HILLSIDE IN THE NEWS

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USING DATA TO DRIVE DECISIONS WHEN LOOKING AT THE 2024 FEDERAL BUDGET

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When it comes to making important decisions, having the right data means everything.

This year's Federal Budget, released on April 16th, included changes to the capital gains inclusion rate for both individuals and corporations.

FOR INDIVIDUALS:

The capital gains inclusion rate for gains over $250,000 is rising from 50% to 66.67%. The inclusion rate on capital gains under $250,000 will remain at 50%. For individuals, the new rules don't have a big impact, except for estate planning purposes or when someone is selling a secondary property, i.e.. not their principle residence.

FOR BUSINESS OWNERS:

The inclusion rate on all capital gains is increasing to 66.67%. This is meaningful and does change the landscape. Under the current rules, there's a benefit to using corporate dollars to invest, assuming the company benefits from the small business tax deduction.

Here's a summary of what would happen to a corporate portfolio earning a 6% rate of return:

Pre 2024 budget rules	Post 2024 budget rules
7.03%	6.27%

Applying these returns to a $1m portfolio over a 20yr time horizon produced the following dollar values:

Pre 2024 budget	Post 2024 budget
$3,891,441	$3,374,532

There's not much point in crying over a ~$500,000 difference. But we should do whatever we can to adjust to the new landscape to protect capital moving forward.

Here’s what business owners/incorporated professionals should consider moving forward:

1. **Take full advantage of RRSPs moving forward.**
   Strongly consider drawing out enough income from the company to generate max RRSP contribution room and maximize contributions- this made a lot of sense for most folks pre-2024 budget and makes even more sense now.

2. **Individual Pension Plans (IPPs).**
   IPPs are pension plans which incorporated business owners/professionals can build for themselves. They are much like RRSPs- tax deductible/deferred and you pay tax on the pension benefit when you start drawing it out at retirement. The big benefit is for anyone mid 40s or older with a strong history of salaried income- you can contribute much more than you would using a standard RRSP investment. Yes, IPPs in the right scenario are a “juiced-up” version of an RRSP. Again- these made good sense in the past and make even more sense now.
3. **Corporately owned life insurance.**
   If you have more money invested in your company than you could possibly spend in your lifetime, a properly constructed insurance solution was the most tax efficient way of allocating the capital. With the kicker being you must die for you, or your estate, to benefit. Again, these will be even more attractive under the new tax regime.

The existing rules, pre-budget 2024, rules are in place until June 24, 2024- so there’s time to intentionally trigger gains and benefit from the lower inclusion rate. The problem is if you do this, you’ll need to come up with cash to pay the resulting tax bill. The money will either come from your portfolio or your bank account, which should’ve been in your portfolio if you were following our 2nd golden rule! Either way you’d be shrinking your portfolio to voluntarily pay more tax.

Generally, this is a bad idea because you have less money working for you. But if you need the money in the next ~2yrs it makes sense to trigger the gains now and pay the tax. Also- remember all short-term money shouldn’t be invested, so this really should be done regardless of the potential tax benefits. Anything longer than ~3yrs, you’re better off leaving things as is.

The discussion of pulling money out of a company is more complex. Generally, the same 2-3yr rule still applies, but there are different avenues, namely capital dividends, which should be explored.

Our monthly theme is ***Data Drives Decisions***, quite timely. The message is clear: we strongly recommend taking a good look at your data and see what tweaks should be made pre/post June 24, 2024, to ensure you’re on the right track.

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