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The Krygier Report

An exclusive newsletter from Mark J. Krygier, Senior Portfolio Manager | June 2024 www.krygierwealthmanagement.ca

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Gain problems? This is no time for dieting!

For many years I have been riding my bike in an annual charity event to raise money for a local school for physically and mentally challenged children called *Kayla's Childrens' Centre* or *KCC* (stay tuned for my fund-raising email!). On several of the rides the organizers brought in some professional riders to ride alongside us amateurs to generate a little excitement. A few years ago, the organizers arranged a Zoom video conference call in which one of the pro-riders provided us with tips she had gleaned from experience, to help us better prepare for the upcoming ride. One of these tips stuck out in my mind. She stressed the importance of staying well hydrated while exerting oneself for several hours, as well as the need to consume calories to offset the calories being burned. While in general a healthy diet is an important part of one's overall health plan and weight loss strategy, but during a long bike ride she stressed, "This is no time for dieting!" I believe this sound advice, to effectively focus on the big picture, can be applied in many other situations as well.

The Federal Government in Canada recently introduced legislation to increase the Capital Gains inclusion rate, effective if passed as of June 24, 2024. If passed, instead of the current inclusion rate of 50% of the capital gains one has earned on stocks, real estate holdings, etc. being included in one's annual taxable income, the new rate will be 66% of the gains – effectively increasing one's tax burden by 8% or more on gains obtained from investing. For individuals, this increase will only apply for gains over $250,000 in a given calendar year. However, for corporately held investments it will apply to every dollar of capital gains "realized" after June 24, 2024. With the proliferation of Investment Holding companies as well as Professional Corporations for dentists, doctors, lawyers and accountants, this will increase the tax burden on many Canadians. Not surprisingly, we have received several calls from both clients and their accountants to try and determine what should be our strategy with regards to crystallizing or "realizing" capital gains both in the short and the long-term. After having had several conversations with the accountants of some of our highest net worth clients, these are the conclusions we have drawn:

A) **<u>When an investor has short-term needs for liquidity</u>**:

- **a)** Firstly, it is not clear the legislation will pass, as the last attempt to raise the capital gains tax rate was dropped due to strong lobbying efforts from groups such as the Ontario Medical Association.
- **b)** Secondly, even if it passes, following the next Federal election, should the Conservatives gain a majority government perhaps they may revoke the legislation and reduce the capital gains rate back down to the current level?
- **c)** Finally, while minimizing tax is important, like trying to diet as part of a health plan, it is only one factor in managing one's assets. If for instance one intends to trim gains in a portfolio for risk management reasons, or if one has a need to create liquidity in the foreseeable future, then trim gains before June 24th, to lock in today's capital gains rate.

B) **<u>When an investor has no need for short-term liquidity</u>**:

a) If an investor has sufficient cash flow to meet his/her daily needs and has no intentions to make any large capital withdrawals from his/her investments, then the most tax efficient investment strategy may be to simply continue to defer all or most of the gains for as long as possible.

b) A separate reason to consider selling and crystallizing gains early would be if one expects a “deemed disposition” in the foreseeable future, such as an estate liquidation or if one is permanently moving to another country. Everyone should be consulting with their tax professionals to consider all these issues within a broader context.

In the world of will & estate planning we also find examples of where this same logic would apply**.** Firstly, there is a lot of hoopla when it comes to trying to avoid “probate tax” (the cost of having the court system confirm that a will is the last will and testament of a deceased person, so that third parties like banks can rely on it to distribute estate assets without fear of liability from unknown third parties). Everyone needs a properly drafted will (and for those of you who don’t have one yet, <u>please</u> make it a priority on your “to-do” list for this calendar year!), but there is no need to drive oneself crazy in drafting the wills, just to avoid the cost of probate which amounts to a maximum of 1.5% of an estate. Another example is the expectation that one’s relatives – especially if they lack experience in dealing with lawyers, the court system, or government agencies – should be the executors for one’s will. Except in the simplest of estates, the role of executor can be a nuisance and can take a tremendous amount of time, so to expect one’s non-professional relatives to perform this function may be asking too much. What is the cost of a professional executor? Typically, the fee is 1-3% of the value of the estate. Consider that when the after-tax value of an estate is divided amongst several beneficiaries, very little in dollar terms is really being “lost” from the estate to hire a professional. In short, we need to focus on the main task at hand and stop worrying about the minutiae.

Bottom line

The importance of eating healthy and exercising regularly cannot be understated. At the same time, reducing one’s calorie intake when performing excessive exercise can be terribly counter-productive. Likewise, for investors, it is very important to try and achieve the most tax-efficient total returns. However, that goal needs to be considered within one’s overall financial plan. Each investor needs to focus on the big picture and their own particular needs. If you or someone you know wants to discuss tax efficient investing, getting a will and estate plan reviewed, or any other financial issues affecting your “big picture”, contact us to set-up a time to meet by phone, video or an in-person meeting.

Global benchmarks

As of May 31, 2024 (Canadian $Returns – except where noted)

Asset class	YTD	1 year	3 years
S&P/TSX Composite T/R (Canada)	7.6%	17.6%	7.4%
S&P 500 TR - **US$**	11.3%	28.2%	9.6%
NASDAQ Composite - **US$**	11.5%	29.4%	6.8%
MSCI Europe Index Price Return	9.3%	16.9%	5.6%
MSCI Emerging Markets	5.4%	9.9%	-4.9%
China S.E Shanghai A Price Return	4.6%	-5.1%	-5.3%
MSCI World Index Price Return	11.8%	23.5%	9.4%

Asset class	YTD	1 year	3 years
30-year U.S. T-Bond - **US$**	-8.2%	-8.9%	-11.2%
10-year U.S. T-Bond - **US$**	-3.3%	-2.9%	-5.2%
Long GOC Bond (2053)	-8.5%	-4.4%	-7.7%
10-year GOC Bond	-2.9%	-0.2%	-3.1%
5-year GOC Bond	-0.9%	2.2%	-1.5%
3-month CDN T-bill	2.2%	5.1%	2.8%
US$/CDN$ (1.3626)	2.9%	0.4%	4.1%

Source: RBC Capital Markets Quantitative Research

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