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Corporate donations

Corporate Donations: Another way to give

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What is charitable giving?

Charitable giving provides an opportunity for Canadians to transfer assets to registered charities and support the causes that matter most to them. Incorporated business owners may wonder if they should make charitable donations personally or through their business. This paper will explain the advantages of donating through a corporation versus personal donations.

Tax deductions on corporate donations

When donating through a corporation, the company is entitled to a tax deduction for the donated amount, equal to its fair market value. By reducing taxable income, the corporation can reduce its tax liability. Corporations are limited to a charitable deduction of up to 75% of net income in a year and may carry over excess donations for a period of five years. The value of the tax savings is dependent on whether the charitable deduction is used to reduce income subject to the small business tax rate, the general corporate tax rate, or corporate investment tax rate. In Quebec the charitable deduction is a maximum of 100% of net income in a year. The carry over is the same 5 years.

The example below compares the donation made by the corporation versus paying a salary to the shareholder in order to make the donation personally. For illustrative purposes, the corporation and shareholder are resident in Ontario. Corporate donation is used to reduce income subject to the small business tax rate and shareholder is in the top personal tax bracket. Donations are in excess of $200. 2021 tax rates apply.

Corporate vs. Personal donation (funded by salary)

		Donating through a corporation	Donating personally
Business	Business Income	$100	$100
	Less: Char Don (1) / Salary (2)	($100)	($100)
	Net Business Income	$0	$0
	Corporate Tax (12.2%)	$0	$0
	Net After-tax Cash Flow (Corp)	$0	$0
	Non-Eligible Dividend Paid to S/H	$0	$0
Personal	Salary	$0	$100
	Dividends	$0	
	Personal Tax	$0	($54)
	Charitable Donation	$0	($100)
	Donation Tax Credit	$0	$50
	Overall Savings	**0.00**	**-3.12**
	Net Corporate Donation Benefit	**3.12**	
Assumptions	Active Business Income	$100	
	Desired Charitable Donation	$100	
	Marginal Tax Rate (Salary)	53.53%	
	Small Business Tax Rate	12.20%	
	Donation Tax Credit	50.41%	

- As the table highlights, a $100 donation made by a corporation is slightly more advantageous than paying salary and making a donation personally, under these assumptions.
- Another option is to pay a dividend, instead of salary or bonus to fund the personal charitable donation. Because of integration, the results are similar to the salary option. That is, a slight advantage is still available to a corporate versus a personal donation.

Additional benefit of the capital dividend account (CDA)

- However, if there's a surplus of assets in the corporation that can be withdrawn, as well as securities that have unrealized capital gains, the overall tax benefits can be increased by making a donation of the security in-kind from the corporation.
- As with personal donations, when the security is liquidated by the charity, the capital gain is eliminated for the corporation. Therefore, 100% of the capital gain is credited to the corporation's capital dividend account (CDA).
- The CDA can distribute tax free capital dividends to shareholders.

The example below illustrates the value of choosing to donate $50,000 worth of securities in mutual funds through the corporation instead of liquidating the assets and donating $50,000 in cash. It is assumed the corporate donation deduction is used to offset passive income at a 50% tax rate.

	Sell securities and donate cash	Donate securities directly through corporation
Fair market value of donation (X)	$50,000	$50,000
Adjusted cost base	$10,000	$10,000
Capital gain	$40,000	$40,000
Taxable capital gain	$20,000	$0
Tax on capital gain @50% (Y)	$10,000	$0
Value of tax deduction @50% (Z)	$25,000	$25,000
Amount added to the capital dividend account	$20,000	$40,000
Total cost of donation (X+Y-Z)	**$35,000**	**$25,000**

- To calculate the total cost of the donation, we take the fair market value of $50,000, add the tax to the capital gain ($10,000) and then subtract the value of the tax deduction from the donation ($25,000). Note: an adjustment must be made to factor in each province or territory's tax rate. **Total Cost of Donation = X + Y – Z**

Active business versus investment holding company

An in-kind donation can be made from either an active business or an investment holding company, with the same benefits. It may make sense to consider an in-kind donation from the holding company because taxation of investment ("passive") income is much higher than the tax on active business income. The 75% limit on the deduction from income and the five-year carry-forward apply to both.

Summary

Charitable donations can be made either by individuals, corporations or investment holding companies. The best decision as to which to choose varies from situation to situation. Donors should discuss the best option for their unique circumstances with their financial advisor.