



Wealth
Management

the Navigator

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC FAMILY OFFICE SERVICES

Aaron Fennell, MBA, CFA
Portfolio Manager & Investment
Advisor
Tel: 416-313-6397
aaron.fennell@rbc.com

RBC Dominion Securities
181 Bay Street, Suite 2350
Toronto, ON M5J 2T3
www.aaronwfennell.com

Donating flow-through investments

To encourage charitable giving, the government provides you with a tax credit when you make a donation to a registered charity. This donation tax credit can be used to reduce your taxes payable. In some cases, you may receive a further benefit if you donate flow-through investments. This article discusses the tax implications of donating flow-through investments in-kind from your personal non-registered account.

Tax benefits of donating flow-through investments

When you purchase a flow-through investment and subsequently donate the investment in-kind, you may benefit from the following:

- Deduction of exploration and development expenses flowed through to you against your taxable income;
- Applicable federal mineral exploration tax credit (METC), critical mineral exploration tax credit (CMETC), and applicable provincial/territorial flow-through share tax credits that reduce your taxes payable;
- Donation tax receipt for the fair market value (FMV) of the donated flow-through investment; and
- A portion of the capital gain realized on the donation of the investment may be eliminated.

Capital gains on donating flow-through investments

Generally, when you gift property, the property is deemed to have been

disposed of at FMV. As such, you may realize taxable capital gains if you donate property that has an adjusted cost base (ACB) that is lower than its FMV. If you donate the publicly traded securities in-kind, the capital gains realized may be eliminated.

The elimination of capital gains works differently for flow-through investments. Because the ACB of a flow-through investment is typically zero or close to zero, there would be a significant benefit if the capital gain could be eliminated on the donation of a flow-through investment.

In 2011, the federal government introduced rules to limit what they saw as excessive tax benefits. Under these rules, you may realize a deemed capital gain when you donate flow-through investments. The deemed capital gain is equal to the actual capital gain realized on the donation or your "exemption threshold," whichever is less. In very simplified terms, your exemption threshold is equal to the original cost of all flow-through shares



of the same class, less any cumulative capital gains realized on the disposition of flow-through shares in the same class. This essentially means the exemption from capital gains tax will be available only to the extent that the actual capital gain on the donation of flow-through investments is in excess of your original cost amount.

Please note if you are a resident of Quebec, you may still be able to eliminate the entire capital gain when all the conditions are met for provincial tax purposes.

Grandfathering for certain flow-through investments

The deemed capital gains rules do not apply to flow-through common shares acquired before March 22, 2011, or shares of a mutual fund corporation that are received in exchange for flow-through limited partnership (LP) units acquired before August 16, 2011 (no contributions to the partnership can be made on or after August 16, 2011).

Generally, only the original cost of flow-through shares acquired on or after March 22, 2011, and flow-through LP units acquired on or after August 16, 2011, will be added to your exemption threshold. For example, if you only owned flow-through common shares purchased prior to March 22, 2011, your exemption threshold will remain at zero and you can donate the shares and benefit from the old rules (i.e. you will still be able to exclude your entire capital gain realized at the time of donation). Likewise, if you acquired flow-through LP units before August 16, 2011, once they are exchanged for shares of a mutual fund corporation, you can donate them and still benefit from the old rules.

Generally, only the original cost of flow-through shares acquired on or after March 22, 2011, and flow-through LP units acquired on or after August 16, 2011, will be added to your exemption threshold.

Example – Tax impact of donating a flow-through investment

Here's an example to illustrate the impact of the deemed capital gains rules. Say you purchased 500 flow-through shares of XYZ Co. for an original cost of \$50,000 and later donated all 500 shares of XYZ Co. when they're worth \$45,000. Under the grandfathering rules, the taxable capital gain would be zero.

Under the deemed capital gains rules, the exemption threshold is calculated as the original cost of \$50,000.

The deemed capital gain is calculated as the lesser of:

- The actual capital gain on the donation (\$45,000); and
- The exemption threshold (\$50,000).

As a result, you realize a deemed capital gain of \$45,000 on the donation.

The following table illustrates the tax implications of selling the XYZ Co. shares and donating the proceeds versus donating the shares in-kind. In this example, we are assuming the capital gains realized are subject to the 50% inclusion rate.

	Sell and donate proceeds	Donate in-kind (grandfathering rules)	Donate in-kind (deemed capital gains rules)
Initial cost of investment (a)	\$50,000	\$50,000	\$50,000
Deductions claimed	\$(50,000)	\$(50,000)	\$(50,000)
Tax savings from the deduction at 48%* (b)	\$24,000	\$24,000	\$24,000
FMV of donation	\$45,000	\$45,000	\$45,000
ACB	\$0	\$0	\$0
Capital gain/deemed capital gain	\$45,000	\$45,000	\$45,000
Taxable capital gain	\$22,500	\$0	\$22,500
Tax on taxable capital gain at 48% (c)	\$10,800	\$0	\$10,800
Tax savings from donation tax credit (d) (\$45,000 at 48%)*	\$21,600	\$21,600	\$21,600
Total cost of donation = (a) – (b) + (c) – (d)	\$15,200	\$4,400	\$15,200

This illustration doesn't take into account the lower donation tax credit rate on the first \$200 of donations. It also doesn't factor in the various investment tax credits that may be available when investing in a flow-through investment.

*The above illustration uses a marginal tax rate and a donation tax credit rate of 48%.

Alternative minimum tax (AMT)

If you're purchasing and donating a flow-through investment to reduce your tax liability, it's very important to consider AMT. This tax aims to ensure that every Canadian individual pays a minimum amount of tax. The calculation of AMT is based on an adjusted taxable income, which seeks to remove the advantages of certain tax-preferential items such as deductions from flow-through investments. In addition, starting in 2024, you can only deduct 80% of the donation tax credit to reduce AMT. If any capital gains you realize on the donation of the flow-through investment is exempt under the regular tax calculation, you will need to include 30% of the exempt capital gains as income for AMT purposes. If the AMT calculated is greater than your regular tax liability, the AMT becomes your tax liability for the year. The difference between the AMT you have to pay in a year and your regular tax liability can be carried forward for seven years to reduce your future regular income tax liability when your taxes payable exceed your AMT. For more information about charitable giving and AMT, ask your RBC advisor for an article on this topic.

Be sure to speak with a qualified tax advisor to help you determine how AMT will affect you if you're thinking of donating flow-through investments.

Conclusion

Making charitable donations provides you with a chance to give back to your community and receive tax incentives at the same time. When you donate a flow-through investment, in addition to getting a donation tax receipt for the FMV of the investment, some of the accrued capital gain on the investment may also be eliminated. Speak with a qualified tax advisor to determine whether it may make sense for you to donate flow-through investments in-kind.

This article may contain strategies, not all of which will apply to your particular financial circumstances. The information in this article is not intended to provide legal, tax or insurance advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified tax, legal and/or insurance advisor before acting on any of the information in this article.



Wealth
Management

This document has been prepared for use by the RBC Wealth Management member companies, RBC Dominion Securities Inc. (RBC DS)*, RBC Phillips, Hager & North Investment Counsel Inc. (RBC PH&N IC), RBC Wealth Management Financial Services Inc. (RBC WMFS), Royal Trust Corporation of Canada and The Royal Trust Company (collectively, the "Companies") and their affiliates, RBC Direct Investing Inc. (RBC DI)* and Royal Mutual Funds Inc. (RMFI). *Member – Canadian Investor Protection Fund. Each of the Companies, their affiliates and the Royal Bank of Canada are separate corporate entities which are affiliated. "RBC advisor" refers to Private Bankers who are employees of Royal Bank of Canada and mutual fund representatives of RMFI, Investment Counsellors who are employees of RBC PH&N IC, Senior Trust Advisors and Trust Officers who are employees of The Royal Trust Company or Royal Trust Corporation of Canada, or Investment Advisors who are employees of RBC DS. In Quebec, financial planning services are provided by RMFI or RBC WMFS and each is licensed as a financial services firm in that province. In the rest of Canada, financial planning services are available through RMFI or RBC DS. Estate and trust services are provided by Royal Trust Corporation of Canada and The Royal Trust Company. If specific products or services are not offered by one of the Companies, RBC DI or RMFI, clients may request a referral to another RBC partner. Insurance products are offered through RBC Wealth Management Financial Services Inc., a subsidiary of RBC Dominion Securities Inc. When providing life insurance products in all provinces except Quebec, Investment Advisors are acting as Insurance Representatives of RBC Wealth Management Financial Services Inc. In Quebec, Investment Advisors are acting as Financial Security Advisors of RBC Wealth Management Financial Services Inc. RBC Wealth Management Financial Services Inc. is licensed as a financial services firm in the province of Quebec. The strategies, advice and technical content in this publication are provided for the general guidance and benefit of our clients, based on information believed to be accurate and complete, but we cannot guarantee its accuracy or completeness. This publication is not intended as nor does it constitute tax or legal advice. Readers should consult a qualified legal, tax or other professional advisor when planning to implement a strategy. This will ensure that their individual circumstances have been considered properly and that action is taken on the latest available information. Interest rates, market conditions, tax rules, and other investment factors are subject to change. This information is not investment advice and should only be used in conjunction with a discussion with your RBC advisor. None of the Companies, RMFI, RBC WMFS, RBC DI, Royal Bank of Canada or any of its affiliates or any other person accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or the information contained herein. In certain branch locations, one or more of the Companies may carry on business from premises shared with other Royal Bank of Canada affiliates. Notwithstanding this fact, each of the Companies is a separate business and personal information and confidential information relating to client accounts can only be disclosed to other RBC affiliates if required to service your needs, by law or with your consent. Under the RBC Code of Conduct, RBC Privacy Principles and RBC Conflict of Interest Policy confidential information may not be shared between RBC affiliates without a valid reason. ®/™ Trademark(s) of Royal Bank of Canada. Used under licence. © Royal Bank of Canada 2024. All rights reserved.