 20-year period, he can actually produce a net deduction from income of $140,000 and a tax reduction of $70,000. However, spreading it over such a long period may be quite impractical for many older donors. Even for younger donors, foregoing any other donations for such a long period would be undesirable. In addition, of course, the fact that tax has to be paid on the taxable capital gain during the first five years, while the tax benefit of the deduction for charitable donations is spread over 25 years, makes the arrangement far from generous. It may help but it is far from being a sufficient answer to the problem of how best to encourage gifts to charities of appreciated capital property.

### 4. The Need for a Legislative Solution for the Problems Arising from Gifts of Appreciated Property

Some of us have objected strenuously to what we regard as a tax penalty on charitable giving in the form of appreciated property and we have made a number of approaches to the Ministers of Finance over the years since the tax reform legislation of 1971, in each case without any apparent success.

We recognize that it would be unfair to permit a person to make a gift of appreciated capital property to a charity and to get a deduction from income for the value of the gift without having to include in his income a taxable capital gain in respect of the gift, if the charity were immediately to sell the property which it had received. In such a case, there is no real reason why the donor should not first sell the property, pay tax on the capital gain and then make a cash contribution to the charity out of his after-tax proceeds of sale.

However, this situation does not arise in the case of most gifts of appreciated capital property. Most such gifts, particularly those involving an interest in an incorporated business, are intended to be held more or less permanently by the charitable foundation or organization, as endowment funds, with only the income being distributed to charity. The nature of such gifts would not be affected by a rule which required a charity which received a gift of appreciated capital property to pay the tax which the donor would otherwise have had to pay, if the charity sold the property within, say, three years of receiving the gift. (I hope that you will write the new Minister of Finance and let him know that you consider that legislation alleviating the tax penalty on gifts to charity of appreciated capital property must be given the highest priority. Our task will not be easy, since there is serious opposition to this proposal in the senior levels of the federal Department of Finance.)

**5. An Interim Solution (?) for Gifts of Appreciated Property**

In the meantime, is there anything which can be accomplished, through tax planning, to improve this situation? I believe that there is, although, at best, it can only remove the tax penalty; it cannot create a tax incentive for substantial gifts of appreciated capital property. The key to this type of tax planning lies in making use of the tax-free rollover provisions of subsection 85(1) of the Income Tax Act, in respect of the transfer of appreciated property to a charitable foundation. Before the amendment of this subsection, applicable to dispositions of property after December 11, 1979, it was possible to transfer appreciated property to a registered charitable foundation which was incorporated with share capital, in a tax-free rollover, in return for non-participating special shares. In my view, a provision in the articles of a charitable foundation with share capital, prohibiting payment of dividends on its shares, would be legally valid.

The special nature of the shares involved in this type of gift would specifically preclude any possibility of dividend distribution (in order for the foundation to retain its status as a charitable foundation) but they could still be redeemable at the company's option or at the holder's option.

Since the amendment to subsection 85(1) of the *Income Tax Act*, this specific technique is no longer available, as the subsection now requires that the transfer be made to a taxable Canadian corporation. "A taxable Canadian corporation" is defined in paragraph 89(1)(i) in such manner as to exclude a corporation which is, by virtue of a statutory provision, exempt from tax. Paragraph 149(1)(f) exempts from taxation the taxable income of a registered charity, a term which is defined in paragraph 110(8)(c) as meaning, *inter alia*, a charitable foundation that has been registered by the Minister of National Revenue. As a result, a rollover of appreciated property to a registered charitable foundation is no longer feasible.

However, this may not present an insuperable obstacle to a tax-free rollover of appreciated property to a charitable foundation. Suppose this property is transferred to such a foundation *after* it is incorporated but *before* it applies to the Minister for, and receives, registration under the *Income Tax Act.* Since an unregistered charitable foundation is not exempt from tax, it qualifies as a taxable Canadian corporation for the purposes of the tax-free rollover under subsection 85(1). There seems to be no reason, therefore, why the technique which was available before the amendment to this subsection for tax-free transfer of appreciated property to a registered charitable foundation would not still be available today for a transfer to an unregistered charitable foundation. Such a foundation should therefore be able to join with the transferor in making an election under this subsection, thereby avoiding any immediate tax liability for the transferor.

Of course, one would expect that, immediately after the transfer, the charitable foundation would apply for registration under paragraph 110(8)(c). As long as it meets the criteria for a charitable foundation which are found in paragraph 149.1(1)(a), there seems to be no logical reason for the Minister to refuse to register it. Indeed, if he refused to do so, an appeal would lie under subsection 172(3) to the Federal Court of Appeal.

Under this plan, the appreciated property would be transferred to the unregistered charitable foundation in return for special shares which are redeemable at the holder's option for aggregate proceeds of redemption, in our example, of $1,000,000. As long as these special shares are not entitled to receive any dividend, in my opinion, it cannot be said that any part of the income of the foundation is payable to, or is otherwise available for, the personal benefit of any shareholder; this is the test established by paragraph 149.1(1)(a) for an organization which wishes to qualify as a charitable foundation.

Perhaps a contrary argument may be raised, to the effect that if income of the foundation can be used to redeem these special shares, the foundation cannot qualify as a charitable foundation. I doubt whether this could be the correct interpretation. If it were correct, it would equally be true that if the transferor had simply sold his appreciated property to the charitable foundation in return for a non-interest-bearing promissory note, the use of the foundation's income to discharge this note would also disqualify it as a charitable foundation. However, I believe that the specific exclusion in paragraph 149.1(4)(d) for debts incurred in connection with the purchase of investments means that a charitable foundation may properly devote part of its income to the discharge of a capital obligation which it has incurred in order to purchase investments provided, of course, that it still meets the usual disbursement requirements of paragraph 149.1(4)(b). There seems no reason why a charitable foundation could not also devote part of its income to the redemption of a capital "obligation" in the form of special shares, without impairing its tax status. I suggest that the only sensible meaning of the clause in paragraph 149.1(1)(a) which reads, "no part of the income of which is payable to, or is otherwise available for, the personal benefit of any proprietor, member, shareholder, trustee or settlor thereof" is that amounts may not be distributed to such persons *as income.* However, there is no rule, in my opinion, prohibiting redemption by a foundation of its special shares for an amount equal to their paid-up capital.

The transfer of appreciated capital property to a foundation could be regarded as a gift made by the transferor, to the extent of any difference between the fair market value of the transferred property and the fair market value of the foundation's special shares which he received in exchange for the transferred property. However, it seems to me that, if the special shares are redeemable on 30 days' notice, for an amount which is equal to the fair market value of the appreciated property which has been transferred to the foundation, there is no element of gift in this exchange. Of course, the transferor cannot claim any deduction for a charitable donation by reason of the exchange, notwithstanding clause (c) of subsection 245(2); there is simply no element of gift in the transaction, merely an exchange of assets of equal value.

In any event, even if there were some element of gift, paragraph 85(1)(e.2) would be inapplicable. This paragraph deals with situations where property is transferred to a corporation pursuant to subsection 85(1) at less than its fair market value and it is reasonable to regard any portion of the difference as a gift made by the transferor to or for the benefit of any other shareholder. Since the foundation will have no other shareholders, this provision cannot apply.

If the transferor of appreciated property to the foundation retained these special shares during his lifetime, he would be deemed to have disposed of them at their fair market value immediately before his death, under paragraph 70(5)(a), or, if he left them to his spouse or to a spousal trust, they would be deemed to have been disposed of at the spouse's death, under paragraph 104(4)(a), unless they had been disposed of earlier. We must, therefore, still be concerned about the tax liability which would arise in respect of these special shares at the shareholder's death or, at the latest, at the spouse's death. However, I believe that it should be possible to avoid this tax liability by providing that the special shares will be redeemable only upon 30 days' notice to the charitable foundation, given during the lifetime of the original shareholder, and that this notice will be effective only if the original shareholder is alive at the end of this 30-day period.

Legal support for this position is found in an Australian estate duty case, *Bray* v. *Commissioner of Taxation*, (1968), 42 A.L.J.R. 231. In that case, the deceased had, during his lifetime, made a loan to a company, the shareholders of which were relatives, without interest, repayable in annual instalments over a 40-year period reserving, however, the right to demand payment of the total amount outstanding at any time, on 90 days' notice in writing "under his own hand". Owen, J. of the Australian High Court held that since the right to give this notice was personal to the lender and since it therefore ceased with his death, for estate duty purposes the value of the debt owing to his estate had to be discounted to take account of the fact that it was repayable over many years, without interest.

The *Bray* decision supports the view that if the special shares issued by the charitable foundation in our example can be redeemed at any time during the original shareholder's lifetime, but only on 30 days' notice, and if such notice is effective only if the original shareholder is alive at the end of this 30-day period, the value, immediately before that shareholder's death, of his special shares, in respect of which he has not given notice of redemption more than 30 days earlier, must be calculated without reference to the possibility of redemption. Since these special shares are not entitled to any dividends, they would have only a nominal value immediately before his death for the purposes of paragraph 70(5)(a), and no tax liability could arise at the shareholder's death under this paragraph. In fact, there seems no reason why he could not realize a capital loss immediately before his death, to the extent of his adjusted cost base of these special shares.

It would be relatively simple for the shareholder to provide in his will that these shares were to be distributed after his death to a charitable organization or foundation. It would seem to be equally satisfactory, and much simpler, if they were bequeathed to the charitable foundation which had issued them. Once they have been received as a bequest by the charitable foundation, they will no longer form part of its issued share capital. Since there will then be no issued share capital, it would probably be convenient for the foundation to be converted into a non-profit corporation without share capital.

### 6. Split-Dollar Life Insurance Arrangements With a Charity

One of the more interesting uses of life insurance in estate planning involves a policy of whole life insurance which is owned jointly by the individual whose life is insured under the policy and a charity, on a split-dollar basis. The split-dollar arrangement provides that each year the charity will pay, as its share of the premium, an amount equal to the lesser of the premium and the increase for that year in the cash value of the policy. In order to enable the charity to make this payment, the individual will make a cash donation to the charity. The balance of the premium for that year will be paid by the individual, on a non-deductible basis. However, after a certain number of years, usually from five to 10, the annual increase in the cash value of the policy will equal or exceed the annual premium, at which time the whole of each year's premium will become payable by the charity.

When the individual dies, the charity will receive, as its contractual share of the insurance proceeds, an amount equal to the cash value of the policy. The balance of the proceeds will be paid to the individual's estate. If he has provided in his will that his estate's portion of the insurance proceeds will go to the charity, this amount will, I believe, be deductible as a charitable contribution in the year of his death, with a one-year carryback of any amount which cannot be fully utilized in the year of death. This can be of great value in offsetting tax liabilities arising in the year of death, in respect of taxable capital gains deemed to be realized on death, reserves which must be included in income or, in the case of some professionals, 1971 receivables. This is certainly an even more attractive arrangement than simply having a policy of insurance on an individual's life owned outright by a charity, with premiums paid out of annual cash donations by the individual whose life is insured under the policy.[1]

The only problem with the use of split-dollar insurance in this manner is that Revenue Canada doesn't like it. It has issued a private-letter ruling which states that the life insured's contributions to the charity will not be deductible for income tax purposes. It is difficult to see why this should be so. Surely, the individual's annual contributions to the charity are fully deductible under paragraph 110(1)(a), even if the charity uses these monies to pay its share of the insurance premiums. It seems even clearer that the bequest of the estate's share of the insurance proceeds is deductible in the year of death under subsection 110(2.1) with a one-year carryback of the excess under subsection 110(1.2). However, Revenue Canada has warned us of its hostility to this plan and we shall have to govern ourselves accordingly.

**7. The Trend Away From Using Private Foundations**

I think we can all be thankful that the Honourable Marc Lalonde, when he was Minister of Finance, reconsidered the proposals for changes in the tax treatment of charities which had been announced by his predecessor, the Honourable Allan MacEachen, in his famous, or infamous, budget of November 12, 1981.[2] The first signs of a change in attitude came with the agreement between Finance and the Association of Canadian Foundations which was announced on April 21, 1982.[3] It will be recalled that the November 1981 budget had proposed requiring all charities to include realized capital gains in income for the purpose of computing their disbursement quotas. It had also proposed a minimum 10-per-cent-per-year payout in respect of investments other than those in marketable securities. The April, 1982 agreement provided, instead, a new principle: that a foundation had to disburse a minimum of 4.5 per cent per year of the value of its investments. It makes a great deal of sense to frame the disbursement quota in this fashion. Because it does not have to distinguish between ordinary income and capital gains or between realized and unrealized gains, a foundation is able to pursue a rational investment policy without concerning itself with problems created by differential tax treatment of ordinary income and capital gains or of realized and unrealized gains.

To the surprise of many of us, however, new proposals from the Department of Finance in May, 1983[4] outlined an elaborate system under which the existing distinctions between public and private foundations and charitable organizations were to be eliminated. A complicated formula was proposed for a disbursement quota which would be applicable to all types of registered charities. These proposals found few supporters outside the Department of Finance and, in response to a considerable number of highly critical submissions, Mr. Lalonde requested The Canadian Centre for Philanthropy to appoint a committee of professional people with experience in this area to work with Department of Finance officials on less drastic proposals. Finance's team was led by Professor Guy Lord, of the University of Montreal, who has been working under contract with the Department. The Centre's discussions with Finance proved to be extremely useful. In addition, Professor Lord consulted with a number of other organizations and individuals before making his recommendations to the Minister. The February, 1984, federal budget[5] now seems to have resolved most of the outstanding issues in a fashion which Canadian charities and their supporters can live with.

Little purpose would be served by reviewing the budget proposals in detail, since I assume that you are quite familiar with them. However, I should like to point out one aspect of these new proposals which, in my view, deserves special attention.

You will recall that a charity which does not have an independent board of directors, and which has received more than half of its monies from a single donor or a non-arm's-length group of donors, will have to be registered in future as a private foundation. Moreover, it will have to be registered in this manner even if it carries on its charitable activities directly, rather than merely giving money to other charities.

As a private foundation, it will be subject to two special rules which will not apply to public foundations or charitable organizations. The first rule is that if a private foundation receives money from another charity it will have to disburse 100 per cent of that amount by the end of the following year; other registered charities will be required to disburse only 80 per cent. This should not really present any problem, since a private foundation really has no business receiving gifts from other charities. The second rule, however, is of much greater importance, since it imposes minimum income requirements in respect of non-qualified investments, that is, those which are not made at arm's length. Ordinary equity shares are to be exempted from this requirement, even when the investment has not been made at arm's length, but non-arm's-length loans and investments in preference or special shares will be affected. The impact of this proposal could be very serious.

Consider the following scenario:
Three brothers each own 17 per cent of the voting shares of a prosperous public company, the remaining shares being held by members of the general public. One of the brothers also owns some non-voting, non-participating preference shares of the company, bearing a normal commercial dividend rate. This brother transfers some of his preference shares to his private foundation. Since these shares are "non-qualified investments" we must be concerned about the tax on the company which is proposed by Budget Resolution 32. Assume that no such tax problem arises at the time the shares are acquired by the private foundation, since the dividend rate is not less than two-thirds of the interest rate which is prescribed for income tax purposes. Unfortunately, however, some years later the company is unable to continue paying dividends on its preference shares, either because of financial reverses or because the company needs the funds for further investment. As a result, the company will incur a liability for tax, in circumstances which I consider to be most unfair. Even if the brother who transferred these preference shares to his private foundation wished to have the company pay dividends, he is not in a position to require it to do so. Similar problems can, of course, arise even if he is in control of the company and if he would be in a position to cause it to pay dividends were it not for the fact that it is incurring substantial losses which make it improper, or even illegal, for it to declare dividends.

Having regard to this problem, consideration should be given to a development which has been taking place in the United States, namely, the development of philanthropic funds which are, in a legal sense, integral parts of a public foundation. Under U.S. law the donor to a philanthropic fund has no right to designate or direct distributions from the fund, however he may make recommendations concerning distributions from the property he has contributed. Such a philanthropic fund resembles a private foundation in all other respects. It may bear the name of the donor and may be used to memorialize his family. It provides the donor with the satisfaction of seeing the use of his philanthropic fund during his lifetime. The public foundation of which it is a part can provide professional management of the donor's contributions and it can also bring to the donor's attention the types of agencies, projects and charities which he should consider supporting.

In the United States the principal impetus for this move toward philanthropic funds as a replacement for private foundations is that the donor to a philanthropic fund is granted the maximum tax deduction for charitable contributions, that is, a deduction of up to 50 per cent of adjusted gross income for contributions in cash and a deduction of up to 30 per cent of adjusted gross income for the fair market value of contributions of appreciated long-term capital gains property. In addition, a five-year carryover is allowed for the excess of these deductions over these limits. In contrast, in the United States, gifts to private foundations are limited to a deduction of up to 20 per cent of adjusted gross income, with no provision for carryovers to future years.

In Canada, the advantage of using a philanthropic fund, rather than a private foundation, lies primarily in the philanthropic fund's complete exemption from the rules governing non-qualified investments. As a result, the issuer of shares to the foundation and the borrower of funds from the foundation are completely exempted from any possible tax liability if the transaction fails in any year to yield the minimum annual rate of return to the foundation. In my view, this reason alone is sufficient to justify serious consideration of the use of gifts of earmarked funds to public foundations, to be held as a philanthropic fund, rather than gifts to private foundations.

## EDITOR'S FOOTNOTES

1. See Glenn C. Tompkins, "Deferred Giving Through Life Insurance", *The Philanthropist*, Spring 1984.
2. See "Submissions of The Association of Canadian Foundations to the Minister of Finance on the Budget Proposals of November, 1981", *The Philanthropist*, Summer 1982.
3. See "Release dated April 21, 1982 from the Office of the Honourable Allan J. MacEachen", *The Philanthropist*, Summer 1982.
4. See "New Tax Proposals for Charities", *The Philanthropist*, Summer 1983.
5. See C. Arthur Bond, "New Tax Proposals for Charities", *The Philanthropist*, Winter 1984 and M.L. Dickson and Laurence C. Murray, "Recent Tax Developments", *The Philanthropist*, Spring 1984.