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

Year of sale of your business

Sale of your business – Part 3

This article is the third in a four-part series intended to highlight key strategies to consider at different stages of your business. It isn't exhaustive, but it may help you to gain deeper understanding of some strategies you're already using or that might be suggested to you. This article discusses tax planning strategies to consider in the year of sale of your business. These strategies focus on minimizing your taxes payable in the year of the sale.

The other articles in the series are:

Part 1: Preparing your operating company for future sale

Part 2: Planning the sale of your business

Part 4: Year after the sale of your business

In this article, the terms "corporation" and "company" are used interchangeably to refer to a Canadian-controlled private corporation (CCPC). In simple terms, a CCPC is a private Canadian corporation that's not controlled by a non-resident of Canada, a public corporation or a combination; in addition, no class of shares of the corporation is listed on a designated stock exchange. This four-part series does not apply to public corporations or to businesses operating as a partnership or a sole proprietorship.

Tax strategies to implement before year-end

The third stage of selling your business is the year of sale. The sale may result in a significant capital gain, either in your hands personally because you've sold shares or in your corporation because you've sold assets of your corporation. If you sold shares of your corporation personally, the applicable tax year-end would be December 31 of the year in which the sale occurred. If your corporation sold assets, the applicable year-end would be your corporation's tax year-end in which the sale of assets occurred. Determining the year-end is important, as many tax planning strategies need to be implemented prior to year-end to be effective.

Here's a list of some tax strategies to minimize taxes on the capital gains on the sale of your business, and the following sections discuss certain strategies in more detail.

1. Charitable donations or establishing a charitable foundation
2. Establishing an individual pension plan (IPP) or a retirement compensation arrangement (RCA)
3. Triggering capital losses to offset the capital gains
4. Investing in flow-through shares to claim the tax deductions
5. Receiving the proceeds from the sale over a number of years to claim a capital gain reserve to defer tax over a period of up to five years

Charitable giving/foundation

You may consider using some of the sale proceeds to make a charitable gift in the year of sale either directly to a registered charity, donor-advised fund or charitable foundation. If you're interested, ask your RBC advisor for information about the RBC Charitable Gift Program, which is a donor-advised fund.

In general, every two dollars donated will eliminate one dollar of tax on the sale of the business (actual amount varies by the donation amount and your province/territory of residence). However, for this strategy to be effective, the charitable donation should be made before the end of the year in which the sale occurs (either December 31 in the case of an individual vendor or the tax year-end of the corporation for a corporate vendor). Since the donation is irrevocable, ensure you have adequate other assets to meet your retirement income and estate planning goals. A financial plan may help in this regard.

Alternatively, if the purchaser is a Canadian public company, consider structuring the sale so that you receive some shares of the Canadian public company as part of the sale proceeds on a rollover or tax-deferred basis. The public company shares could then be donated in-kind to eliminate the capital gains tax relating to the donated shares. You would also receive a donation tax receipt equal to the fair market value of the shares donated, allowing you to claim a donation tax credit. This may help reduce the tax on the sale of your business.

In general, every two dollars donated will eliminate one dollar of tax on the sale of the business (actual amount varies by the donation amount and your province/territory of residence).

Individual pension plan (IPP) or retirement compensation arrangement (RCA)

In some cases, you may consider the pros and cons of setting up an IPP or RCA in the year of sale, if you've not already done so. Ask your RBC advisor for more information about IPPs and/or RCAs. If your business is incorporated and the sale is structured as an asset sale, your corporation's contribution to these retirement plans is considered a deduction to the corporation, which would reduce the corporate taxes payable. A more detailed analysis of the pros and cons of this should be performed given that income received from an IPP or an RCA in retirement is taxed as regular income. In comparison, taxes payable today on an asset sale may be at lower tax rates (i.e. at capital gains rates).

Capital losses

If you have publicly traded securities that are in a capital loss position, consider selling these loss securities prior to year-end to trigger the capital loss. The capital loss can be used to offset the capital gains realized from the sale of your business, allowing you to reduce your taxable income and tax liability for the year. This decision should be made based on investment merits of the securities as well. Further, if you want to repurchase the same security, you may want to wait 30 days from settlement before repurchasing the security in order to avoid the loss being denied under the "superficial loss" rules. Ask your RBC advisor for a copy of the article discussing the superficial loss rules and planning strategies for more information.

Capital gains reserve

Instead of receiving all the sale proceeds in the year of sale, consider taking back a promissory note and having the purchaser pay the proceeds over a number of years, assuming you have an adequate guarantee of payment and an attractive interest rate on the note. In this case, a capital gains reserve may be taken to spread the capital gain on the sale over a maximum of five years. If your marginal tax rate is expected to be lower in the near future, the deferral of the capital gain can help minimize

your overall tax on the capital gain. However, if you're always going to be in the top marginal tax bracket, this strategy may not be effective.

Flow-through shares

Another option might be to purchase flow-through shares prior to year-end to help reduce the tax relating to the sale of the business. Flow-through shares are resource-based investments where the government allows, in certain circumstances, the purchase cost of the investment to be fully deducted against any other taxable income. However, the investments are more speculative in nature and may not be suitable for all individuals. If you're considering purchasing these types of investments, it's very important to consider the quality of the investment and not just the potential tax write-off. Keep in mind that for flow-through limited partnerships, there may be an 18- to 24-month holding period (the holding period does not apply to flow-through common shares).

To be eligible for the tax deductions, expenses incurred by the resource company and passed on to the investor must meet certain criteria. There may be a tax risk that the Canada Revenue Agency may deny the resource company from passing on their expenses if they don't meet these qualifications, which means you wouldn't be eligible for the tax deduction.

Alternative minimum tax (AMT)

The earlier sections address many tax savings strategies which can assist to reduce the ultimate tax you pay. In conjunction with these strategies, you'll want to consider if AMT will apply. AMT is intended to prevent high-income individuals (and certain trusts) from significantly lowering their taxes through the use of certain tax preferences, such as claiming certain tax deductions or earning primarily Canadian dividends and capital gains.

Consequently, you're required to compute your tax liability by calculating your regular tax and AMT. You pay either the regular tax or the AMT, whichever is highest. The AMT calculation allows fewer deductions, exemptions and tax credits than the regular income tax rules. This is the government's way of ensuring you pay at least a minimum amount of tax.

Historically, AMT applied in relatively narrow scenarios, such as when an individual claimed the lifetime capital gains exemption (LCGE) or claimed large flow-through share deductions. However, due to the recent changes, more high-income individuals may now be affected. In planning the sale of your business, it will be important to understand if AMT will apply and if there's any planning that can be done to reduce it.

To be eligible for the tax deductions, expenses incurred by the resource company and passed on to the investor must meet certain criteria. There may be a tax risk that the Canada Revenue Agency may deny the resource company from passing on their expenses if they don't meet these qualifications, which means you wouldn't be eligible for the tax deduction.

Conclusion

It may be possible to implement some or all of the strategies discussed in this article to reduce your taxes on the capital gain that results from the sale of your business. If you're interested in any of these approaches, your RBC advisor may be able to provide additional articles that contain more information. Review these strategies with a qualified tax advisor to determine if they are suitable in your circumstances.

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 2025. All rights reserved.

NAV0123 (10/2025)