2024

Federal budget

Insights from our
Tax & Estate Planning professionals

RICHARDSON Wealth

On April 16, 2024, Deputy Prime Minister and Finance Minister Chrystia Freeland tabled the Liberal Government's federal budget ("**Budget 2024**").

Titled *Fairness For Every Generation,* Budget 2024 is intended to build a Canada that works better for all generations, with net new spending of $39.2 billion over the next 5 years to make housing more affordable, to make life cost less, and to drive economic growth and productivity. While Budget 2024 did not include a plan to balance the budget, it forecasts declining deficits over the next 5 years, from $39.8 billion for 2024–25 to $20 billion for 2028–29.

Insight:

Budget 2024 **does not** propose changes to the following items:

- Personal income tax rates;
- Corporate income tax rates; and
- The Principal Residence Exemption.

Budget 2024 also **does not** introduce a wealth tax for individuals.

However, Budget 2024 proposes to:

- Increase the capital gains inclusion rate for corporations, trusts, and certain individuals;
- Increase the Lifetime Capital Gains Exemption (LCGE); and
- Introduce a new Canadian Entrepreneurs' Incentive (CEI) to provide preferential tax treatment for sales of qualifying shares of a business.

The following is a summary of the tax and wealth planning proposals that we believe are of interest to Richardson Wealth clients, as well as our insights on those proposals.

Capital gains inclusion rate

For **capital gains realized on or after June 25, 2024**, Budget 2024 proposes to modify the current capital gains inclusion rate of 50% in the following manner:

Taxpayer	Proposed inclusion rate(s)	Proposed top federal tax rate on capital gains
Individuals	**50%** for the first $250,000 of capital gains realized in the year **66.67%** for capital gains realized in the year **exceeding $250,000**	**16.5%** for the first $250,000 of capital gains realized in the year **22%** for capital gains realized in the year **exceeding $250,000**
Corporations	**66.67%**	**25.78%**
Trusts	**66.67%**	**22%**

This represents a **33.33% increase** in capital gains tax.

Insight:

An increase to the capital gains inclusion rate has been speculated for many years. If the increase is enacted, there are numerous implications that can impact your wealth planning. Some of the implications include but are not limited to the following:

Deemed disposition rules may cause individuals to realize more than $250,000 of capital gains in a particular year.

- An individual generally has control over when capital gains are realized; however, tax rules can deem a disposition of assets upon certain events which may be outside of their control. A deemed disposition may result in an individual realizing more than $250,000 of capital gains in a particular year, which are taxed at the higher inclusion rate. Common events that trigger deemed dispositions include:
  - An individual's death, unless they transfer their property to a surviving spouse or common-law partner; or
  - An individual becoming a non-resident of Canada for tax purposes.

Alternative Minimum Tax (AMT): less of an issue for some

- The proposed changes to the AMT introduced in Budget 2023 may no longer be of major concern for individuals realizing more than $250,000 of capital gains, since the top proposed regular tax rate of 22% would exceed the proposed minimum tax rate of 20.5%.

Corporations and trusts: More planning is needed

- Unlike individuals, corporations and trusts do not benefit from a tiered inclusion rate. Therefore:
  - The integrated personal and corporate tax cost of earning capital gains inside a corporation would be increased.
  - Trusts may have a greater incentive to distribute taxable capital gains to individual beneficiaries to make use of their annual $250,000 threshold.

Capital Dividend Account (CDA): additions will be reduced

- A Canadian-Controlled Private Corporation (CCPC) realizing capital gains would only be able to add 33.33% of the gain in its CDA versus 50% under current rules. The CDA is beneficial as it permits the payment of tax-free capital dividends to Canadian-resident shareholders.

The Small Business Deduction may be impacted

- A CCPC may not be able to claim a full Small Business Deduction on its active business income due to the "passive income rules," which grind down the maximum $500,000 deduction limit by $5 for every $1 of passive income exceeding $50,000. Passive income includes capital gains, which would take into account the increased inclusion rate.

Planning tips:

If you have assets with material accrued capital gains, consider and seek tax advice on the following planning strategies:

- Realize capital gains before June 25, 2024 in order to lock in the current 50% inclusion rate. For individuals, this strategy should factor in the proposed changes to the AMT from Budget 2023 (which have not yet been enacted) that were intended to apply as of January 1, 2024.
- For individuals, realize sufficient capital gains each year (on or after June 25, 2024) in order to benefit from the 50% inclusion rate on the first $250,000 of capital gains.
- Explore the use of life insurance to move taxable funds into a tax-sheltered vehicle that can help with funding increased taxes at death.

These decisions may be easy to make for assets that you are already planning to sell, but less so for assets that you plan on holding for the long-term. It is important to consider your overall investment objectives and circumstances and to not let the "tax tail wag the investment dog."

For more information on "tax-gain harvesting strategies," ask your **Richardson Wealth Advisor** for a copy of our education article on the topic.

The federal government will provide additional details in the coming months. The following is a summary of some of the key design details released so far.

Determination of $250,000 threshold for individuals

For individuals, the $250,000 threshold would apply to capital gains, either directly or indirectly via a partnership or trust, net of any capital losses (from the current or other years) and capital gains where the LCGE, the proposed Employee Ownership Trust (EOT) exemption, or the proposed CEI is claimed.

Treatment of capital losses

The inclusion rate applies to capital losses. Net capital losses from prior years, which are based on the inclusion rate(s) applicable in the year(s) the losses were incurred, would continue to be deductible against taxable capital gains in the year by adjusting their value to reflect the inclusion rate of the capital gains being offset.

Insight:

This suggests that a capital loss realized prior to the rate change would fully offset an equivalent capital gain realized after the rate change. Therefore, it may become more beneficial for taxpayers to preserve net capital losses from prior years so that they can be applied against capital gains that would be subject to the higher 66.67% inclusion rate.

Transitional rules

Since the increase to the inclusion rate is proposed to apply on or after the effective date of June 25, 2024, many taxpayers will have to face the complexity of having two inclusion rates in one taxation year. Transitional rules would be implemented to identify capital gains and losses realized before and on or after the effective date, and apply the appropriate inclusion rate. Furthermore, the annual $250,000 threshold for individuals would be fully available in 2024 and would apply only in respect of net capital gains realized on or after the effective date.

Employee stock option deduction

The employee stock option deduction mimics the taxation of capital gains by providing a deduction currently equal to 50% of the taxable benefit associated with exercising stock options issued by an employer.

As a result of the changes to the capital gains inclusion rate, employees claiming the stock option deduction in respect of stock options exercised on or after June 25, 2024 would only be permitted a deduction of **33.33% of the taxable benefit**, but would still be permitted the current deduction of 50% of the taxable benefit, up to a combined limit of $250,000 for both employee stock options and capital gains.

Note:

There are a number of conditions that need to be satisfied in order for employee stock options to qualify for the stock option deduction. For more details, ask your **Richardson Wealth Advisor** for a copy of our education article on the topic.

Lifetime Capital Gains Exemption

Every individual can claim a LCGE to exempt all or a portion of the capital gains realized on the disposition of qualified small business corporation shares and qualified farm or fishing property. The LCGE for 2024 is $1,016,836 and is indexed to inflation.

Budget 2024 proposes to increase the LCGE to **$1.25 million** for **dispositions that occur on or after June 25, 2024**. The increased LCGE will be indexed to inflation after 2025.

Canadian Entrepreneurs' Incentive

To encourage entrepreneurship, Budget 2024 proposes to introduce the CEI, which will reduce the capital gains inclusion rate to **33.33%** on **up to $2 million of capital gains realized by an individual over their lifetime** on sales of qualifying shares of a business.

The lifetime limit would be phased in by **increments of $200,000 per year, beginning on January 1, 2025**, before ultimately reaching a value of $2 million by **January 1, 2034**.

Qualifying conditions

There are a number of conditions that need to be satisfied in order for shares to qualify for the CEI, some of which align with the conditions under the LCGE. In addition:

- The individual must be a founding investor at the time the incorporated business was initially capitalized.
- For at least 5 years prior to the sale:
  - The individual must have directly held shares in the business; and
  - The individual must have been actively engaged on a regular, continuous, and substantial basis in the business.
- At all times since the initial share subscription until the time of sale, the individual must have directly held shares representing more than 10% of both votes and value in the business.
- The corporation cannot be a professional corporation, nor a corporation providing consulting or personal care services, or operating in the financial, insurance, real estate, food and accommodation, arts, recreation, or entertainment sector.

Integration with the LCGE

The CEI applies in addition to the LCGE. Therefore, once the CEI is fully rolled out in 2034, eligible individuals could receive preferential tax treatment on **at least $3.25 million of capital gains** realized on sales of qualifying shares.

Example:

Melissa founded a technology start-up in 2020 and is the sole shareholder. In 2030, she accepts an offer to sell her company to a third party and earns $3,000,000 in capital gains. She has never used her LCGE.

Ignoring the indexation of the LCGE and assuming no other capital gains, Melissa would have taxable income from the sale of **$725,000**.

= $1,250,000 capital gain eligible for LCGE = $0

+ $1,200,000 capital gain eligible for CEI x 33.33% = $400,000

+ $250,000 capital gain x 50% = $125,000

+ $300,000 capital gain x 66.67% = $200,000

Under current rules, Melissa's taxable income would have been $875,000.

Alternative Minimum Tax

The AMT is a parallel tax calculation that calculates personal income tax in a manner that permits fewer deductions, exemptions, and credits than under the regular income tax rules. Each year, an individual pays total income tax equal to the greater of the "minimum tax" calculated under the AMT, and the tax calculated under the regular income tax rules.

The federal government proposed extensive changes to the AMT in Budget 2023, none of which have yet been enacted. Part of the delay in implementation may have been due to significant lobbying from the charitable sector in respect of changes to the rules that would have negatively impacted philanthropy.

Budget 2024 proposes to make several amendments to the AMT proposals, which would apply **on or after January 1, 2024** (the same date as the broader AMT proposals).

The most notable amendment is to permit individuals to claim **80% of the charitable donation tax credit** when calculating the AMT (rather than the previously proposed 50%).

Insight:

The amendment to the amount of the charitable donation tax credit that can be claimed under the proposed AMT suggests that donations are now unlikely to result in AMT implications. This is because 80% of the top federal charitable donation tax credit rate of 33% is 26.4%, which is higher than the proposed AMT rate of 20.5%. Under the original proposed AMT, only 50% of the charitable donation tax credit could be claimed in computing AMT. The resulting tax credit rate of 16.5% would be less than the proposed AMT rate of 20.5%, which could result in AMT applying when an individual makes significant donations.

It is important to note that Budget 2024 did not announce any amendments to the proposal under the AMT to include 30% of capital gains on the donation of publicly listed securities. Therefore, philanthropists who are looking to make significant donations, particularly of publicly listed securities with accrued capital gains, should consult their tax advisors to run projections and assess the potential AMT implications based on their specific circumstances.

For a summary of the broader AMT proposals introduced last year, ask your **Richardson Wealth Advisor** for a copy of our Budget 2023 report.

Initiatives for home buyers

Home Buyers' Plan (HBP)

Budget 2024 proposes a number of changes to the HBP, including:

- An increase to the withdrawal limit from $35,000 to **$60,000**, which would apply to the 2024 and subsequent calendar years in respect of **withdrawals made after April 16, 2024**.
- A temporary deferral of the 15-year HBP repayment period by an **additional 3 years** for participants making a **first withdrawal between January 1, 2022 and December 31, 2025**. This would mean that the repayment period would start the **5th year** following the year in which a first withdrawal is made.

Insight:

This proposal means that between the HBP and the Tax-Free First Home Savings Account (FHSA), a prospective first-time home buyer can now withdraw **$100,000 of capital, plus growth in the FHSA**, to purchase a qualifying home.

Notwithstanding the increase to the HBP withdrawal limit, if you are a first-time home buyer and home ownership is an objective of yours, you should still prioritize maximizing your FHSA over your Registered Retirement Savings Plan (RRSP). Additional savings can then be directed to the RRSP to withdraw under the HBP.

For more details on the HBP and the FHSA, ask your **Richardson Wealth Advisor** for a copy of our education articles on the topics.

Mortgage amortization

To enable more younger Canadians to afford a mortgage and encourage new supply of housing, Budget 2024 announces **30-year mortgage amortizations** for **first-time home buyers purchasing newly-constructed homes**. The new mortgage product will be available starting **August 1, 2024**. Additional details will be released in the coming months.

Employee Ownership Trust tax exemption

Budget 2023 introduced the EOT as an alternative succession tool for business owners. Broadly speaking, an EOT is a trust that holds shares of a corporation for the benefit of the corporation's employees. Instead of selling the shares of a corporation to the employees (who are not in a position to pay for them), the business owner would sell the shares to the EOT. The EOT could borrow to fund the purchase and use the corporation's profits over time to repay the loan. This form of ownership could facilitate continuity of an active business and encourage greater worker participation in employees, who are the ultimate beneficiaries of the EOT.

The legislation necessary to facilitate the creation of the EOT is currently before Parliament.

Note:

For a summary of the EOT proposals introduced last year, ask your **Richardson Wealth Advisor** for a copy of our Budget 2023 report.

Budget 2024 provides further details on a proposal to **temporarily exempt the first $10 million of capital gains realized on the sale of a business to an EOT from tax**, subject to certain conditions. The conditions require, among others, that the individual seller (i.e., business owner) be actively engaged in the business on a regular and continuous basis for at least 24 months before the sale, and at least 90% of the EOT beneficiaries be residents of Canada.

There are also disqualifying events that would either deny the capital gains exemption to the seller (even on a retroactive basis) or deem the EOT to realize a capital gain equal to the amount of exempt capital gains. A disqualifying event would occur if an EOT loses its status as an EOT or if less than 50% of the fair market value of the qualifying business' shares is attributable to assets used principally in an active business at the beginning of 2 consecutive taxation years of the corporation.

Insight:

Similar to capital gains that are exempt under the LCGE, 30% of capital gains exempt under the EOT exemption would be included for AMT purposes. Therefore, sellers may still have some tax to pay on a qualifying sale of their business to an EOT due to the AMT.

The measure would apply to qualifying dispositions of shares that occur **between January 1, 2024 and December 31, 2026.**

Canada Carbon Rebate for Small Businesses

Budget 2024 proposes to return a portion of fuel charge proceeds from a province to small businesses that employ 499 or fewer employees and file tax returns. The Canada Carbon Rebate for Small Businesses would be in the form of an automatic refundable tax credit. The amount of the rebate will be based on the number of individuals the qualifying business employs in the province.

Other measures

- **Introduce a new Canada Disability Benefit** of up to $2,400 per year to bridge the gap between the Canada Child Benefit and Old Age Security for disabled persons.
- **Expand the Disability Supports Deduction** to include additional expenses, such as expenses for service animals.
- **Double the credit amount for the Volunteer Firefighters and Search and Rescue Volunteers Tax Credits** from $3,000 to $6,000 (maximum federal credit of $900).
- **Extend the Mineral Exploration Tax Credit** by an additional year for flow-through share agreements entered into on or before March 31, 2025.
- **Enhance the Canada Pension Plan (CPP)** by providing a top-up to the death benefit for certain contributors, introduce a partial children's benefit for part-time students, and end entitlement to a survivor's benefit following a CPP credit split.
- **Extend eligibility for the Canada Child Benefit (CCB)** in respect of a child for 6 months after the child's death if the individual would have otherwise been eligible for the CCB in respect of that particular child.
- **Accelerate Capital Cost Allowance claims** for purpose-built rental housing and productivity-enhancing assets (e.g., patents, data network infrastructure equipment, general-purpose electronic data-processing equipment).
- **Modernize Canada's tax system** by piloting new automatic filing services and implementing a single sign-in portal for government services, and better services for Canadians.
- **Facilitate the efficiency and effectiveness of tax audits** by introducing a new "notice of non-compliance" that can be issued to persons who have not complied with a requirement or notice to provide assistance or information issued by the Canada Revenue Agency.