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Canada’s 2024 Federal Budget: The Time Is Now ... to Lock in Lower Tax Rates

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Tax practitioners will be busy in the coming weeks. Usually, in the lead-up to the issuance of the federal budget, released this year on April 16, 2024 (“Budget 2024”), there is speculation that the capital gains rate will be increased, and taxpayers often undergo transactions to “lock in” the lower rate. The lead-up to Budget 2024 was no different. This time, however, the capital gains inclusion rate is increasing, albeit not until June 25, 2024. That means that Canadians have roughly two months to crystalize, if they so desire, any capital gains to lock in the current rates.

Here are three things that everyone needs to know about Budget 2024:

1. An Increase to the Capital Gains Inclusion Rate

Currently, when a person sells capital property, only 50% of the capital gain is included in their income. Budget 2024 proposes to increase this capital gains inclusion rate from 50% to $66^{2/3}$% on capital gains realized on or after June 25, 2024. For individuals, this rate change occurs after $250,000 in realized capital gains, but for corporations, there is no such relief. As a result of these changes, capital gains earned by individuals in Ontario — in excess of the $250,000 threshold — who are subject to the top marginal rate will be subject to 35.69% tax instead of 26.76%.

There is a history in Canada of changing the capital gains rate, the most recent being a change from $66^{2/3}$% down to 50% in 2000. The June 25 deadline was designed to give the government a financial boost by incentivizing people to trigger capital gains to lock in the lower rate rather than continue to hold capital property until a desired sale. Certainly, this change is going to be met with criticism, although the government insists that the changes will only affect a small number of individuals and corporations. At first glance, the increased tax on corporations will concern many who are focused on the lack of productivity in Canada. In addition, there is now a disincentive for individuals to hold capital assets through a corporation, which goes directly against the integration principle, which provides that these decisions should be neutral.

2. Changes to the Lifetime Capital Gains Exemption

Presumably, to counteract the changes to the capital gains inclusion rate, the lifetime capital gains exemption (the “LCGE), which provides an individual with a lifetime tax exemption for capital gains realized on the disposition of certain Canadian corporate shares, will be increased for dispositions that occur on or after June 25, 2024. Today, the LCGE is $1,016,836, and this will be increased to apply to up to $1.25 million of eligible capital gains. The indexing for inflation will resume in 2026.

3. The Introduction of the Canadian Entrepreneurs' Initiative

Budget 2024 also proposes a new carve-out for entrepreneurs of certain types of businesses, protecting the disposition of some shares in specific instances. Beginning with sales that occur on or after January 1, 2025, the Canadian Entrepreneurs' Initiative (the "Initiative") would apply to up to $2 million in capital gains per individual over a lifetime and would see proceeds taxed at 33.3%. Notably, the conditions for the Initiative mirror the conditions necessary for the LCGE. However, there are some notable differences. Besides some time and percentage ownership restrictions, the most glaring difference between the LCGE and this Initiative is that the Initiative does not apply to interests in professional corporations, consulting or skill-based corporations, or corporations that carry on activities in the financial, insurance, real estate, food and accommodation, arts, recreation, or entertainment sectors. Clearly, the government is seeking to incentivize only certain industries to the detriment of others.

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