

Scotia Private Client Group

Overview of Private Foundations

This overview has been prepared for individuals and families considering the establishment of a private foundation in Canada. It provides an introduction to this charitable tool, outlining benefits and obligations, as well as services provided by the Scotia Private Client Group.

The Scotia Private Client Group is the leading provider of services to private foundations in the country, with a 75-year tradition, 400 foundations and \$1 billion in assets, which represents 10% of private foundations in Canada. These foundations range in assets from \$500,000 to \$100 million. Services are offered on a “debundled” basis, which enables clients to retain legal control of the foundation and relationships with existing advisors, including outside investment counsel.

1. Context and Definition

There are 80,950 registered charities in Canada divided into three main classes: Charitable Organizations (operating charities – 88% of total), Public Foundations (fundraising and endowment charities with public support – 7% of total), and Private Foundations (5% of total).

There are approximately 4,000 private foundations registered in Canada, which collectively hold approximately \$10 billion in assets in trust for charitable purposes. In simple terms, private foundations are defined as charities where 50% or more of the contributed capital is from an individual or family and the board of directors or trustees are not at arm’s length from each other or the principal donor. In other words, private foundations are, in most cases, family foundations.

2. Long-term Philanthropy

Private foundations are exceptionally flexible tools for creative, long-term philanthropy. They can be thought of as perpetual “philanthropic holding companies”. They are often entities that “live” for more than 100 years and involve successive generations of families. Alternately, by appointing a corporate trustee or service provider a private foundation can operate perpetually to carry out the founder’s intent without direct family involvement. A few foundations, however, have sunset provisions built into them at the outset, typically because the founders want to use the assets for charity within a certain period of time.

The J. P. Bickell Foundation is an example of the long-term nature of private foundation philanthropy. Founded by Toronto-businessman John Paris Bickell through his will 1953, the Foundation started with \$13 million in capital. It has a mixed granting mandate: specific charities, such as the Hospital for Sick Children, as well as charities across

Ontario. Mr. Bickell made the choice to provide long-term benefit to these charities. As of 2004, the Foundation has granted \$107 million to charities, and the capital has grown to \$98 million. And the legacy continues with annual distributions of over \$4 million. Mr. Bickell could have made outright gifts to these charities (although most were not in existence when he died), and if he did the capital would probably have been well-spent within 5 to 10 years. Instead, he chose to create a perpetual, dynamic legacy that meets the ongoing needs of society. It was a philanthropic choice that left Canada a richer place. Scotiatrust (and its predecessor National Trust) has been trustee since inception.

3. Granting Flexibility

While some foundations do function as “operating charities”, engaging in direct charitable works, most make grants (donations) to other registered charities in Canada. There is an obligation to distribute annually a minimum equivalent to 3.5% of the 24-month average market value of the assets on the charitable mission of the foundation. Donations may also be made on a flow-through basis, where a minimum of 80% of the annual gifts to the foundation must be used in the subsequent year for charitable purposes.

4. Legal Structure

In Canada, charitable foundations are established through a two-step legal process. First, the entity is established as a legal entity (either as a trust or not-for-profit corporation). Second, it is registered with the Charities Directorate of Canada Revenue Agency (CRA). All charities are subject to the Income Tax Act of Canada, and must make annual filings to Canada Revenue Agency (the public portion of the filings are posted on the CRA website). Foundations are also subject to provincial trust and charity legislation, but most provinces, with the notable exception of Ontario, are not active in this area.

5. Trusts v. Corporations

While incorporated foundations are most common in Canada, the trust-based foundation is a viable alternative offering a number of advantages. Trusts are created with a trust indenture or agreement, and unlike corporations, do not require federal or provincial incorporation. As a result, they are simpler to set up and there are no annual filings (apart from the T3010 charity return), no audit, and greater privacy for the family. Incorporated foundations require a minimum of three unpaid directors, which is awkward for individuals without children or for families who are small or dispersed. In contrast, foundations established as trusts are ideally suited for succession planning. Often they start with three or more trustees, and then evolve over time to a single corporate trustee. This succession plan ensures that administrative and fiduciary burdens are addressed, without lessening the family's involvement in philanthropy.

6. Tax Planning

While private foundations are principally tools for philanthropy, they are also excellent financial and estate planning tools. Individuals and corporations who donate to private foundations are eligible for tax receipts for the fair market value of the gift. The receipt

translates into tax credits for an individual ranging from 39% to 48% of each dollar donated (depends on provincial tax rates). A variety of assets -- from cash and securities to life insurance and trusts -- can be used to fund foundations. Private foundations are tax-exempt entities and revenue and capital gains accumulate tax-free. All gifts to foundations are irrevocable; gifts cannot be refunded to the donor(s).

The Income Tax Act allows Canadian taxpayers to shift their obligatory contribution to society from taxes to charities, without disadvantaging the family. These significant tax savings are available through prudent planning and clear charitable intent. It is recommended that a complete financial and estate plan be conducted at the same time as the foundation is considered. A well-structured plan will ensure that maximum tax benefits are achieved while balancing the needs of the founders and their family.

7. Timing

Foundations may be set up during life, or at death by will (through a testamentary trust). Foundations established during life can be set-up as a shell, and then funded as assets become available. There are planning advantages to an unfunded foundation, however, they do not come without responsibilities. Even if there are no funds in the foundation, annual filings must be made to CRA.

8. Supporting Diverse Beneficiaries

One advantage of a foundation is philanthropic flexibility and the retention of control over charitable decisions. There is no need to commit to supporting certain charities when the foundation is established. There are no restrictions about the types of charitable causes that can be supported, and no loss of control over the decision making process once a donation is made to the foundation. This flexibility is perhaps the greatest benefit of a private foundation because it enables the foundation to meet the emerging needs of society and the family.

Establishing a foundation during life ensures the founder has the time – and can enjoy the pleasure – of charitable giving. It is possible to put a personal stamp and vision on the foundation, which will be of immeasurable benefit to successor directors/trustee.

9. Cost-Effective & Accountable

A challenge of charitable giving is ensuring donations go to the intended purpose and are not wasted on administration or fundraising costs. The trustees or directors of a private foundation can monitor if donations are being used as intended. If a charity does not meet expectations, the foundation has no obligations to support it again. This level of control is not present with an outright gift to a public charity.

A private foundation is also an efficient way to give. A private foundation with Scotiatrust as trustee with assets of more than \$1 million would have total annual costs of approximately 1.5% annually. The greater the capital base the lower the fees, with fees of

less than 1.0% being typical with Foundations of \$5 million or more supported by Scotia Private Client Group and its partners.

Endowments within public charities typically have annual fees of 1.5% or more. Donor advised funds offered by some financial institutions have fees of up to 2.5% per annum. Many professionally-staffed public charities have total fundraising and administrative costs in excess of 20% of revenue. Often these costs are covered by unrestricted annual donations and bequests by will. A number of public charities use unrestricted bequests to pay for all fundraising and administrative costs of the charity, which is typically not the donor's intention.

10. Minimum Amount

There is no legal minimum required to establish a private foundation, but there are practical minimums based on operating costs. In our experience, the practical minimum with external professional administrative and granting support is \$500,000 in capital for a simple trust-based foundation, and \$1 million for an incorporated foundation. In most situations, we recommend a minimum of \$1 million in capital if the goal is long-term giving. The greater the asset base the more the foundation can accomplish.

It is possible to operate a private foundation on a flow-through basis to organize giving, which means "no money down". Flow-through foundations are normally founded by entrepreneurs and operate out of the private business.

Foundations can also be funded with capital installments over a number of years. The key is establishing a funding plan, within the context of an overall estate plan, to commit to a minimum of \$1 million over time to ensure long-term viability. Most of the foundations that we advise on are funded through a combination of lifetime and estate gifts.

The Scotia Private Client Group Advantage

1. "Instant Office" Services

Scotiastrust offers administrative services to private foundations on a fee-for-service basis. These services are available based on the requirements of the client. These services range from basic record keeping and board support to full-scale granting programs. Each foundation has different needs, and we customize services to fit the situation. Scotiastrust offers a basic "Instant Office" package for \$6,000 per annum that covers a full range of services. Pricing is based on the activity of the foundation and the services provided, not the asset base. Hence, the more ambitious the mission of the foundation, the greater the work involved and the cost. We would be pleased to discuss a service package that meets the needs of your foundation.

Sample Instant Office services:

| Management | Granting |
|---|--|
| <ul style="list-style-type: none"> • Dedicated Foundation Officer • Office Address & Facilities • Record Keeping • Custody of Funds • Annual Government Filings • Disbursement Quota Management • Donation Receipts and Letters • Corporate/Trust Record Keeping • Correspondence/Expenses • Cash Management Services | <ul style="list-style-type: none"> • Grant Policy/Cycle Development • Prescreening Applicants • Assessment of Applications for Trustees • Meeting Support (Agenda, Minutes) • Granting Software/Record Keeping • Grant Letters & Cheques • Support of Strategic Granting • Management of Charity Relationships • Charity Site Visits • Partnerships with other funders |

2. Privacy/Name of Foundation

Individuals and families establishing private foundations should think about the degree of privacy they desire in relation to the Foundation. Private foundations exist in the public domain. The annual charity returns are available online at the Canada Revenue Agency website. Hence, it is important to make decisions about how much information is publicly available to minimize public attention and intrusive, unsolicited charity solicitations.

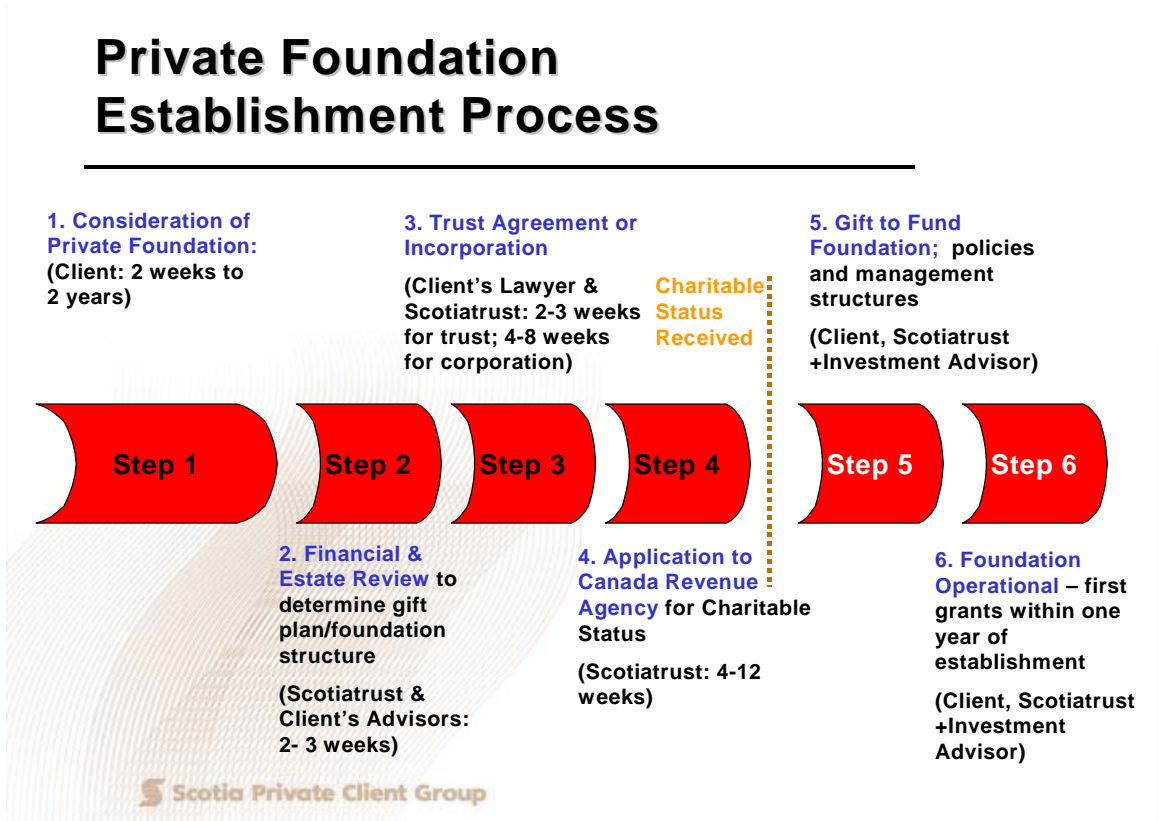
Scotiastrust has extensive experience in protecting the privacy of its foundation clients. This process starts with choosing the name and legal form of the foundation and extends to format of financial records. We have also had extensive experience in ensuring recognition from charitable beneficiaries is appropriate. With Scotiastrust providing administrative services (our Instant Office), all unsolicited inquiries go through the assigned foundation/trust officer. Private information, such as home address, is kept strictly confidential.

3. Personal Legacy

Private foundations are personal philanthropic legacies. They represent the founder’s values, life experience and belief. At Scotiastrust, we take the legacy aspects of foundations very seriously. We interview the founder to create a biography to accompany the foundation documents. This document is both a statement of personal legacy, but also a statement of purpose for the Foundation captured in everyday language. We also ask for photographs to accompany the biography. These documents provide a human record of the donor’s life and intentions, which is of enormous value to future recipients of grants and Scotiastrust as administrator or successor trustee.

4. Establishment

The establishment of a foundation is a multi-step process that involves a team of advisors. While that team can be limited to Scotiatrust and an external lawyer when the foundation is established by Will, the process during life involves more parties to ensure the family’s needs are considered and balanced. The following flow-chart outlines the typical establishment process.



5. Investment Management

Since our foundation services are offered on a debundled basis, clients may choose to retain their own investment advisor to manage the foundation’s endowment. This option is available to ScotiaMcLeod clients, as well as clients who use counsel outside the Scotiabank family. Within the Scotia Private Client Group, investment services are available from Scotia Cassels Investment Counsel, our discretionary investment manager. Scotia Cassels serves 301 foundations with \$686 million in assets.

6. Cost

The cost of establishing a foundation during life is typically under \$5,000 for legal and consulting work. If the client’s situation is very complex the fees for external advisors may be more, but this is exceptional and usually due to other tax planning needs. All fees are paid by the foundation, after registration, using after-tax dollars. This reduces the cost by approximately 40% to 45%.

Scotiastrust offers consulting assistance with the setup of foundation. These services are designed to ensure quality control and thoroughness. They include registration of the foundation, writing the biography of the founder, reviewing all legal documents, assisting with granting policy and mission identification, and keeping the process on schedule.

Since establishing a trust foundation is specialized legal work, we would be pleased to recommend a lawyer experienced with private foundations. If the client prefers, we can work with existing legal counsel to ensure the founding documents are sound.

For more information, please contact:

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