THE CANADIAN BAR ASSOCIATION
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August 18, 2014

Via email: alexandra.maclean@fin.gc.ca; grant.nash@fin.gc.ca

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Dear Ms. MacLean and Mr. Nash:

**Re: Proposals to amend Estate Donations Provisions in the *Income Tax Act***

I am writing on behalf of the National Wills, Estates and Trusts Section of the Canadian Bar Association (CBA Section). The CBA Section represents lawyers specializing in wills, estates and trusts issues from every part of Canada.

The 2014 federal budget (the Budget) proposed changes to Estate Donations, the tax rules for gifts made to charities by will. We commend the greater flexibility to the tax benefits for charitable giving by will. We would like to propose additional changes to improve taxpayer access to the tax benefits of charitable giving. In addition we have some comments on the Budget provisions.

Our proposals would permit easier access to the benefits of charitable giving by wills, trusts and estates in circumstances where it is equitable to do so. These changes would simplify the circumstances in which a donation tax credit is available. Currently some donations through trusts and estates are subject to limitations that have no policy basis. Tax planning to avoid these limitations can require the imposition of artificial or arbitrary conditions that are inconsistent with the charitable intention, and often cannot be achieved without the assistance of sophisticated professional advice.

We propose the following changes:

1. **A distribution of capital from a trust to a beneficiary that is a registered charity or other qualified donee in satisfaction of its capital interest in a trust should qualify for the donation tax credit.**

Our most important proposal addresses barriers to the availability of a donation tax credit where a trustee makes a distribution of trust capital to a registered charity or qualified donee[1] in

[1] We refer to registered charity and charity throughout this letter. These references include all qualified donees as defined in the *Income Tax Act*.

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satisfaction of a capital interest in the trust. We propose an amendment to the *Income Tax Act* (ITA) that ensures such distributions are treated as "gifts", or are otherwise entitled to the donation tax credit, where the distribution is made pursuant to the terms of the trust without the exercise of any discretion the part of the trustee.

Currently, the Canada Revenue Agency (CRA) disallows a donation tax credit for distributions of capital to a registered charity if the transfer is mandated under the terms of the trust. In this case the transfer is not considered a "gift" but rather a distribution to a beneficiary in satisfaction of its interest in the trust, so no donation tax credit is available. The CRA takes the position that the trustee cannot make a voluntary transfer where it is mandated by the terms of the trust, and thus there is "no gift". This is an unduly narrow view and ignores the voluntary act of the settlor or testator when the trust or will was signed. In any event, it results in the denial of a donation tax credit in situations where there is no policy-based reason to do so.

Immediate gifts in a will are not subject to this discretionary requirement. The CBA Section sees no principled basis for allowing a donation tax credit in the case of an immediate gift to a registered charity in a will, and denying a donation tax credit in the case of a delayed gift to a registered charity under the terms of a testamentary or *inter vivos* trust.

This proposal would extend to all trusts, not just testamentary trusts. For example, consider an alter ego trust in which there is a distribution to a registered charity on the death of the settlor. Based on the CRA's current assessing practice that distribution does not qualify for a donation tax credit unless the trustee has some discretion, such as to the quantum of the distribution to the registered charity. Again, this interpretation of the nature of a gift ignores the fact that the gift is put in motion by the settlor in creating and funding the alter ego trust, and is simply completed by the trustee on the settlor's death.

Denying the donation tax credit on the termination of a life interest can be particularly harsh where there is a deemed disposition on the death of the life tenant(s), as in the case of an alter ego trust, joint partner trust, or testamentary or *inter vivos* spousal trust. The result is a large tax liability with no offsetting donation tax credit –all for want of a discretionary condition in the terms of the trust. However, our proposal should not be restricted to only these trusts, but to all situations in which a distribution of capital is made by a trust to a beneficiary in satisfaction of a capital interest in a trust.

The CRA has had numerous requests for informal interpretations and advance rulings to clarify what it considers to be sufficient discretion to convert a distribution in satisfaction of a capital interest in a trust into a gift by the trust or estate. Much uncertainty continues to exist. Terms permitting trustee discretion on the amount or identity of the registered charity are now included in will and trust planning — not because the taxpayer wishes to permit the discretion, but to ensure that tax relief is available for charitable giving from the trust. In other cases, taxpayers and their advisers are unaware that what they assume to be gifts to a registered charity by a trust will not produce any donation tax credit. The requirement for an element of discretion is not only arbitrary, but can present a trap for the unwary, introducing undesirable uncertainty for the settlor or testator, the trustee or executor, and the registered charity.

2. **A gift to a registered charity under the terms of a trust made on termination of a life interest should have the same flexibility for timing the use of the donation tax credit as gifts by will.**

Our second proposal follows from the first and addresses an important timing issue for gifts made on the termination of a life interest. Where a trust provides for a charitable gift on the termination of a life interest, we propose an addition to the ITA, similar to subsection 118.1(5) as amended by

the Budget. This would permit the trustee or legal representative to elect to use the donation tax credit, in the year of death of the life tenant, in the year in which the payment is made, or in any intervening year. The 36-month limitation in the Budget (that is, the gift must be made within 36 months after the death of the life tenant) might be appropriate, subject to Ministerial discretion to extend the period if the trustee makes a timely request.

This proposal would address the mismatch of a tax liability and donation tax credit where there is a deemed disposition on the death of a lift tenant, but a delay in the payment to the registered charity to a subsequent taxation year. For example, there is a deemed disposition on the death of the life tenant of a spousal trust or alter ego trust, or on the death of the last life tenant in the case of a joint partner trust. If the donation is made after the year of the "triggering" death, the donation tax credit would not be available to offset the tax liability for the deemed disposition. This may occur, for example, if the life tenant dies late in the taxation year of the trust before there is time to make the donation, or if time is needed to liquidate assets to complete the donation. Currently, subsection 118.1(5) addresses this mismatch on death where the deemed disposition triggers tax, but gifts made by will are paid by the personal representative at a later date.

### 3. The 36-month period for qualifying donations made by will should be subject to extension

The Budget proposals will limit the availability of the donation tax credit for gifts by will to those actually made by the trustee within 36 months after the death of the testator. In many situations the actual gift to a registered charity might be delayed beyond 36 months. It may be necessary to complete a sale of assets, or settle litigation, for example, before the trustee can make the payment, or even determine the quantum. CRA administrative policies deal with delayed payments for gifts by will in the absence of a specific requirement in the ITA. The discretion CRA exercises now may not be available if this provision is not included in the new legislation. We think it is appropriate to add a provision similar to subsection 70(6) to permit the personal representative to make a written application to the Minister to extend the time for making the donation beyond the 36-month period.

### 4. Settlements giving rise to charitable donations on death qualify for donation tax credit

An individual's intent to bestow a benefit on a registered charity at the time of death can be threatened where another person seeks financial gain (to the detriment of the registered charity) a successful legal challenge to the validity or interpretation of the relevant document. The challenge may be resolved not by a judicial determination, but by alternative dispute resolution (ADR). Mediation is one form of ADR that has become a favoured approach in many jurisdictions. Indeed, Ontario law requires that before a court can decide the merits of a dispute about the entitlement of a registered charity to benefit from the purported intentions of an individual who died in the City of Toronto, the City of Ottawa or Essex County, the parties must participate in mediation.

In mediation, a third party neutral seeks to assist the parties to reach a mutually agreeable resolution of the dispute. A mediated resolution of the dispute will result in a settlement that gives a registered charity an amount of money or property that lies somewhere between the extreme positions articulated each party. As a result, the amount or nature of the benefit received by the registered charity cannot be characterized as a gift made by the deceased person. The CBA Section sees no policy reason for denying the enhanced donation tax credit for the full value of the money or property ultimately received by the registered charity in the settlement, as it might inhibit parties from resolving a dispute through ADR.

A mediated settlement could result in a gratuitous payment to a registered charity, that is, a payment having no nexus to the dispute being mediated. The following example will illustrate.
A and B are in dispute over the interpretation of a will. B proposes a settlement where B will make

a payment to a registered charity, C, known to be important to A. A accepts B's settlement proposal. C would have no entitlement to that payment under any interpretation of the will: the testator had no intent to benefit C under the will.

The CBA Section urges the government to ensure that, subject to the exception in the last paragraph, any changes to the ITA on the availability of the donation tax credit be sufficiently elastic to make it available for the full value of any amount or property paid or transferred to a registered charity as a result of a mediated settlement of a dispute arising out of a document purporting to have been authored by a deceased individual. With the delays inherent in extra-judicial dispute resolution, those changes should allow for Ministerial discretion to extend any period mandated for the timing of that payment or transfer.

**Conclusion**

Thank you for considering these views of the CBA Section on the rules for charitable donations relating to gifts made by will. We would be pleased to provide further information or respond to any questions at your convenience.

Yours truly,

*(original signed by Rebecca Bromwich for Richard Niedermayer)*

Richard Niedermayer
Chair, National Wills, Estates and Trusts Section