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Personal Newsletter from Nicole Deters, Harbourfront Wealth Management – Gilman Deters Private Wealth

SUMMER 2024

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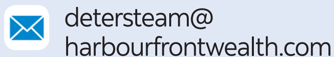
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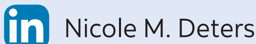
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The Largest Wealth Transfer in History is Here

It's been termed the "greatest wealth transfer in history." As the last of the Baby Boomers reach the age of 60 this year, and the oldest approach 80, an estimated $1 trillion of wealth has begun to change hands.[1]

The boomers are now commonly referred to as the "luckiest generation" due to their significant leap in prosperity, benefitting from substantial price growth in the housing and financial markets. Consider that the average price of a Canadian home has risen about 800 percent since 1981, when most boomers were in their 20s and 30s — the prime years for household formation.[2] At that time, a house cost around $75,000,[3] though we mustn't forget that a five-year mortgage back then reached a crippling 21 percent! Over the same period, the S&P/TSX Composite Index Total Return has risen by more than 3,000 percent.[4]

While much of this wealth is anticipated to be passed along, some suggest that we are instead witnessing a shift in the spending habits of the boomers. The ***Wall Street Journal*** published an article late last year suggesting that U.S. boomers were the "economy's silver bullet," with increases in spending by retirees propping up economic growth to largely avert a recession.

Regardless of the extent to which wealth will transfer, the inevitable generational shift should prompt questions about our own wealth management. Are you prepared for this transition?

According to recent surveys, we may not be doing the best job. Studies continue to show that around one-half of Canadians still don't have a will; surprisingly, this hasn't changed over many decades. Only one-quarter of us appear to have a plan for our assets if we are unable to make financial decisions, and only 21 percent have had detailed discussions with beneficiaries or executors of their will.[5] How about you?

Even if we do have a detailed plan to pass along our assets, many of us do not feel confident in the next generation's ability to preserve or grow their inheritance.[6] The old "shirtsleeves to shirtsleeves" adage still holds true, suggesting that wealth gained by one generation is often lost by the third. The first works hard to accumulate wealth, the second benefits and maintains it and the third, having not experienced the hardships of wealth creation, ends up losing it. Planning ahead may be one way to mitigate this risk. Whether it is working alongside you to facilitate a generational wealth transfer plan or assisting younger folks with wealth management education or investing support, I am here to help.

Summer often affords us a bit more downtime, making it an opportune time to assess your own wealth transfer plan. If you've yet to give your estate plan the attention it deserves, why not make this a priority? It has the potential to enhance your overall wealth management and can be one of the greatest gifts you leave for your loved ones.

1. https://financialpost.com/personal-finance/retirement/canadian-inheritances-could-hit-1-trillion-over-the-next-decade-and-both-bequeathers-and-beneficiaries-need-to-be-ready; 2. Based on CREA April 2024 average national home price of $703,446 and 1981 price of $75,000. These figures are not adjusted for inflation, however consumer prices have risen about 200 percent over those 43 years; 3. https://policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2010/08/Canadas%20Housing%20Bubble.pdf (page 4); 4. S&P/TSX Composite Total Return Index 1/31/81: 2,658.85 and 1/31/24: 84,500.02; 5. https://www.ig.ca/en/media-room/media-releases/ig-estate-planning-study-despite-aging-population-most-canadians-lack-estate-plan; 6. https://financialpost.com/personal-finance/family-finance/high-net-worth-families/most-high-net-worth-individuals-lack-inheritance-plan-despite-largest-transfer-of-wealth-coming-study

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Planning Ahead: A Rising Capital Gains Inclusion Rate*

It has been over 20 years since we've seen changes to the capital gains tax. Since late 2000, 50 percent (1/2) of realized capital gains have been subject to tax. As of June 25, 2024, the inclusion rate increases to 66.67 percent (2/3) for corporations and trusts, and on the portion of capital gains realized in the year that exceed $250,000 for individuals.* The table shows the impact on a capital gain of $500,000 for an individual (assuming no other gains). Are there ways to manage the potential tax bite? Here are a handful of ideas:

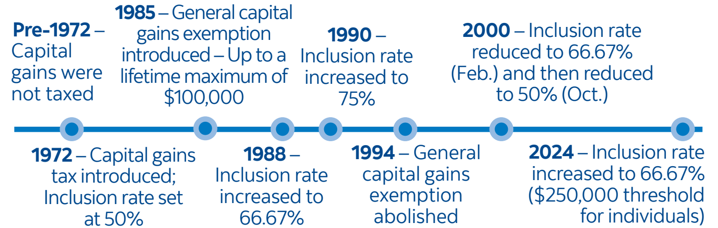
Weigh the benefits of a lower inclusion rate — Tax deferral is commonly viewed as a way to create greater returns since funds that would otherwise go to pay tax can remain invested for future growth. However, individuals may wish to evaluate the possibility of accelerated taxation at a lower rate versus deferred taxation at a higher rate: a higher inclusion rate for gains over $250,000. For example, based on a capital gain of $100,000 and a marginal tax rate of 48 percent, an investor would save $8,000 in taxes by realizing a gain at the lower inclusion rate. Yet, this comes at the cost of "pre-paying" $24,000 in capital gains tax today. If this amount was invested with a return of 6 percent per year, it would take 7 years of tax-deferred growth, based on a 2/3 inclusion rate, to beat the $8,000 in tax savings.

Spread gains over multiple years — If possible, consider realizing gains over multiple years to take advantage of the lower inclusion rate (under $250,000) versus a larger realized gain in a single year.

Crystallize gains — Deliberately selling and rebuying stocks to trigger a capital gain ("crystallizing") can reset the book value over time. This strategy, often used in years when an investor is in a lower tax bracket, may help to capitalize on the lower inclusion rate each year.

Plan to cover increased tax liabilities — Plan ahead for an increased tax liability. The use of insurance or other planning techniques may be considered to cover the eventual higher tax liability, such as for the transfer of family property.

A History of Capital Gains Tax in Canada



Source: "A Primer on Capital Gains Taxes in Canada," CBC, 10/18/2000.

Donate securities — Assuming new rules apply to the deemed disposition of assets at death, if you're considering donations in estate planning, consider the use of publicly-listed securities to a registered Canadian charity as any accrued capital gain is excluded from taxable income and a donation receipt equal to the value of the donated securities is received.**

How Much More For a $500,000 Gain?

Province	Tax Rate on Capital Gain*		Additional Tax
	1/2 Inclusion	2/3 Inclusion	
BC	26.75%	35.67%	$22,292
AB	24.00%	32.00%	$20,000
SK	23.75%	31.67%	$19,792
MB	25.20%	33.60%	$21,000
ON	26.76%	35.69%	$22,304
QC	26.66%	35.54%	$22,213
NB	26.25%	35.00%	$21,875
NS	27.00%	36.00%	$22,500
PEI	25.88%	34.50%	$21,563
NL/LB	27.40%	36.53%	$22,833

*For individuals based on top marginal tax rates, 01/01/24.

Business owners — Evaluate whether certain assets should be held in the corporation or owned personally. For corporations, there is no $250,000 threshold; realized gains are taxable at a 2/3 inclusion rate. The use of corporate-owned insurance or an individual pension plan may be considerations for a business' tax strategy. Plan ahead to use deductions, such as the lifetime capital gains exemption, to reduce taxes payable on the disposition of qualified shares.

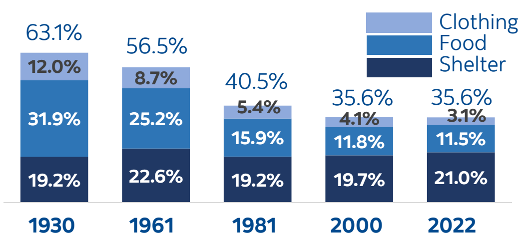
As always, seek advice from a tax expert regarding your situation.

*Note: At the time of writing, legislation has not been enacted.
**If managing over a lifetime, this applies to individuals not affected by the AMT.

The Increasing Cost of Living: A Taxing Time

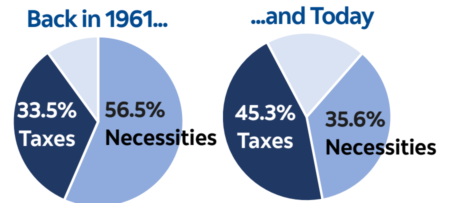
While the growing cost of living continues to be top of mind for many, a differing perspective has emerged on our cost pressures. Despite the rising prices we see today, the proportion of income spent on necessities like food and clothing has declined substantially over time. In 1961, Canadians allocated one-third of family income to these costs; today, they make up less than 15 percent.

% of Income Spent on Necessities, 1930 to Today



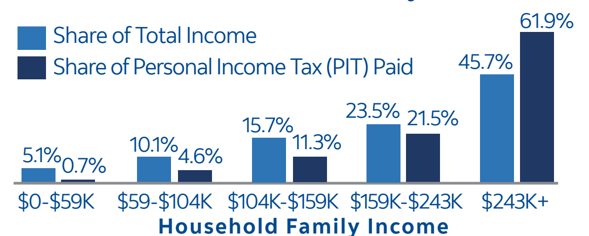
Instead, a recent report suggests that the burden of escalating expenses weighs more heavily on taxes. The Canadian Consumer Tax Index tracks family expenditures on necessities (food, shelter, clothing) and taxes. Today, the average Canadian family spends 45.3 percent of income on total taxes (pie chart). Since 1961, there has been a 2,778 percent increase in the taxes we pay, far outpacing the 863 percent increase in the Consumer Price Index that measures changes in prices.[1]

Average Canadian Family's Tax Burden vs. Necessities, 1961 and 2022



Who shoulders the heaviest tax burden? When comparing the share of tax paid to share of income, the highest-income earners do. The top 20 percent of income earners (family income over $243,000) pay 61.9 percent of personal income taxes (PIT) but represent only 45.7 percent of total income. Every other income group pays a smaller share of PIT versus share of income.[2]

Share of PIT Paid & Income Earned by Quintile 2023



1. https://www.fraserinstitute.org/studies/taxes-versus-necessities-of-life-canadian-consumer-tax-index-2023-edition; 2. https://www.fraserinstitute.org/studies/measuring-progressivity-in-canadas-tax-system-2023

Your Home Is Not a Retirement Plan

Summer — the season for home sales — is here! With real estate prices continuing their rise, it may be tempting to see your home's value as a potential source of retirement income. However, when supporting clients in planning for retirement, it's generally not recommended to factor in a home's value as a primary part of that plan. While some homeowners consider downsizing as a way of unlocking retirement funds and others may look to borrow against their homes, there are reasons to exercise caution in relying on home equity for retirement. Here are a handful:

You may not move — If you are planning to sell your home and downsize, there is a good chance you may eventually decide not to move. Recent reports suggest seniors are now less likely to sell their homes before age 85; the sales rate among those ages 75 or more has been trending downward since the 1990s.[1] This may not be surprising. Selling a lifelong home can be more emotionally difficult than many anticipate. Many seniors remain in their dwellings to stay close to family, friends or their community and to maintain their sense of independence. Some have instead chosen to "downsize from the inside," using only a portion of their homes to reduce costs like heating.

Low housing supply — Even if you do plan on downsizing or renting, will you be able to find suitable accommodation? While selling a home in this market may be easy, finding a suitable replacement may be more challenging given low inventories, including rental properties.

Moving can be expensive — The costs associated with moving homes may be greater than anticipated: real estate fees, lawyers' fees, land transfer tax, staging and other expenses can add up to be significant. There may also be other unanticipated expenses that come with a new dwelling, such as maintenance, renovations and, if you end up in a condo, monthly management fees. All of these costs can erode the net financial gain by downsizing.

Higher interest rates — Recent reports suggest that around 25 percent of retirees carry mortgages as individual wealth has shifted to real estate.[2] Many mortgage holders have seen mortgages reset at higher rates, leading to lower disposable income, especially for those on fixed incomes. While it's possible to access home equity for retirement, consider that this has become more costly with rising rates. Reverse mortgages, although not common in Canada, may allow you to borrow against home equity (usually up to 55 percent) with minimal proof of income. Yet, reverse lenders charge very high rates and there are few large providers. More commonly, a home equity line of credit, often secured prior to retirement when income is high, allows you to draw on the line as needed and pay interest only on what you borrow.

These are just a handful of reasons to exercise caution when considering home equity for retirement. For a deeper discussion on this, or any other aspects of retirement planning, please call the office.

1. "Canadian seniors not downsizing, partly owing to lack of options," S. Peesker, Globe & Mail, 02/12/24; 2. "Wealth tied up in real estate can hurt your retirement," R. Carrick, Globe & Mail, 11/30/23, B10.

Timing Is Everything: Why Some Regret Taking Early CPP Benefits

With most Canadians choosing to start their Canada Pension Plan (CPP) benefits early, there's been growing attention to the potential advantages of waiting. Recall that starting CPP benefits before age 65 (as early as 60) decreases payments by 0.6 percent per month, whereas delaying beyond 65 increases payments by 0.7 percent per month, up to 42 percent (age 70). Actuarial studies continue to show that many people are better off delaying benefits as the break-even age* is often below the average life expectancy. Those who live past the break-even age will receive a higher overall benefit by waiting.

Of course, this decision is influenced by various factors beyond just life expectancy, such as immediate income needs. As more Canadians work past age 65, the impact of retiring early, or late, should also be a consideration. Working past age 65 and delaying benefits can lead to a potentially greater benefit. This is because CPP benefits are generally calculated using the best 40 years of income, usually between ages 18 and 65. Since lower-earning years tend to be at younger ages when first starting a career, extending the working years past age 65 may add higher-earning years to the calculation, thus increasing the benefit.

CPP Timing: Change Your Mind?

If you start benefits and change your mind, you can cancel CPP within 12 months of its start. The cancellation must be in writing to Service Canada and you must pay back the benefits received.

The good news? It doesn't work the other way: Any low-earnings years after age 65 will have no effect on the benefit calculation. Yet, if you retire before 65 and wait to take benefits, the zero-earnings years can negatively impact the benefit. Retiring at 60 and waiting to collect CPP at 65 could potentially add five zero-earning years to the calculation.

Regrets, We've Had a Few...

Indeed, the old words of Frank Sinatra may be a reminder to carefully consider the timing decision. A recent article in the Globe & Mail highlighted Canadians who had "regrets" after starting benefits early:[1]

Impact on survivor benefits — One widow discovered that starting her own CPP reduced her maximum entitlement from survivor benefits. She was also unaware that survivor benefits would change when she turned 65 and hadn't considered the impact of deferring her own benefits beyond that age.

Legacy considerations — A man who wasn't in immediate need of the funds wished he had delayed his CPP after realizing how much more he could have left for beneficiaries. One study suggests that taking CPP at age 60 instead of 70 can forgo $100,000 of lifetime benefits.[2]

Inflation adjustments — Another retiree noted that had he waited, the multiplier for starting later would have further enhanced the inflation-indexed benefits.

Returning to work — One man who began receiving CPP at 60 and retired at 63 decided to return to work. He regretted starting early due to the taxes paid on CPP income during his subsequent employment.

*The age at which total benefits received by delaying payments exceed total benefits received by starting payments earlier. 1. https://www.theglobeandmail.com/investing/globe-advisor/advisor-news/article-these-canadians-wish-they-had-waited-to-take-their-cpp-benefits-heres/; 2. https://www.fpcanadaresearchfoundation.ca/media/5fpda5zw/cpp_qpp-reseach-paper.pdf

Oh, Canada! We've Got a Productivity Problem

"Why isn't Canada an economic giant?" This was the headline of a Financial Times article highlighting our "vast potential" but suggesting we "underperform on the global stage."[1] It's a valid perspective. With the second-largest land mass globally and an abundance of resources, including oil and natural gas, minerals critical to the green energy transition and a strong agricultural industry, "by any measure, Canada's geography suggests it could be an economic powerhouse."[1]

We also boast a highly educated population and a strong standard of living. Yet, despite these advantages, Canada has had little productivity growth over recent decades, falling second to last among G7 nations, ahead of only Italy. Canadian workers produce only 70 percent of our U.S. counterparts' output, based on 2022 figures.[1]

Productivity is crucial for economic growth, as reflected in Statistics Canada's latest report of real GDP per capita now lagging seven percent below its long-term trend.[2] The Bank of Canada recently voiced its concerns, suggesting we have a "productivity problem" and highlighted three elements key to driving highly productive economies: i) capital intensity, including access to better machinery and new technologies to improve efficiency and output; ii) labour composition, improving skills and training; and iii) multi-factor productivity, using capital and labour more efficiently.[3]

How can we improve our productivity problem? Two recent op-eds published in the Globe & Mail provide some notable perspectives:[4]

- **Encouraging capital investment**, including in machinery and equipment, as well as intellectual property and skills training for workers to drive output. This may be fostered by lowering barriers to capital formation, such as tax rates.
- **Increasing competition by loosening restrictions**, including foreign investment controls, interprovincial trade barriers, foreign entry constraints and protectionism, as examples.
- **Reassessing current government spending**, including evaluating subsidies for industries, research and innovation that have not contributed to growth.
- **Increasing the supply of labour.** Immigration has helped, as have changing demographics that have increased the participation of women over recent decades. However, when normalizing labour participation as a proportion of the total population, employment rates have dropped from 75 percent to around 61 percent, a similar level to 1988.

Lessons from the Past: From (Almost) Worst to First

Let's not forget that it was just 30 years ago when Canada was referred to as "an honorary member of the Third World." At that time, we had the second worst fiscal position of the G7 (Group of Seven of the world's advanced economies), suffering from a "vicious debt circle" — ironically, similar to today, only Italy was worse.[5]

Yet, 1994 would be the turning point. Then-Prime Minister Jean Chretien and Finance Minister Paul Martin orchestrated one of the most dramatic fiscal turnarounds in history, with the greatest reduction in government spending since post-WWII. Canadian debt shrank from 68 percent of GDP in 1995/96 to 29 percent by 2008/09 and the budget was in the black for 11 consecutive years. Our fiscal position became the best of the G7. While it wasn't without significant sacrifice that the deficit was finally controlled, it is notable that Canada did not fall into recession during this time. In fact, "after wrestling the deficit to the ground," what followed was "the payoff decade" when Canada outperformed the rest of the G7 in growth, job creation and inward investment.[5]

History is a reminder that profound change is possible, perhaps a lesson relevant to the situation in which we find ourselves today. While there's much work to be done, leadership from the top can drive transformation. Now it's time for us to get started.

1. https://www.ft.com/content/67e97cc4-6ab0-4e78-b4a8-7c97b8e52ada; 2. https://www150.statcan.gc.ca/n1/pub/36-28-0001/2024004/article/00001-eng.htm; 3. https://www.bankofcanada.ca/2024/03/productivity-problem/; 4. https://www.theglobeandmail.com/opinion/article-what-might-a-serious-growth-agenda-look-like-more-labour-more-capital/; https://www.theglobeandmail.com/business/commentary/article-the-budget-needs-bold-change-to-fix-canadas-falling-productivity/; 5. https://financialpost.com/uncategorized/lessons-from-canadas-basket-case-moment

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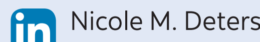

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