



Top Fallacies about Canadian Private Foundations in Canada in 2022¹

By Mark Blumberg, Lynn Gluckman and Uma Karthigeyan (January 24, 2022)

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 operations.

There are approximately 6,300 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.

Most of the confusion relating to the compliance requirements and the regulation of private foundations is a lack of knowledge or out-of-date information and not attempts at deliberate malfeasance. Our firm works with many private foundations to assist them to understand the regulatory framework and also the flexibilities that are available in the operations of private foundations.

Here is a list of some of the top fallacies we see about Canadian 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) and *Top Fallacies about Private Foundations in 2019* by Mark Blumberg, Lynn Gluckman and Taylor Teasdale

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, Warren Buffet, and Li Ka-Shing or large for-profit companies such as Mastercard or Walmart. However, most private foundations 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 as a simple foundation that simply makes grants to other Canadian registered charities, or it could be set up to conduct its own charitable activities, while also making grants to other Canadian registered charities. A simple private foundation can be established for as little as \$5,000 - \$6,000 and may only take 3-4 months to create. If the private foundation conducts its own charitable activities and if those activities are complicated or if foreign activities are involved, it can be more costly and time-consuming.

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 as a simple foundation, to only provide gifts to other registered charities/qualified donees. That being said, despite the 'simplicity' of running many private foundations, the degree of non-compliance in private foundations is high. This is largely because those who are responsible for running private foundations, (although they may be very successful and talented), often are very busy, don't understand the regulatory framework and its requirements and don't treat their charitable endeavors with the same serious mindset that they treat other matters in their lives.

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 largely 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 (as a simple foundation), then it is prohibited from conducting its own charitable activities. However, if the legal objects are broader and worded in a manner to enable a private foundation to conduct its own charitable activities and programs, then the private foundation has more flexibility.

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. We assist many private foundations with expanding their legal objects to allow for greater flexibility in terms of grantmaking and activities.

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. The largest group of qualified donees in Canada is registered charities followed by Canadian municipalities. There are very few foreign charities that are qualified donees and they are mostly about 600 foreign universities that are registered with CRA.

If a private foundation has objects that are not limited to a specific jurisdiction such as Canada and that allow for their own charitable activities, 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, you should consult your legal counsel on approaching CRA to [expand your legal objects](#). You should also be aware of CRA's helpful guidance dealing with foreign activities and we have [a directory of resources on Canadian charities carrying out international activities](#).

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 fundraise and 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. Some organizations may wish to avoid receiving external funds, to avoid becoming a soliciting corporation or to have great external accountability. This approach obviously limits fundraising opportunities. It is however a choice and can be generally changed by amending the constating documents or policy if the foundation decides later to receive outside donations.

A properly established private foundation should be able to carry out the same fundraising activities as charitable organizations and public foundations.

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 and prohibited by CRA, as an undue private benefit.

This rule applies to all private foundations, all charitable organizations and all public foundations. Private foundations must be very careful to avoid providing any undue private benefits or using their funds for inappropriate 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's guidance, but private foundations cannot conduct any business activities. There is only one narrow exception in that private foundations are able to invest in limited partnerships, which is still considered a business activity, but a change to the Income Tax Act now 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. Alternatively, 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 directors 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 to each other), 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. With the increasing scrutiny of private foundations, some have brought in ‘independent’ arm's length board members to increase the skill set and diversity of the board. Diverse boards of charities' tend to make fewer big mistakes.

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 stated purposes, 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 the 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 (PPDDAs) connected to the stated purposes of the charity, as long as they do not support or oppose any political party or candidate for public office. If the private foundation has objects that only allow gifts to registered charities or qualified donees, then it is CRA's view that they generally cannot conduct their own PPDDAs. As we have discussed above such foundations can go back to CRA and can broaden their objects.

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 and information on all grants made by the private foundation, etc.) is publicly available on 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 with and donating directly to charitable organizations or public foundations or establishing a donor advised funds at a community foundation or a commercial donor advised fund charity. If you are not familiar with donor advised funds you might find our [course on DAFs](#) helpful.

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](#) and our course on [receipting](#).

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 generally 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 4- 6 months depending

upon the complexity of the objects and activities, but CRA has been processing these requests at record speeds. You might find our [article on changing charitable 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.

Myth #16 – Private foundations take a long time to set up.

While there have been delays over the last few decades at the CRA when it comes to all types of charity applications, at the moment CRA is processing charity application far more quickly than over the last decade. In some cases, private foundations have been established in less than 3 months although we typically advise they will take between 4-6 months. A private foundation that is only making grants to other registered charities or qualified donees is typically far quicker to establish than a charity conducting its own charitable activities.

Myth #17 – The directors of the private foundation control the foundation

For incorporated foundations it is actually the members who have the ultimate control over the foundation, because they elect the directors and can make major changes, such as to the governing documents. While the directors of a private foundation have an important role, they can be replaced if the membership decides to have a different group. So, the real control of a private foundation is typically in the hands of the members and not the board.

Myth #18 – A private foundation can be tightly integrated with a family or for-profit corporation and it is like having another bank account

A private foundation needs to be [separate](#) from non-qualified donees such as individuals, NPOs or for-profit corporations.

The private foundation should be separately established. Typically, with new foundations it is incorporated under the *Canada Not-for-profit Corporations Act* (“CNCA”). The private foundation should have its own books and records, a separate bank account and everything must be kept sufficiently separate from any non-qualified donees. If there is any confusion between the private foundation and the non-qualified donees such as for-profit entities or non-profits, then CRA can revoke the charitable status of the private foundation. CRA has recently revoked a number of charities for not being sufficiently separate from non-qualified donees.

Myth #19 – When we give funds to a registered charity, our private foundation needs to have an elaborate application process and lengthy grant agreements.

Many private foundations have put into practice a set processes, sometimes over decades and based on their experience and knowledge. Sometimes their processes can be cumbersome, burdensome, unnecessarily complicated and based on an incorrect understanding of their legal obligations. This results in wasted resources of the private foundation and also wasted resources on the part of grantees and prospective grantees. If you total up time spent by these grantees and prospective grantees, with some private foundations, it may be more than the amount actually granted. Obviously, this is not how the system is supposed to work.

Sometimes the objects of a private foundation are inadequate for their needs, but if the private foundation has an ability to make gifts to registered charities or qualified donees, then there usually are simple and straightforward ways to make grants. There is a movement entitled “trust-based philanthropy” which has a lot of important suggestions for how funders can more efficiently and effectively fund registered charities. We work with many private foundations on training and systems to improve grantmaking and to focus on the private foundation’s real compliance.

Myth #20 – A donor advised fund and a private foundation are the same.

Both a donor advised fund (DAF) and a private foundation can issue an official donation receipt. That is where the similarities generally end.

With a private foundation, you can control the organization but that is not typically the case with the DAF. With a private foundation you can determine within the legal limits of a charity how to invest the funds, but DAFs often provide very limited opportunities to invest funds. With a private foundation your board can determine where funds will go, but with a DAF you can only recommend that the funds go to another registered charity or qualified donee. With a private foundation you are in control of your costs, with a DAF, the DAF decides on the fees you will be paying them.

There are many advantages to having a private foundation or a DAF, but they are certainly not the same thing. They also are not mutually exclusive in that a person can have both a private foundation and a DAF and many of our larger clients do. Also, as time moves on the private foundation or DAF may no longer suite your needs and we have worked with private foundations that wish to wind down to a DAF and also DAF funds that are granted out to a newly established private foundation.

Myth #21 – Our private foundation is set up as a trust and there is nothing we can do about that.

In the past, although far less today, some private foundations were established as trusts, rather than incorporated entities. While this may not in some circumstances be a problem in other cases it can result in personal liability for the trustees. We have assisted a number of private foundations, with CRA approval, to move from being established as trusts to being incorporated entities. You will then be able to maintain your registered charity status but also obtain the limited liability protection of an incorporated non-profit corporation.

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 with the funds. 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.

Those who are considering establishing a private foundation may find this [course](#) to be helpful. For corporations wish to establish a corporate foundation this [course](#) may be more appropriate.

For those running existing private foundations we have a full day [course on foundation compliance requirements](#).

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. More importantly if you have a private foundation that you are responsible for, make sure that it is compliant with its legal requirements.

Mark Blumberg, Lynn Gluckman and Uma Karthigeyan are lawyers at Blumberg Segal LLP in Toronto, Canada. To find out more about legal services that Blumbergs provides to Canadian charities and non-profits please visit www.CanadianCharityLaw.ca, www.SmartGiving.ca, or www.CharityData.ca, email us or call us at 416-361-1982.

This article is for information purposes only. It is not intended to be legal advice. You should not act or abstain from acting based upon such information without first consulting a legal professional.