Should I sell or should I hold? Capital gains tax planning

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Should I sell, or should I hold now?
If I hold, there could be trouble,
And if I sell, it could be double!

- With apologies to The Clash[1]

The planned increase in the capital gains inclusion rate announced in the 2024 federal budget (Budget) has created a frenzy of discussion, worry and anxiety, and, in some cases, the opportunity to get ahead of the change by doing some proactive planning. Here's what's happening, who may be impacted, and what you can do about it.

The changes

Under the current tax rules, if you dispose of capital property (other than your principal residence) for a profit, only half (50%) of the capital gain is included in your taxable income. The Budget proposed to increase the capital gains inclusion rate to two-thirds (66.67%) for some capital gains realized starting on June 25, 2024.

[1] The Clash. "Should I Stay or Should I Go" written by Mick Jones. Combat Rock, CBS Records, 1981. LP.

For corporations and trusts[2], the higher 66.67% inclusion rate applies to all gains realized on or after that date. But the rules are expected to work a bit differently for individuals. An individual who realizes a capital gain on or after June 25, 2024 will still be able to take advantage of the 50% inclusion rate on the first $250,000 of annual capital gains. This $250,000 limit is not prorated for 2024, and only applies to gains realized on or after June 25. This means the current 50% inclusion rate applies to total capital gains realized before June 25, 2024, as well as the first $250,000 of total capital gains realized from June 25 onwards. The new 66.67% rate will apply to total capital gains above $250,000 that are realized after June 25.

Investors who have capital losses carried forward from prior years will still be able to deduct them against taxable capital gains in the current year by adjusting their value to reflect the inclusion rate of the capital gains being offset. This effectively means that a capital loss realized at the current 50% allowable rate will be fully available to offset an equivalent capital gain realized once the inclusion rate goes up to 66.67%. For example, a $1,000 capital loss will always fully offset a $1,000 capital gain, regardless of the capital gains inclusion rates at the time of the loss and gain.

What are the new capital gains tax rates?

Individuals

Given that for individuals 66.67% of the gain will now be taxable for dispositions above $250,000 annually on or after June 25, 2024, this means that the effective tax rate on capital gains will be increasing. Consider, for example, an Ontario investor who pays tax at the top marginal rate. Before June 25, 2024, the tax rate on capital gains is 26.76%. Starting on June 25, for individuals the tax rate will be 26.76% for the first $250,000 of total capital gains each year[3], and 35.69% for gains over $250,000. This means that the tax rate will be 8.93 percentage points higher when the 66.67% inclusion applies.

Figure 1: Highest marginal tax rates on capital gains for individuals in 2024

Region	50% inclusion rate[4]	66.67% inclusion rate[5]	Increase (percentage points)
AB	24.00%	32.00%	8.00
BC	26.75%	35.67%	8.92
MB	25.20%	33.60%	8.40
NB	26.25%	35.00%	8.75
NL	27.40%	36.53%	9.13
NS	27.00%	36.00%	9.00
NT	23.53%	31.37%	7.84
NU	22.25%	29.67%	7.42
ON	26.76%	35.69%	8.93
PE	25.88%	34.50%	8.62
QC	26.65%	35.54%	8.89
SK	23.75%	31.67%	7.92
YT	24.00%	32.00%	8.00

Source: Tax Templates Inc.

[2] Although the higher 66.67% inclusion rate applies to all gains realized in a trust on or after June 25, 2024, it's generally less problematic since trusts are generally able to distribute their capital gains to their beneficiaries.

[3] This rate also applies to the first $250,000 of capital gains realized in the period starting June 25, 2024 and ending December 31, 2024.

[4] For capital gains realized before June 25, 2024, and for the first $250,000 of total capital gains realized after June 25, 2024.

[5] For total capital gains over $250,000 realized on or after June 25, 2024.

The increase in tax on capital gains varies by province or territory. Figure 1 shows the top 2024 marginal tax rates on capital gains at both the current (50%) inclusion rate, and the new (66.67%) rate.

Corporations

As stated above, the capital gains inclusion rate for gains in a corporation will also be going up for gains realized on or after June 25, 2024, with no $250,000 limitation. For example, in Ontario, the corporate tax rate for capital gains is currently 25.09%, and will increase by 8.36 percentage points to 33.45% starting on June 25, 2024.

The increase in tax on capital gains realized inside a corporation varies by province or territory. Figure 2 shows the tax rates on capital gains for corporations at both the current 50% inclusion rate, and the new 66.67% rate.

Figure 2: Corporate tax rates on capital gains in 2024

Region	50% inclusion rate[6]	66.67% inclusion rate[7]	Tax rate increase (percentage points)
AB	23.34%	31.11%	7.77
BC	25.34%	33.78%	8.44
MB	25.34%	33.78%	8.44
NB	26.34%	35.11%	8.77
NL	26.84%	35.78%	8.94
NS	26.34%	35.11%	8.77
NT	25.09%	33.44%	8.35
NU	25.34%	33.78%	8.44
ON	25.09%	33.44%	8.35
PE	27.34%	36.44%	9.10
QC	25.09%	33.44%	8.35
SK	25.34%	33.78%	8.44
YT	25.34%	33.78%	8.44

Source: Tax Templates Inc.

Impact on integration

The portion of the capital gains (either 50% or 33.33%) that was not taxed in the corporation may generally be distributed to the shareholder(s) as capital dividends, which are usually received tax-free. The corporation can distribute the remaining after-tax amount of capital gains (along with any refundable tax that may be recovered), as non-eligible dividends, which are taxable.

The integrated tax rate is the effective tax rate paid on income earned in a corporation and distributed to the shareholder(s) once both corporate and personal tax are paid. If the integrated tax rate on capital gains is lower (or higher) than the personal tax rate on capital gains, there is a tax savings (or cost).

6 For capital gains realized before June 25, 2024.

7 For capital gains realized starting June 25, 2024.

Capital gains over $250,000

For the portion of capital gains that exceeds $250,000 in a year, the capital gains inclusion rate will increase to 66.67% from 50% for dispositions on or after June 25, 2024 for both corporations and individuals. Figure 3 shows the integrated tax rates and tax costs when these capital gains are earned through a corporation in 2024, for all provinces and territories, assuming the shareholder pays tax at the top marginal tax rate.

Figure 3: Capital gains over $250,000 – Comparison of 2024 integrated tax rates and personal tax rates for capital gains, when shareholder is taxed at the top marginal rate

Region	Integrated tax rate before June 25	Top personal tax rate before June 25	Tax Savings (Cost)	Integrated tax rate starting June 25	Top personal tax rate starting June 25	Tax Savings (Cost)
AB	25.77%	24.00%	(1.77%)	34.36%	32.00%	(2.36%)
BC	29.56%	26.75%	(2.81%)	39.41%	35.67%	(3.74%)
MB	28.67%	25.20%	(3.47%)	38.23%	33.60%	(4.63%)
NB	29.60%	26.25%	(3.35%)	39.46%	35.00%	(4.46%)
NL	30.83%	27.40%	(3.43%)	41.10%	36.53%	(4.57%)
NS	30.15%	27.00%	(3.15%)	40.20%	36.00%	(4.20%)
NT	24.58%	23.53%	(1.05%)	32.76%	31.37%	(1.39%)
NU	25.12%	22.25%	(2.87%)	33.49%	29.67%	(3.82%)
ON	28.96%	26.76%	(2.20%)	38.62%	35.69%	(2.93%)
PE	30.76%	25.88%	(4.88%)	41.00%	34.50%	(6.50%)
QC	29.35%	26.65%	(2.70%)	39.14%	35.54%	(3.60%)
SK	26.54%	23.75%	(2.79%)	35.39%	31.67%	(3.72%)
YT	27.62%	24.00%	(3.62%)	36.82%	32.00%	(4.82%)

Source: Tax Templates Inc.

As we can see in Figure 3, the tax cost of earning capital gains in a corporation versus earning them personally increases slightly in each province for gains subject to the higher 66.67% inclusion rate even if earned personally. But, as we will see below, if capital gains of $250,000 or less are realized on or after June 25, 2024, the cost of realizing those gains in a corporation versus personally goes up significantly.

Gains up to $250,000 in a year

For capital gains up to $250,000 in a year, starting on June 25 the capital gains inclusion rate will remain at 50% for individuals, but will increase to 66.67% for corporations. This difference in inclusion rates has an even greater impact on integrated tax rates and tax costs as shown in Figure 4.

Figure 4: Capital gains up to $250,000 – Comparison of 2024 integrated tax rates and personal tax rates, when the shareholder is taxed at the top marginal rate

Region	Integrated tax rate as of June 25, 2024	Top personal tax rate as of June 25, 2024	Tax Savings (Cost)
AB	34.36%	24.00%	(10.36%)
BC	39.41%	26.75%	(12.66%)
MB	38.23%	25.20%	(13.03%)
NB	39.46%	26.25%	(13.21%)
NL	41.10%	27.40%	(13.70%)
NS	40.20%	27.00%	(13.20%)
NT	32.77%	23.53%	(9.24%)
NU	33.49%	22.25%	(11.24%)
ON	38.62%	26.76%	(11.86%)
PE	41.01%	25.88%	(15.13%)
QC	39.13%	26.65%	(12.48%)
SK	35.38%	23.75%	(11.63%)
YT	36.82%	24.00%	(12.82%)

Due to the tax cost in all provinces and territories it's generally better to earn capital gains personally, rather than through a corporation, both before and after June 25. But, for capital gains up to $250,000 in a year, it may be even more desirable to earn those capital gains personally on or after June 25, 2024 due to the significant increase in the tax cost of earning those gains in a corporation.

There is one notable exception. A shareholder who is not US person,[8] and who has a worldwide gross estate exceeding the US estate tax exemption (USD$13.61 million in 2024), may still wish to hold US securities in a Canadian corporation for US estate tax planning purposes, despite the high cost of doing so, to avoid the US estate tax, which can be up to 40% of the fair market value of US-situs assets held on death.

Who will be affected?

While the changes to the capital gains were said to primarily be aimed at high-income Canadians who regularly realize substantial capital gains in a non-registered portfolio each year, they may also affect others. Let's look at a few examples of who else may be impacted by the capital gains tax rate increase.

Individuals with a second home or investment property

Consider someone who is planning to sell a secondary property, perhaps a vacation home or investment property. It's conceivable that the gain on that property could be more than $250,000, meaning that if the property is sold anytime after June 25, 2024, and the principal residence exemption isn't claimed, any gain in excess of $250,000 would be taxed at a higher rate.

[8] US citizens and green card holders are usually US persons. This strategy is generally not recommended when shareholders are US persons, due to US tax rules for passive income earned in a non-US corporation.

Suppose Alexi lives in Alberta and inherited a family vacation home 20 years ago when it had a fair market value (FMV) of $200,000, which is Alexi's adjusted cost basis (ACB). The home has a FMV of $700,000 in 2024, so the capital gain would be $500,000. Let's assume Alexi has no other capital gains. If the home is sold before June 25, Alexi's tax bill would be $120,000[9]. If sold after June 24, 2024, Alexi's tax bill would rise to $140,000[10], a $20,000 increase.

Planning tip

If property is owned jointly with a spouse or partner[11], where each person contributed equally to the purchase of that property, then each spouse or partner should have access to $250,000 of gains annually at the lower 50% inclusion rate. Upon sale, the 50% inclusion rate may apply for up to $500,000 ($250,000 for each spouse) of capital gains.

Lifetime capital gains exemption

Individuals who sell their qualifying small business corporation (QSBC) shares, or qualified farm or fishing property (QFFP), may be able to take advantage of the lifetime capital gains exemption (LCGE), which will soon be enhanced. The Budget announced that the LCGE will increase to $1,250,000 from $1,016,836 as of June 25, and will be indexed annually starting in 2026. This means that, as of June 25, the first $1.25 million of capital gains realized on qualifying properties during your lifetime will not be taxed. Regular tax rates for individuals apply to total capital gains, after applying the LCGE.

Suppose Rendi, who lives in B.C. and has never claimed the LCGE, owns QSBC shares with a value of $3 million and nominal ACB. If Rendi sells the shares before June 25, the tax bill will be about $530,000[12]. If Rendi sells the shares in 2024[13] on or after June 25, the tax bill will be about $602,000[14], a tax increase of about $72,000. Even though the LCGE will increase as of June 25, it won't be enough to offset the additional tax from the higher, 66.67% inclusion rate.

Estates

In the year of death, there's a deemed disposition of all your capital property at fair market value. This means that if there's a sizable non-registered investment portfolio, or second property, with some accrued gains on the day you die, the 66.67% inclusion rate will apply for any capital gains above $250,000. The capital gains would be calculated as shown in the examples above.

If your surviving spouse or partner is a beneficiary of your estate, the assets can generally be transferred to your spouse or partner at ACB. It may also be possible for your estate representative to elect out of this rollover for certain assets, to control the capital gains that are realized. This may help limit the amount of capital gains that are realized on your death, so they can be kept under $250,000.

Note that many Canadians may have all their financial assets in registered plans[15] and their principal residence, and for these people there may be minimal capital gains in non-registered accounts that would be subject to tax at the higher 66.67% inclusion rate (for gains over $250,000).

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9 Calculated as a $500,000 ($700,000 minus $200,000) capital gain, taxed at 24.00%.

10 Calculated as a $500,000 ($700,000 minus $200,000) capital gain, with the first $250,000 taxed at 24.00% and the remaining $250,000 taxed at 32.00%.

11 In this report, spouse refers to someone to whom you are legally married. Partner refers to a common-law partner under the Income Tax Act, which means someone who cohabits with you in a conjugal relationship, provided the two of you have cohabited for the past 12 months or are jointly parents of a child.

12 Calculated as $1,983,164 ($3,000,000 minus $1,016,836), taxed at 26.75%.

13 Starting in 2025, it may also be possible to claim the Canadian Entrepreneurs' Incentive that was announced in the 2024 federal budget.

14 Calculated as $1,750,000 ($3,000,000 minus $1,250,000), with $250,000 taxed at 26.75% and the remainder of $1,500,000 taxed at 35.67%.

15 The federal government's Budget Plan 2008 estimated that TFSAs, in combination with existing registered plans, would permit over 90% of Canadians to hold all their financial assets in tax-efficient savings vehicles.

Should you proactively crystalize gains?

Perhaps one of the biggest planning opportunities to consider is whether to trigger capital gains prior to June 25, 2024, to take advantage of the 50% inclusion rate on an unlimited amount of capital gains.

Individuals won't need to trigger gains before June 25 if total capital gains in the future will be less than $250,000 each year (or between June 25, 2024 and December 31, 2024), since they'll still be able to take advantage of the 50% inclusion rate. You'd only need to consider triggering capital gains before June 25 if you expect to realize more than $250,000 of total capital gains in a future year, or if the gains are expected to be realized in a corporation. In those situations, you may want to consider selling capital property before June 25 if you don't expect future earnings on the property to exceed the increase in tax when you later sell it.

For example, let's say you're an individual in Ontario. You pay tax on capital gains at the top tax rate and have assets that you expect will generate over $250,000 annually. You're trying to decide whether to sell or hold a property with a current capital gain of $100,000. If you sell before June 25, you'd pay tax of $26,760 (at 26.76%). If you continue to hold the property, the tax bill would increase by $8,930 to $35,690 (at 35.69%) when you later sell it. To make it worthwhile to hold the property, you'd need to earn enough additional after-tax income to offset the additional tax of $8,930.

If the property earns only capital gains, the amount of time needed to reach the break-even point (earn an additional $8,930, after tax) depends on the rate of growth for the property. For example, if you expect the property to appreciate by 6% annually, it would take about 8 years.

Figure 3 shows the number of years it would take to reach the break-even point using various growth rates. This applies in all provinces and territories, for capital gains earned personally or in a corporation.

Figure 3: Number of years to the break-even point when property earns only capital gains

Growth rate (annual appreciation)	2%	3%	4%	5%	6%	7%	8%
Number of years	21	15	11	9	8	7	6

Corporations

If you earn capital gains in your corporation, you would need to consider both corporate and personal levels of tax. As a result, the break-even analysis may be more complicated than for individuals, who face only one level of tax. Professional tax advice should be sought in this area to determine whether triggering capital gains in your corporation before June 25, and prepaying corporate tax, makes sense in the long run.

The bottom line on crystalizing capital gains

When deciding whether to sell capital property personally or in a corporation before June 25, 2024, keep these points in mind:

- You'd only need to consider triggering capital gains before June 25 if you expect to realize more than $250,000 of total capital gains in a year after June 25, or if the gains are earned in a corporation.
- Consider selling any capital property before June 25 if you think you'll ultimately sell it before the break-even point, when additional future earnings on the property will equal the increase in tax when you later sell it.
- If the property earns only capital gains, the number of years it would take to reach the break-even point depends on the growth rate, as shown in Figure 3.
- You should consult a tax adviser for further analysis before crystalizing any capital gains. This is particularly important if capital gains will be earned in a corporation, or if you could be subject to Alternative Minimum Tax (as discussed below), since the analysis is more complicated.

Alternative Minimum Tax (AMT)

Both the 2023 and 2024 federal budgets proposed changes to the AMT system starting in 2024. Under the proposals, a minimum tax rate of 20.5% would apply for high income earners with certain types of income, deductions or credits. In addition, under the revised AMT rules, 100% of capital gains are taxable. If you have more than $173,205 of taxable income in 2024, the AMT may affect the tax you'll pay if you have significant capital gains taxed at the 50% inclusion rate. Realizing gains intentionally, as discussed above, could be less beneficial if it triggers AMT.

A final note

Although the proposals are targeted at high-income taxpayers, there are other Canadians who could be hit with increased taxes as a result. That's left many Canadians wondering how their own situations could be affected by the proposed changes for capital gains. To truly understand how the changes may impact you, be sure to consult with your tax adviser, who can perform an analysis that's tailored for you.

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