



Wealth
Management

the Navigator

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC WEALTH MANAGEMENT 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

Tax planning checklist for high-income earners

Depending on your province of residence, you may be subject to tax at a rate of 50% or higher when your income exceeds \$200,000. This article highlights a non-exhaustive list of tax minimization strategies to consider with a qualified tax advisor. The use of these strategies will vary based on personal circumstances. As such, it's crucial to check with a qualified tax advisor prior to implementing any of these strategies.

For the purposes of this article, any reference to a spouse includes a common-law partner.

Income splitting with family members

Family income splitting is a strategy that benefits from the progressive tax system where marginal tax rates rise as taxable income increases. It involves moving taxable income from a family member in a higher tax bracket to one in a lower tax bracket. By spreading taxable income among family members, a family may be able to retain more after-tax income.

It's important to understand the impact of the "attribution" rules in the Income Tax Act if you plan to income split with your family members. These rules have the effect of attributing taxable income back to the family member who supplied the capital for investment so that in effect, no tax savings are achieved. For more

information on income splitting and the attribution rules, ask your RBC advisor for an article on this topic.

Prescribed rate loan

If you have a low-income spouse, consider establishing a spousal loan to shift investment income and capital gains to them. This will allow you to take advantage of your

spouse's lower marginal tax rate. The strategy involves you transferring funds to your low-income spouse through a formal loan arrangement at the Canada Revenue Agency (CRA) prescribed interest rate. Your spouse may then be able to earn investment income on these loaned funds and pay taxes on the income and capital gains at their lower marginal tax rate, decreasing the overall family tax bill.

The prescribed rate is set by the CRA quarterly. The rate in effect at the time the funds are loaned should be used and will apply to the loan so long as it remains outstanding. Your spouse must pay you annual interest on the loan, which may be deductible to them. You (the lender) must include the interest you receive in your taxable income. This strategy may result in tax savings if the rate of return on your spouse's investments is higher than the interest paid to you by your spouse.

The prescribed rate loan strategy may also function between a parent and low-income adult child or grandchild. If you have minor children or grandchildren with little or no income, and you wish to split income with them, you may want to consider making a prescribed rate loan to a family trust.

Family trust

If you have children, grandchildren, nieces or nephews with little or no income, you may wish to consider establishing a family trust to shift investment income that would otherwise be taxed in your hands at a high marginal tax rate, to the hands of your low-income family members. If the trust is properly structured, income and capital gains earned in the trust that is paid or made payable to the trust beneficiaries may be taxed at their marginal tax rate.

As mentioned previously, when contemplating any income splitting strategy, you need to consider the attribution rules. To ensure the attribution rules do not apply and the trust income can be taxed in the beneficiary's hands, consider making a prescribed rate loan to the family trust. For more information, ask your RBC advisor for an article on using a family trust for a prescribed rate loan. In addition, you also need to consider the Tax on Split Income (TOSI) rules and how they might apply to the trust income earned and allocated to the trust beneficiaries. If the TOSI rules apply, income and capital gains allocated to a beneficiary would be taxed at the highest marginal tax rate in their hands. The TOSI rules are complex and should be discussed with a qualified tax advisor.

Expense optimization

If you have a low-income spouse, consider paying for all of your household expenses. Your lower-income spouse can then save and invest more of their income and the investment income earned can be taxed at your spouse's lower marginal tax rate.

Invest in registered accounts

Tax-Free Savings Account (TFSA)

In addition to investing in a TFSA of your own, consider making a gift to your spouse or other adult family members to enable them to contribute to a TFSA. All of

If you have children, grandchildren, nieces or nephews with little or no income, you may wish to consider establishing a family trust to shift investment income that would otherwise be taxed in your hands at a high marginal tax rate.

the investment income in the TFSA grows tax-free and future withdrawals are not taxable. Further, any income or capital gains earned in the TFSA do not attribute back to you.

Registered Retirement Savings Plan (RRSP)

If you contribute to an RRSP, you can deduct the amount of your RRSP contribution from your taxable income, up to your annual RRSP deduction limit. This will reduce the taxes you have to pay for a particular tax year. In addition, funds in an RRSP grow on a tax-deferred basis. The investment income and capital gains generated in the plan are not subject to tax until you make a withdrawal in the future.

You may also want to consider contributing to a spousal RRSP for your low-income spouse to equalize future retirement income. Any contributions you make to a spousal RRSP utilizes your own RRSP contribution room, and can be claimed on your tax return and deducted against your taxable income. Withdrawals from a spousal RRSP will be taxable to your spouse (provided you did not make a contribution in the year of withdrawal or in the two previous tax years.)

Registered Education Savings Plan (RESP)

Are you planning on paying for your child's post-secondary education? If so, consider setting up an RESP. While your contributions to an RESP are not tax-deductible, there are no taxes paid on the income and capital gains earned in the plan until the funds are withdrawn. Also, contributions to the plan may attract government grants which help your savings grow faster. When your child attends a qualified post-secondary education program, and withdrawals are made from the plan, the income earned in the plan may be taxed in your child's hands, presumably at a lower tax rate than your own.

Invest in tax-efficient investments

Flow-through shares

A flow-through share is a type of tax-advantaged investment vehicle designed to encourage investing in resource companies engaging in exploration and development in the mining, oil and gas, and renewable

energy and energy conservation sectors. If structured properly, the resource company may “renounce” or “flow through” certain expenses it incurs to you, which you can then deduct personally on your tax return. The maximum amount you can deduct is the amount you paid for the investment. You may apply the deductions against all sources of income, thereby reducing your net income and the associated tax liability. It is very important to consider the quality of the investment, and not just the potential tax write-off.

Tax-exempt life insurance

If you have surplus assets that you plan to pass on to your heirs, you should probably consider how these assets are invested. If you invest these assets in a non-registered account, the investment income earned will be exposed to your high marginal tax rate. As well, on death, you will generally be deemed to have disposed of these non-registered assets at fair market value, triggering any unrealized capital gains. This may result in a significant tax liability, reducing the size of your estate left to your heirs. As well, estate assets may need to be liquidated to meet this tax obligation.

Investing in a permanent tax-exempt life insurance policy may help achieve a variety of objectives. It may be used to provide an income replacement for your family should you die prematurely. It may also serve as a separate asset class to grow your estate tax-free. Under current tax laws, income earned within a tax-exempt life insurance policy is free from tax. As well, when you pass away, the death benefit is received by beneficiaries or your estate tax-free. A tax-exempt life insurance policy may also provide liquidity to your estate. The proceeds can be used to pay any taxes arising on death, preserving your estate for your beneficiaries.

Speak to a licensed life insurance representative to determine if you have an insurance need and/or to find out how tax-exempt insurance may work for you.

Maximize tax credits and deductions available to you

It’s important to be aware of the tax credits and deductions that may be claimed by you on your tax return to ensure maximum tax savings. One tax credit that’s often overlooked is the medical expense tax credit. You may wish to keep a running tally of the eligible medical expenses paid for out-of-pocket, as well as the receipts, so that you can more easily determine whether you qualify for the tax credit. These types of expenses accumulate quickly and, with organization, may potentially reduce your taxes payable.

Making a charitable donation is another way you can significantly reduce the personal tax you pay.

Making a charitable donation is another way you can significantly reduce the personal tax you pay. As an alternative to cash, consider donating publicly listed securities with an accrued gain in-kind to qualified charities. Any capital gain realized as a result of the donation will not be subject to tax. You will also receive a donation tax receipt equal to the fair market value of the security at the time of the donation. This may help reduce your total taxes payable and cost you less than if you were to sell the securities and donate the proceeds to the charity.

If you’ve thought about leaving a legacy for charitable purposes but are unsure about the best way to accomplish this, speak to your RBC advisor on the benefits of setting up your own charitable foundation through the RBC Charitable Gift Program.

Speak with a qualified tax advisor to ensure you’re claiming all tax credits and deductions available to you. Some commonly missed examples may include, childcare expenses, the disability tax credit, the pension income credit, non-reimbursed union and professional dues, and other employment expenses.

Tax residency planning

While moving to a lower tax jurisdiction is not a decision that should be taken lightly, it may be beneficial to consider this strategy if you have ties (e.g. family or a vacation property) in another province. The provincial tax rates to which you’re subject are based on your province of residence on December 31 of the taxation year. Residency status is always a question of fact and is based on the residential ties you have with each province. You should speak with a qualified tax advisor to determine your province of residence and whether this strategy may be beneficial to you.

Plan now

Tax planning should be an ongoing, dynamic process so that you don’t overlook opportunities to minimize tax. Whether you’re able to take advantage of the tax planning opportunities discussed earlier, or pursue other tax planning strategies, advance planning is a key part of the process.

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 Global Asset Management Inc. (RBC GAM), Royal Trust Corporation of Canada and The Royal Trust Company (collectively, the "Companies") and their affiliates, RBC Direct Investing Inc. (RBC DI) *, RBC Wealth Management Financial Services Inc. (RBC WMFS) 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, Royal Trust Corporation of Canada, The Royal Trust Company, 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 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. ®/™ Registered trademarks of Royal Bank of Canada. Used under licence. © 2021 Royal Bank of Canada. All rights reserved. NAV0025 (03/20)