

# Borrowing Money to Leverage a Flow-Through Investment

Borrowing money to make investments can magnify the investment results of both a positive and a negative investment return. Applied to flow-through limited partnership investments, leverage may provide risk management and performance enhancements. Below are 3 examples of how leverage can impact a flow-through investment comparing a **\$6,000 flow-through investment with a \$6,000 flow-through investment leveraged to \$10,000**. Note: returns "With Leverage" includes repayment of the loan in full (see below).

## I. Assumes the flow-through portfolio's NAV at liquidation is **100%** of original capital invested:

	<b>No Leverage</b> (\$6,000 Investment)	<b>With Leverage</b> (\$10,000 Investment)
Investor's initial capital invested	\$ (6,000)	\$ (6,000)
Amount of borrowed money invested	0	(4,000)
Investor's flow-through tax deduction savings <sup>(1)</sup>	2,700	4,500
Investor's loan interest cost <sup>(2)</sup>	0	( 640)
Investor's interest tax savings <sup>(1) (4)</sup>	0	288
Liquidity value of flow-through investment (100% of initial investment) <sup>(3)</sup>	6,000	10,000
Capital gain tax on liquidity value	<u>(1,350)</u>	<u>(2,250)</u>
<b>Net Cash to Investor</b>	<b><u>\$ 1,350</u></b>	<b><u>\$ 1,898</u></b>
<b>Return on initial capital invested</b>	<b>22.5%</b>	<b>31.6%</b>

## II. Assumes the flow-through portfolio's NAV at liquidation is **125%** of original capital invested:

	<b>No Leverage</b> (\$6,000 Investment)	<b>With Leverage</b> (\$10,000 Investment)
Investor's initial capital invested	\$ (6,000)	\$ (6,000)
Amount of borrowed money invested	0	(4,000)
Investor's flow-through tax savings <sup>(1)</sup>	2,700	4,500
Investor's loan interest cost <sup>(2)</sup>	0	( 640)
Investor's interest deduction tax savings <sup>(1) (4)</sup>	0	288
Liquidity value of flow-through investment (125% of initial investment) <sup>(3)</sup>	7,500	12,500
Capital gain tax on liquidity value	<u>(1,688)</u>	<u>(2,813)</u>
<b>Net Cash to Investor</b>	<b><u>\$ 2,512</u></b>	<b><u>\$ 3,835</u></b>
<b>Return on initial capital invested</b>	<b>41.9%</b>	<b>63.9%</b>

## III. Assumes the flow-through portfolio's NAV at liquidation is **70%** of original capital invested:

	<b>No Leverage</b> (\$6,000 Investment)	<b>With Leverage</b> (\$10,000 Investment)
Investor's initial capital invested	\$ (6,000)	\$ (6,000)
Amount of borrowed money invested	0	(4,000)
Investor's flow-through tax savings <sup>(1)</sup>	2,700	4,500
Investor's loan interest cost <sup>(2)</sup>	0	( 640)
Investor's interest deduction tax savings <sup>(1) (4)</sup>	0	288
Liquidity value of flow-through investment (70% of initial investment) <sup>(3)</sup>	4,200	7,000
Capital gain tax on liquidity value	<u>( 945)</u>	<u>(1,575)</u>
<b>Net Cash to Investor</b>	<b><u>\$ ( 45)</u></b>	<b><u>\$ ( 427)</u></b>
<b>Return on initial capital invested</b>	<b>(0.8%)</b>	<b>(7.1%)</b>

(1) Assumes a 45% marginal tax rate

(2) Assumes a 2 year loan at 8% per annum

(3) Adjusted cost base (ACB) is nil

(4) Interest may be tax deductible - please consult your tax specialist for advice