



Top Fallacies about Private Foundations in Canada in 2019 ¹

By Mark Blumberg, Lynn Gluckman and Taylor Teasdale (January 13, 2019)

When a Canadian registered charity is established, it can be set up as a

- (i) charitable organization,
- (ii) public foundation or
- (iii) private foundation,

depending upon its structure, source of funding and operation. There are approximately 5,800 private foundations in Canada. Private foundations have been growing at a higher rate than any other type of Canadian registered charity. Although there are some differences between a private foundation in comparison to charitable organizations and public foundations, over the last two decades those differences have diminished.

That being said, it is quite common in our practice to hear that there is confusion and misunderstanding relating to the operation of a private foundation and the rules that govern it.

Here is a list of some of the top fallacies we see about Canadian private foundations:

Myth #1 - You need to donate millions of dollars to set up a private foundation (i.e. private foundations are for rich people only).

Not really. There has been a lot of media focus on the private foundations of wealthy philanthropists such as Bill Gates and Li Ka-Shing or large for-profit companies such as Mastercard or Walmart. However, most private foundations

¹ This article is adopted from an article entitled *Top Fallacies about Private Foundations in Canada* by Mark Blumberg, Kate Robertson and Lynn Gluckman (April 11, 2016)

are set up by individuals, families or corporations with far less wealth or prominence. Some are used as an incorporated vehicle to conduct their philanthropic work and funds are only contributed when needed. One example of a private foundation we established was for a family interested in conducting educational activities in Haiti. The incorporated private foundation provided limited liability protection and also a vehicle for the family to organize their philanthropic activities. However, total contributions of the family (and other donors) to the charity was only in the range of \$30,000 per year and no long-term funds were contributed to the foundation.

Myth #2 - Private foundations are expensive and complicated to establish and operate.

The cost of establishing a private foundation largely depends on how complicated the structure will be and who sets it up. For example, the private foundation could be set up simply to make grants to other Canadian registered charities, or it could be set up to also conduct its own charitable activities. A simple private foundation can be established for as little as \$5,000 - \$6,000 and may only take 4-6 months to create. If there are foreign activities involved or other more complicated charitable activities, it can be more costly. The actual operation of a private foundation is not any more complicated than that of a charitable organization and is, in fact, often much simpler to run when it is set up to only provide gifts to other registered charities/qualified donees.

Myth #3 - Private foundations are set up to give money to other charities and cannot carry on their own activities.

What a private foundation can and cannot do is dictated by its legal objects and the *Income Tax Act* (Canada). If a private foundation has legal objects that only allow it to make gifts to registered charities, then it is prohibited from conducting its own charitable activities. However, if the legal objects are broader, then the private foundation has more flexibility to conduct its own activities. Whereas a charitable organization should spend more than 50% of its disbursements on its own charitable activities each year and a public foundation should spend more than 50% of its disbursements on gifts to other registered charities, a private foundation can, for example, spend 90% of its disbursements on gifts to charities in one year and spend 90% on its own charitable activities the next year, if its objects are broad enough to allow for that.

Myth #4 - Private foundations cannot conduct foreign activities.

Canadian registered charities are allowed to conduct their activities both inside and outside of Canada. However, as mentioned above, private foundations can only conduct activities that fit within their legal objects. If a private foundation has narrow objects such as to only fund qualified donees, then it can only fund qualified donees. In general, the qualified donees are registered charities in Canada. Almost no foreign charities are qualified donees. One exception is that there are about 600 prescribed foreign universities that are qualified donees. At least when it comes to certain prescribed universities outside of Canada it can be exceptionally easy for private foundations to fund those universities. If a private foundation has broad objects that are not limited to a specific jurisdiction such as Canada, they should have the flexibility to be able to conduct foreign activities within the parameters set by the CRA. You might find this article on [Canadian charities conducting International Activities helpful](#). Also if your objects are not broad enough consult your legal counsel on approaching CRA to [expand your legal objects](#).

Myth #5 - A private foundation can only receive donations from the family establishing the private foundation.

While many private foundations are supported by a single donor or family, private foundations can generally receive donations from the general public and issue charitable donation receipts for these donations in the same way as other registered charities. There are, however, a small number of private foundations that preclude themselves from accepting outside funds in their constating documents or through operational policy. This approach obviously limits fundraising opportunities and can be generally changed by amending the constating documents or policy if the foundation decides later to receive outside donations.

Myth #6 - Private foundations cannot fundraise.

Generally, a private foundation can conduct its fundraising in the same way as other registered charities. CRA has a “Fundraising by registered charities” guidance that applies to all registered charities, regardless of their designation. While some private foundations don’t need to or don’t want to fundraise many others do fundraise.

Myth #7 - Private foundations can pay for children's wedding expenses or for gala fundraising tickets for their directors.

This is not acceptable. Private foundations must be very careful to avoid providing any undue private benefits or using their funds for non-charitable expenditures or creating even the perception that they are applying their resources for improper purposes.

Myth #8 - Private foundations can carry on business activities.

One significant difference between private foundations and other registered charities is that private foundations are prohibited from conducting any business activities. In contrast, public foundations and charitable organizations can carry on related business activities as set out in CRA Guidance, but private foundations cannot conduct any business activities. There is only one narrow exception in that private foundations are now able to invest in limited partnerships which is considered a business activity but a change to the Income Tax Act allows for it. To the extent a private foundation would like to carry on a business activity, the foundation can change its structure (sometimes not difficult to do at all) to be re-designated as a charitable organization or public foundation, or another charity, for profit or non-profit that is not a charity could be established to carry on the business activity. Existing foundations should occasionally review their structures to ensure that they have enough flexibility to achieve their goals.

Myth #9 - All board members of a private foundation must be family members.

The board of directors of a private foundation can be structured in several different ways. Some boards may be composed of a majority of or all individuals from the same family. Some boards may be composed of individuals related by close business ties. These people are considered "non-arm's length" from each other. On the other hand, some private foundations have arm's length board members where no one is related by family or close business ties. If most of the people on the board of a registered charity are non-arm's length from one another (i.e. related), then the organization must be a private foundation. However, a private foundation is not required to have most of its board at arm's length.

Myth #10 - Private foundations cannot conduct political activities.

All Canadian registered charities, regardless of their designation, have the ability to engage in non-partisan political activities that are related to their objects as long as they comply with CRA guidance and other legal requirements for political activities. If a private foundation wants to have great impact, it should carefully consider possible involvement in non-partisan political activities. There were significant changes in late 2018 to the *Income Tax Act* (Canada) that allow registered charities, including private foundations, to conduct unlimited public policy dialogue and development activities (PPADA) connected to the legal purpose of the charity as long as they are not directly or indirectly partisan.

Myth #11 - Private foundations are 'private'.

CRA requires that all Canadian registered charities complete a Form T3010 – Registered Charity Information Return on an annual basis. Most information contained in the T3010 and its schedules (which includes financial information of the charity, information on the directors, information on all grants made by the private foundation, etc.) is publicly available on the CRA's web site. Private foundations are not excluded from this transparency requirement. If you really want privacy and anonymity there are other better options than private foundations such as working directly with a charitable organization or public foundation or establishing a donor advised funds at a community foundation or commercial donor advised fund charity.

Myth #12 - When a private foundation makes a gift to a registered charity it should receive an official donation receipt.

This is incorrect. When a Canadian registered charity (irrespective of its designation) provides funds to another Canadian registered charity or other qualified donee it should not be issued an official donation receipt because the donor, being exempt from income tax, does not need the receipt. A private foundation should ensure that, when making a gift to a charity, the charity is currently registered with the Canada Revenue Agency and the private foundation should note the BN number and the amount of the donation so that it can accurately complete its T3010 filing. It is inappropriate for a private foundation to request an official donation receipt and it is inappropriate for another Canadian registered charity to provide a private foundation with such a receipt. A charity can provide an acknowledgement or business receipt to the private foundation if it so desires or the private foundation requests it. Additional helpful information about receipting can be found in [Blumbergs' Receipting Kit](#).

Myth #13 - Once a private foundation is established and approved by the Canada Revenue Agency it cannot change its objects or methods of operation.

This is a common myth. Private foundations, just like other registered charities, typically can make changes to both their objects and methods of operation. If your private foundation is going to change its objects it will require CRA pre-approval for such a change. It is a good idea to speak to a charity lawyer familiar with CRA requirements to assist you with this process. The process can take between 6 – 12 months depending upon the CRA backlog and the jurisdiction in which the foundation is established. CRA delays in reviewing object changes may get worse and you might find this [article on changing objects](#) helpful.

Myth #14 - A private foundation is named after the main donor.

Private foundations, just like other charities, can use any name as long as it is not confusing and does not violate certain prescribed rules. While some private foundations have family names attached to them, it's common for a private foundation to use a name that focuses on its mission.

Myth #15 - A donation to a private foundation must be endowed.

Definitely not. Before 2010, if a donor contributed, for example \$100,000, to a private foundation and received an official donation receipt for the contribution, the foundation was required to spend \$80,000 the following year on charitable activities or gifts to qualified donees. This was referred to as the “80/20 rule”. If you wanted to avoid such a result, you would make a “10-year gift” to the foundation which meant that the capital needed to be endowed for at least 10 years with generally only the income being spent each year. Some 10-year gifts were only restricted for 10 years and others were perpetual endowments. In 2010, the *Income Tax Act* (Canada) was amended to remove the 80/20 rule. Consequently, there is now no reason when contributing to a private foundation to use 10-year gifts or to endow capital in the foundation even if you want to keep the funds in the foundation for the long term. Some foundations may wish their boards to self restrict funds, but creating a perpetual endowment can often undermine the value, flexibility and impact of the charitable funds in a private foundation.

Obtaining charitable status as a private foundation is a privilege that comes with many obligations and responsibilities. It is important that private foundations understand their regulatory obligations and comply with the rules. An important part of understanding the regulatory system is being aware of these fallacies, which can, in some cases, significantly impede a private foundation's activities and effectiveness.

If you are planning on establishing a private foundation, it is best to obtain appropriate legal and practical advice before you donate large amounts of money in a way that could significantly hinder the effectiveness of your philanthropic work. The same argument can be made when it comes to depositing large amounts of money in a donor advised fund. We have seen many donors provide large contributions to donor advised funds without fully understanding all the funds' terms and conditions, and then a few years later become extremely disappointed that they cannot do what they now want to do. Private foundations are not appropriate for everyone and it is best to establish them only if you really understand how they operate and can be used.

For those who want to have a great degree of control over their philanthropic funds and strategy, private foundations provide a useful vehicle. For Canadians who don't have children or who have more wealth than they wish to provide for their children, private foundations may be a useful tool for dividing your wealth between family and public causes that you care about. There are certainly very generous tax incentives for donating to a private foundation; however, those tax incentives can be achieved through other mechanisms and a private foundation is certainly not the best approach for many philanthropists. If you are going to establish a private foundation, make sure you obtain appropriate advice from counsel who is knowledgeable in this area.

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