Transferring Wealth: Leaving a Legacy

As the parents of baby boomers make their final exit, an estimated $1 trillion in assets in the form of cash and securities, real estate, and other valuables will be transferred over the next two decades. Last week we looked at various strategies for transferring that wealth to family members. This issue looks at ways in which charitable giving can fit into an overall wealth transfer strategy—one that is designed to minimize taxes and maximize the value of a charitable bequest.

Giving and receiving: the two-way street

While the desire to leave a legacy is part of the human condition, our charitable urges don't go unrewarded when it comes to minimizing our taxes. Federal and provincial governments recognize the value of our charitable donations and provide tax benefits for those who give. It's the tax considerations to you personally and to your estate that can make charitable giving an important part of your wealth transfer strategy.

Better to give than to receive

Gifts can include securities, real estate, tangible personal property, and the like, usually coming with tax-saving on accrued capital gains. Charitable giving has become a lot easier for investors after the government eliminated capital gains tax on charitable gifts of publicly traded securities, bonds, and mutual funds. This tax exemption applies to gifts of these assets to registered charitable institutions as well as public and private foundations. In effect, the charity receives the full present value of the donation, the investor pays no capital gains on the taxable value of the assets at the time of the donation, and the investor or the investor's estate gets a tax credit for the full value of the donation.

Transferring your income-producing assets to a Charitable Remainder Trust with yourself and a charity as the designated beneficiaries is another way to maximize your gift. The income flows back to the donor or a designated beneficiary for life or for a set number of years, after which the trust is terminated and the assets (the remainder) are transferred to the charity or foundation. This transfer may trigger capital gains tax, which will be more than offset by the donor's tax credit received on the present value of the donated assets.

Leverage your gifting

Life insurance can be an attractive way to enhance the legacy you leave behind as you are buying a product for pennies on the dollar. A number of strategies can be used. You can purchase the insurance yourself and name the charity as beneficiary, or you can own the policy yourself and name your estate as beneficiary and provide direction in your will to gift the funds. You may also choose to make the charity the owner of the insurance policy outright, with you paying the premiums on the charity's behalf. Not only do each of these options provide the charity with the policy's proceeds when you die, but the charity will issue a charitable receipt you can use on your tax return to reduce the amount of tax you pay. And since the gift is not part of your estate, it escapes probate taxes as well as the often-lengthy process of settling the estate (unless you name your estate as beneficiary). Nor are such gifts contestable by the putative heirs.

Often a life insurance policy is combined with a life annuity or trust, which can further leverage the size of your donation. Insured annuities can create an effective way to both give and receive. A lump sum donation is made to the charity generating a tax receipt, which can be carried forward (up to 5 years) if not fully used in the current year. The charity then uses the donation to buy an annuity on the donor's life, which produces tax-free annuity income for the charity. The annuity income is then used to buy life insurance with a death benefit far greater than the original cash donation.

Alternatively, the income generated by a Remainder Trust could pay the premiums on a life insurance contract with a death benefit equal to the originally donated assets to the trust. Upon the donor's death, the Remainder Trust's assets go to the charity and the beneficiaries (usually a surviving spouse or the children) receive the tax-exempt death benefit.

Creating a legacy

The desire to leave a legacy or to pass on to those in need requires thought and planning to accompany the sentiment of giving to a good cause. If you envision philanthropy as part of your estate planning, your financial advisor can work with our estate planning advisors to develop your planned giving strategy, one that can make an impact while extending your legacy and generosity well into the future.

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