SUBMISSION TO:

HOUSE OF COMMONS STANDING

COMMITTEE ON FINANCE

HEARINGS ON TAX INCENTIVES FOR CHARITABLE DONATIONS

JANUARY 2012

OBJECTIVE:	**STIMULATE CHARITABLE GIVING WHILE REDUCING THE DEFICIT**
RECOMMENDATION:	**REMOVE THE TAX BARRIER FOR CHARITABLE GIFTS OF PRIVATE COMPANY SHARES AND REAL ESTATE.**

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STIMULATING CHARITABLE GIVING WHILE REDUCING THE DEFICIT

Executive Summary

One of the government's top priorities is to achieve a balanced budget by 2015/16. It has committed not to increase taxes or reduce transfer payments to the provinces. Consequently, a balanced budget can only be achieved by reducing spending on government programs and limiting measures that might cost tax revenues. Canada's not-for-profit sector is also facing significant fiscal challenges, because it will be difficult for the federal, provincial and municipal governments to increase funding to the charitable sector while their focus is on eliminating deficits. However, demand for services such as health care, post-secondary education, social services and arts and culture, continue to grow.

The 2012 budget provides a unique opportunity for the federal government to address these challenges. **Elimination of the capital gains tax on gifts of listed securities has resulted in over $1 billion of donations of shares each year since 2006. The capital gains tax exemption can be expanded to include gifts of two other significant appreciated capital assets—private company shares and real estate**. Charitable donations of both these asset classes are exempt from capital gains tax in the U.S and on real estate in the U.K. Extending the exemption from the capital gains tax for charitable gifts of these assets would unlock additional private wealth for public good on a basis that is much more effective and targeted than the bureaucratic process of direct government appropriation.

Any concern about valuation abuse can be addressed by one simple measure: the charity would not issue a tax receipt to the donor until it has received the cash proceeds from the sale of the asset. Also, if the purchaser of the asset is not at arm's length from the donor, the charity would need to obtain two independent, professional appraisals to confirm that the charity is receiving fair market value for the sale of the asset.

The C.D. Howe Institute hosted a Conference on Strengthening Charity Finance in Canada on March 8th, 2011. **A prominent expert on charitable giving estimated that our two proposals would result in an annual increase in charitable giving in the form of private company shares and real estate of $170 to $225 million and the tax revenue cost to the federal government would be only $50 to $65 million**. These estimates have been reviewed by a former senior tax policy professional in the Department of Finance and he has agreed that the estimates are reasonable.

The Canadian Federation for Independent Business (CFIB), which has 105,000 members, supported this initiative in its 2010 Submission to the House Finance Committee in its pre-budget consultation hearings. All members of CFIB are private enterprises. Also, most of the 1,800 mayors who are members of the Federation of Canadian Municipalities (FCM) are supportive. Not-for-profit organizations in the municipalities would receive incremental funding from donors who live in their community, but there is no tax revenue cost to the municipality because they derive their revenues primarily from property taxes, not income taxes. The C.D. Howe Institute published an e-brief on September the 15th, 2009, endorsing both these measures.

We urge the Finance Committee to recommend that the government implement these measures in the upcoming budget. The 2.1 million Canadians who are employed by the not-for-profit sector, the managements of our charities, the tens of thousands of community leaders who serve as volunteer board members and the millions of Canadians whom our charities serve, would all be very grateful.

STIMULATING CHARITABLE GIVING WHILE REDUCING THE DEFICIT

Introduction

As someone dedicated to Canada's charitable sector, I thank you for this opportunity to participate in your hearings on "Tax Incentives for Charitable Donations". These are challenging times for Canada's federal, provincial and municipal governments, as all governments are focussed on eliminating fiscal deficits. These are also challenging times for Canada's vital not-for-profit sector, as our charities cannot realistically expect governments to increase funding materially when their focus is on balancing their budgets. Our Submission addresses the challenges faced by governments and charities in this uncertain global economic environment. It outlines an opportunity for the government to stimulate additional funding for our charities from the private sector, on a basis that is value-added for all three levels of government.

Fiscal Challenges Facing the Federal Government

Eliminating the fiscal deficit by 2015/16 is one of the government's top priorities. The government has committed not to raise taxes or to reduce transfer payments to the provinces. Given these commitments, the deficit can only be eliminated by a combination of reduction in spending on government programs and limiting measures that could potentially cost the government tax revenues.

Fiscal Challenges Facing Our Charitable Sector

Given the fiscal challenges facing our governments, it is unrealistic for our not-for-profit sector to expect any material increase in direct government funding during the next few years. However, each area of our not-for-profit sector can expect demands for their services to increase for the foreseeable future:

- As our population ages, the demand for timely access to healthcare services continues to increase. All of our hospitals face the challenge of reducing waiting times;
- Fiscal challenges faced by the U.S. and European countries have raised concerns about the possibility of another recession. The uncertain job outlook will increase the need for assistance provided by our social service agencies;
- In order for Canada to compete more effectively in international markets, we need to place a greater focus on innovation and creativity, key drivers for improving productivity. Increasing our commitment to post-secondary education is an important part of this strategy;
- Our arts and cultural organizations play an important role in making Canada an attractive place in which to live and work. Demand for their services continues to grow.

In addition to the increased funding requirements to address the growing demand for their services, our charities have also suffered from the reduction in the number and size of major gifts of stock. The recent collapse of global stock markets and the decline in the value of their endowment funds, and the reduction in the disbursement percentage caused by the decline in interest rates, have also reduced financial support from endowment funds.

The Opportunity

The government of Canada now has a unique opportunity to unlock significant ***additional*** private wealth for public good in the next budget. **The government can capitalize on the enormous success of the 2006 budget measure that eliminated the remaining capital gains tax on gifts of listed securities. Removal of this barrier has resulted in annual charitable donations of listed securities of over $1 billion each year since 2006**.

The capital gains tax exemption that currently applies to gifts of listed securities should be expanded to include gifts of two other significant asset classes that have unlocked appreciation. **These two currently untapped sources of potential donations are shares of private companies and real estate.** The total value of all private companies exceeds the total market value of all publicly listed securities in Canada. Real estate, including principal residences, represents approximately 40% of the personal net worth of all Canadians. The proposal would apply to gifts of vacation, industrial, commercial and residential investment properties, but would exclude principal residences, which are already tax exempt. Both asset classes are exempt from capital gains taxes in the United States and gifts of real estate are exempt in the U.K. when the property is donated. Currently, in Canada, only gifts of listed securities are exempt.

Addressing Concerns about Valuation Abuse for Gifts of Private Company Shares

The capital gains tax exemption in Canada was limited to listed securities because there is a publicly listed market for these securities and there was no concern about valuation abuse. Any concern about valuation abuse for gifts of private company shares can be addressed by requiring a charity to issue a tax receipt to the donor only after it has received the cash proceeds from the sale of the asset. In the vast majority of cases, the charity wants to monetize its gift of appreciated capital property at the earliest opportunity, for its fair market value. If the purchaser of the asset is not at arm's-length from the donor, the charity would be required to obtain two independent, third-party professional appraisals for the asset to ensure that it is receiving fair market value on the sale.

These conditions not only address any concerns about valuation abuse, but also significantly decrease the administrative burden and risk for the charity. Frankly, it would be simpler and less costly for both the charity and the donor than the U.S. system. The U.S. requires an independent third party evaluation of the private company shares and the donor receives a tax receipt even though the charity has not yet received the cash from the sale of the asset.

Addressing Concerns about Valuation Abuse for Gifts of Real Estate

We propose two separate measures for charities to receive gifts of real estate, both of which would be exempt from capital gains taxes. Under the first measure, the qualified donee would receive all or part of the cash proceeds from the sale of the property, and the donor would be exempt from capital gains tax on that portion of the real estate sale which he or she donated to the charity. If the purchaser of the real estate asset is a non-arm's length party, two independent, third party appraisals would be required, as is proposed for private company shares. Under the second measure, the donor could gift the real estate to the qualified donee to retain the property for use within its mission.

In the United States, once the charity assumes ownership of the property, it has to address the liability and administrative issues associated with the ownership of the real estate and the complexities associated with its sale. Understandably, if charities had a choice, they would prefer not to assume ownership of the donated property, but, instead, simply receive the cash proceeds derived from its sale.

Under our proposal, the donor would be responsible for the sale of the real estate and the valuation of the gift would be based upon a matter of fact, rather than an evaluation. The precedent exists within the Income Tax Act of Canada to sell certain property to fund a donation – and to eliminate the capital gains tax on its disposition – as long as the cash is donated within a certain period of time. Gifts of publicly traded securities acquired under a securities option plan must be donated within 30 days of the exercise date to eliminate the capital gain. Moreover, there is a provision in the Income Tax Act that provides the ability to donate all or a portion of the cash proceeds of disposition to a qualified donee, if this gift is made within 30 days of the tax event.

Obviously, a taxpayer willing to make a gift of real estate, for use or occupation by the charity related to its charitable purposes, should not be penalized with the introduction of a new tax incentive. Those donors should also be exempt from capital gains taxes, but appropriate restrictions would need to be included, such as an independent, third party valuation of the property and the requirements for the charity to hold the real estate for a minimum of 10 years, as well as other restrictions.

Federal Tax Revenue Cost

The federal tax revenue cost of the proposal depends on the amount of the increase in charitable gifts of private company shares and taxable real estate and the adjusted cost base (ACB) of the donated property. **The C.D. Howe Institute hosted a Conference on Strengthening Charity Finance in Canada on March 8th, 2011. A presenter at the Conference estimated that our two proposals would result in an annual increase in charitable giving in the form of private company shares and real estate of $170 to $225 million and the tax revenue cost to the federal government would be only $50 to $65 million.** These estimates were based upon an analysis of the Department of Finance’s Annual Tax Expenditure Report, taking into consideration the percentage of donations of appreciated capital property in the U.S. that are made in the form of private company shares and real estate. These estimates have been reviewed by a former senior tax policy professional in the Department of Finance and he has agreed that the estimates are reasonable.

Canadian Federation for Independent Business (CFIB)

The Canadian Federation for Independent Business (CFIB), an organization that represents 105,000 businesses across Canada, all of which are private corporations or enterprises, has an interest in the proposal to remove the capital gains tax on gifts of private company shares. The CFIB endorsed this proposal in its October, 2010 Submission to the House Finance Committee’s pre-budget consultation hearings. This measure would be of particular interest to business owners considering the sale of their company as an alternative to turning over their business to their children. The sale of their business could be a catalyst for a significant charitable donation to a not-for-profit organization in their community. Importantly, the measure would level the playing field for entrepreneurs who decide to maintain private company status relative to those who take their company public and donate shares to a charity.

Federation of Canadian Municipalities (FCM)

The Federation of Canadian Municipalities (FCM) has 1,800 members who are mayors of cities, towns and villages across Canada. As municipalities derive their revenues primarily from property taxes, not income taxes, these measures would have no tax revenue cost to the municipalities. However, the measures would result in significant increases in private sector funding for the not-for-profit organizations located in their municipalities. Consequently, most of the 1,800 FCM members are supportive of these proposals. To illustrate this point, 35 mayors of major cities across Canada wrote letters of support for the proposal to remove the capital gains tax on gifts of listed securities prior to the 2006 budget. They recognized that the measure would provide crucial incremental funding for their hospitals, universities, arts and cultural organizations and social service agencies.

Thomas Mulcair, the former Finance Critic for the NDP and now one of the candidates to be the Leader of the Party, stated during the House Finance Committee's September 15th, 2009 pre-budget consultation that "I want to begin by saying that Mr. Johnson, whom I have already had the pleasure of meeting and speaking with on the topic he has raised today, is entirely right. My colleague Judy Wasylycia-Leis, the member for Winnipeg North, and myself have had the opportunity of telling him that we support his proposal and find it most interesting. As usual, the devil is in the details. There have to be safeguards in order to ensure that no one can get around or abuse the system, but the idea is positively brilliant, at a time when universities and the health care sector in particular need more assistance. It would be good if we could get things moving." [as quoted in Hansard]

Also, it is relevant that Scott Brison, the Finance Critic for the Liberal Party, has communicated his support for these two measures.

Although these are challenging times for our governments and our charities, implementation of these two proposals in the next federal budget would be gratefully appreciated by the 2.1 million Canadians employed in our not-for-profit sector, the managements of our hospitals, universities, arts and culture organizations and social service agencies across Canada, and the tens of thousands of business and community leaders who serve as volunteer board members of these organizations. In addition to providing advice and oversight to the managements of our charities, each of these individuals is involved in private sector fundraising, as well as donating personally. The millions of Canadians whom our charities serve would be very grateful.

We strongly recommend that your Committee support these proposals in your report to the Minister of Finance!