

Donate stock and get a tax break

Get a capital gains tax cut when you give to charity

Arthur Drache

Financial Post

Tuesday, December 23, 2003

For a large number of Canadians, the end of the year focuses their attention on charitable giving. But many who could take advantage of the nice tax break associated with such donations are losing out on some of the benefits.

When a donation is made with appreciated stocks (including units in mutual funds) that are listed on an exchange and which are given to a charity other than a private foundation, the normal capital-gain bite is cut to one-half of the usual percentage. That is, instead of reporting 50% of the gain as income, you only report 25% of the gain. But you get a tax credit based on the full fair market value of the gift.

Many argue that people who donate relatively modest amounts to smaller charities do not get much benefit from this incentive. But the benefits are available if both the donor and the organization want to take advantage of the incentive.

We recent looked at a portfolio of a "small" investor who amongst other things had shares of Royal Bank of Canada, which had an adjusted cost base of about \$14 a share. They are now worth about \$60 a share. He also had many other "safe" investments, blue chips, which he had held for about 10 years, including other bank stocks and oil stocks.

This year he has some cash flow problems, but did not want to cut back on donations to some of his favourite charities. He would normally give between \$1,000 and \$2,000 to each of a half dozen organizations, including his church.

We pointed out that a gift of 20 shares of Royal Bank stock would be worth about \$1,200. We gave this simple example using Ontario tax rates:

EXAMPLE 1 Suppose that in order to give \$1,200, he sold 20 shares of the stock. If he did this, we would get the following result.

Cost of stock for tax purposes

(20 times \$14) \$280

Proceeds of sale \$1,200

Capital gain \$920

Taxable capital gain

(50% of full gain) \$460

Tax liability (46% of \$460)\$212

Assuming he gifted the full \$1,200 in proceeds to the charity, the value in cash of the charitable tax credit would, at the combined top federal and provincial rate of 46%, be \$552. Thus, after paying for the capital gain, he would have \$340 in tax credits to offset other tax liabilities.

EXAMPLE 2 All the facts are the same, but he gifts 20 shares of Royal Bank stock to the charity. As a consequence, the inclusion rate in respect of the capital gains falls to 25%.

Cost of stock for tax purposes

(20 times \$14) \$280

Proceeds of sale \$1,200

Capital gain \$920

Taxable capital gain

(25% of full gain) \$230

Tax liability (46% of \$230) \$106

The value of the gift, of course, is still \$1,200, but he ends up with tax credits of \$552 and after taking into account the \$106 in tax on the capital gain, he has an extra \$446 to work with.

And equally important, he has no cash flow problem because he needn't make up any shortfall in cash to give the charity the \$1,200.

The major problem we found was that because many charities do not have investments of their own, they do not have a brokerage account to which the donated stock can be gifted. And as a consequence some of the charities simply did not want to take the gift of stock. This is not a unique situation, but it helps to explain the genesis of the criticism that smaller charities do not benefit from the incentive. The fact is that many would and could benefit but for the fact that they are not being co-operative with potential donors.

On the other hand, we are getting reports that many larger charities, most notably public foundations, are prepared to work out an arrangement where they will accept the stock gift on behalf of the small charities, sell the stock soon after it is received and transfer the funds to the charity, giving the small charity the benefit of their experience and facilities.

In some cases, the larger charities will charge a fee, but we have also heard of cases where it was done at no charge simply to accommodate another local charity.

The incentive is there and it works for even modest donors who have appreciated stock to give away. We would hope that donors and charities can work out methods by which more stock donations are given, with the ensuing benefits offering a bonus to donors.

© National Post 2003

Arthur Drache, QC, has been a *Financial Post* columnist and contributing editor for more than 20 years. He is a taxation specialist and a partner in the Ottawa law firm of Drache, Burke-Robertson & Buchmayer. His column appears Tuesdays.

REPRINTED WITH PERMISSION FROM ARTHUR DRACHE December 24, 2003