



UNITY'S PRACTICAL GUIDE TO RECENT TAX CHANGES



This week, the federal government announced its intention to increase the capital gains inclusion rate from one-half to two-thirds, effective June 24, 2024. Our goal in this memo is to explain the most important ways this change may affect you.

The change will affect individual taxpayers differently from business and trusts.

For all corporations and trusts: the higher inclusion rate will affect all capital gains. Professional corporations and holding companies fall into this category.

For individuals: the higher inclusion rate will only affect capital gains more than \$250,000 in a given tax year. Principal residences are exempt from capital gains tax of any type and will be unaffected by this change.

THREE WAYS THESE CHANGES MIGHT AFFECT YOU:

1. ESTATE PLANNING

Many of our clients are using (or are planning to use) permanent life insurance to create liquidity to pay taxes on capital gains realized at death. This planning is often used in conjunction with an estate freeze, which involves freezing the value of certain assets, typically shares in a family business or investment portfolio, at their current fair market value to effectively reduce the taxable value of the estate at the time of death.

With the increase in the capital gains inclusion rate, both regular shareowners and persons that have implemented estate freezes may now be facing a larger tax bill upon death (your tax bill could be about 30% higher). Adding extra permanent life insurance may be required to update your estate plan to ensure your estate has enough liquidity to cover off the full tax bill. Speak to your Unity advisor if you think you're impacted.

2. STRATEGIC TAX PLANNING

In response to higher tax rates, you may want to consider carving out time to discuss tax planning with your Unity advisor. Permanent life insurance offers tax-deferred growth and tax-free withdrawals and is not affected by these tax changes. Our advanced planning strategies can become a vital tax planning tool to complement the rest of your financial portfolio.

3. TAX DEFERRAL IN YOUR CORPORATION

One of the key tax deferral benefits of incorporation is the ability to retain earnings within the corporation. Unlike personal income, which is taxed immediately, earnings retained in the corporation are taxed at the corporate rate, deferring personal tax until the earnings are distributed as dividends. These changes treat capital gains inside a corporation differently than those accruing in your personal hands.

UNITY'S PRACTICAL GUIDE TO RECENT TAX CHANGES



While these changes lessen the tax benefits of incorporating somewhat, the advantages are still immense. Corporations have other special tax advantages, including owning and funding life insurance. Because of the complex nature of the incorporation question, speak to a Unity advisor and your tax professional when considering options around incorporation.

A NUMERICAL ILLUSTRATION OF HOW THIS CHANGE WORKS:

- You buy an asset for \$1000; this is the adjusted cost base (ACB). The ACB is the purchase price of the investment, plus any acquisition costs such as commissions or legal fees.
- If you sold the asset for \$2000, you made a \$1000 gain, against which capital gains taxes apply.
 - Before the proposed changes (50% capital gains inclusion rate)
 - \$1000 gain x 50% is \$500 of taxable income that will be taxed at your marginal tax rate based on your tax bracket.
 - Assuming you are in the top tax bracket in Manitoba, your tax rate would be 50.4%.
 - \$1000 gain x 50% x 50.4% = \$252 total taxes paid

- After proposed changes (66.67% capital gains inclusion rate)
 - \$1000 gain x 66.67% is \$667 of taxable income that will be taxed at your marginal tax rate based on your tax bracket.
 - Assuming you are in the top tax bracket in Manitoba, your tax rate would be 50.4%.
 - \$1000 gain x 66.67% x 50.4% = \$336 total taxes paid
- Effectively, in Manitoba in the top tax bracket, your capital gains taxes paid will increase from 25.20% to 33.60%, or an extra \$84 in taxes owed on every \$1000 of capital gain.

AT A GLANCE THE POSITIVES

- Permanent life insurance tax deferred growth not affected

THE CHALLENGES

- Potential larger tax bill at death (30% larger)
- Changes lessen the tax benefit of incorporating
- Many people now owe more tax

UNITY'S PRACTICAL GUIDE TO RECENT TAX CHANGES



OTHER NOTABLE PROPOSED CHANGES:

LIFETIME CAPITAL GAINS EXEMPTION:

- The budget proposes to increase the LCGE on eligible capital gains from \$1,016,836 to \$1,250,000 for dispositions that occur that June 24, 2024.

CANADIAN ENTREPRENEURS' INCENTIVE:

- The CEI would reduce the tax rate on capital gains resulting from the disposition of qualifying shares of a corporation by an eligible individual. It would effectively exempt up to \$2 million in capital gains per individual over their lifetime.
- The qualification standards may require advanced planning, so speak with a tax professional and your Unity advisor for guidance.

HOME BUYERS PLAN:

- The HBP helps eligible home buyers save for a downpayment by allowing them to withdraw up to \$35,000 from a registered retirement savings plan (RRSP) to purchase or build their first home without having to pay tax on the withdrawal.
- The budget proposes to increase the HBP withdrawal limit from \$35,000 to \$60,000.

AUTHOR:



TREVOR SHAW, CFA
PARTNER