A Wealth Tax Proposal

By: Jason Fleming, CPA, CA, M.Acc

Jason is an associate professor teaching at York University's School of Administrative Studies and is the author of *CFE Tax,* 8th edition and *CFE Case Writing,* 2nd edition (Thomson Reuters)

This article proposes a new, administratively simple, wealth tax for Canada. The goals of this tax are to create income for the federal government and reduce the concentration of wealth. Most Canadians will *not* be subject to this tax and unlike current taxes it will be relatively easy to comply with.

Since Canada does not have a gift or estate tax, a new wealth tax, if properly designed and implemented, may be a good idea[1]. Practical suggestions are given such as using cost to value private businesses in order to make compliance straightforward. The tax rate is 1%, with a $20M exemption, to avoid discouraging hard work and success, and to keep wealthy individuals from leaving Canada.

Given the outrageous complexity of Canada's tax system, this wealth tax should only be implemented at the same time as Canada's income tax system is simplified.

Given the outrageous complexity of Canada's tax system, this wealth tax should only be implemented at the same time as Canada's income tax system is simplified and the payroll tax on employers is eliminated. For suggestions on how to simplify our tax system please see: *Tax Simplification Suggestions,* and see: *Tax Robots Not Payroll A Robot Tax Proposal* (Canadaone.com) for why we must eliminate employer payroll tax. Simplifying our tax system and removing payroll tax on employers, will also help keep wealthy Canadians from leaving Canada.[2]

Proposed Wealth Tax

---

[1] The OECD Tax Policy Studies summary No. 26, *The Role and Design of Net Wealth Taxes in the OECD*, says a wealth tax may be appropriate "…for countries that do not levy taxes on inheritances." Note: Canada has a deemed disposition of capital assets owned on death, but does *not* have an estate or inheritance tax.

[2] Canada's 10% federal luxury tax on certain: cars, trucks, aircraft and boats, that began in 2022, could also be eliminated. While the wealthy can afford to pay this luxury tax, it adds a major compliance burden (and tax risk) to car and boat dealerships. Note: when a rich person buys a multi-million-dollar painting, or other luxury items, they do *not* pay this luxury tax; since it only applies to certain vehicles. My proposed wealth tax will apply to all assets and hence the 10% luxury tax can be eliminated.

Individuals resident in Canada for income tax purposes, 18 and older, who own assets above $20M, will pay an annual federal wealth tax equal to 1% of their wealth over $20M. Worldwide assets beneficially owned on December 31st will be subject to this tax. Married couples (legal or common law) can report their assets, along with any assets of their minor children, on one return. Trusts will *not* need to file this return. See Appendix I for a sample, one-page, wealth tax return.

The wealth tax return, and any wealth tax owing, will be due six months later, i.e., due June 30th of the following year. To reduce the compliance burden, only individuals with assets above $15M will need to file the wealth tax return. With married couples, only couples with assets above $30M will need to file.

Married people will each get the $20M exemption, hence for married couples only assets above $40M will be subject to this tax. Children under 18 will have their assets reported on their parent's (or caregiver's) return unless they are emancipated minors, who do not live with a parent (or caregiver), and who are not dependent upon their parent (or caregiver). Emancipated minors will have to file their own return (if *their* assets exceed $15M).

Simplifying our tax system and removing payroll tax on employers, will help keep wealthy Canadians from leaving Canada.

Value of Assets
Assets include all assets beneficially owned, even tax-deferred assets like RRSPs (and TFSAs). Foreign denominated assets will be translated to Canadian dollars on December 31st.

Determining fair market value (FMV) can be challenging and, in order to make this tax administratively simple, the following rules should be enacted to determine asset values:

- Public company investments will be valued at FMV since market value is easily obtainable. The closest prior (monthly) investment statement provided by the financial institution can be used to determine the December 31st FMV. For example, if a bank's statement happens to be dated December 30 and the statement's FMVs are from December 28 closing share prices, then these values can be used as the December 31st FMVs (to simplify compliance). If foreign-denominated assets are translated into Canadian dollars on the financial institution's closest prior investment statement, then these values can be used; otherwise, foreign assets must be converted to Canadian dollars using the December 31st foreign exchange rate(s). Options and other derivatives on public securities, that are reported on investment statements at FMV will be valued at FMV, and included with public company investments.
- Private company investments will be valued at cost. Given the complexity of valuing private equity, and debt, cost will be used instead of FMV. Using cost is essential to make this

wealth tax easy to comply with and easy to audit. While this usually lowers an individual's asset values for a certain period of time, cost will eventually equal FMV. For example, any shares gifted or bequeathed to another person will have an adjusted cost base (ACB), i.e., tax cost, equal to FMV at the time of gift. Hence, the person receiving the shares now owns the asset with a higher cost (i.e., FMV at the time of the gift) and *they* will report this on their wealth tax return.

Options and other derivatives on private securities will be reported at cost, and included with private company investments. Note: employee stock options have no cost when granted, but will have a cost equal to FMV at the time the options are exercised.

- Real estate will be valued at the assessed value for property tax purposes at the most recent property tax bill prior to December 31st. Should a foreign jurisdiction not have property tax assessments, a valuation from a local real estate professional will need to be done.
- Cash, bonds, GICs, T-bills, and similar interest-bearing investments will be valued at cost. The closest prior (monthly) investment statements provided by the financial institution(s) can be used to determine the December 31st cost.
- Personally owned business assets, such as inventory, furniture and equipment used in a business are valued at cost. Internally generated goodwill does not have a cost (and hence will not be included).
- Life insurance policies with a cash surrender value (e.g., whole life, universal life) will be included as an asset at the cash surrender value as reported on the closest life insurance statement prior to December 31st. Term life insurance will *not* be included in the value of an individual's assets (unless it has a cash surrender value). This is due to the difficulty in valuing life insurance. Note: after death the cash paid out to the beneficiary will be included in the assets of that beneficiary and hence will be included in the beneficiary's future wealth tax returns.
- RRSP/RRIF/TFSA assets, and RCA (retirement compensation arrangements) assets will be included in assets (using the above rules, i.e., public company investments are included at FMV). Other pensions, such as arm's length work registered pension plans (RPPs) and the Canada Pension Plan and Old Age Security (or similar foreign pension plans) will *not* be included in the value of an individual's assets due to the complexity of determining FMV. Work RPP assets from a non-arm's length employer will need to be included in assets. The most recent actuaries' report or financial institution's investment statements, prior to December 31st, can be used to value the RCA or non-arm's length RPP (with public company investments included at FMV).

- A personal trust's/partnership's assets will be included in the beneficiaries'/partners' assets, based on their share, as per above (i.e., public company investments are included at FMV while private company investments are included at cost). With an RESP, the child's trust assets will be included in the parent's return when the child is 17 or younger (as discussed

above), and will be included in the child's return once the child turns 18 (if the child has more than $15M in assets).

- Automobiles and listed personal property (such as art and jewelry) will be included in assets valued at cost. The value of most personal effects (such as home furniture, clothes, etc.) that are considered personal use property for income tax purposes will be ignored, i.e., will not be included in assets. Your home, and other real estate, is included in assets as per above.
- Some complexities are discussed in Appendix II.

Since only individuals with more than $15M in assets need to file a wealth tax return, it should be relatively easy for the Canada Revenue Agency to audit the small number of returns.

Cost

Cost will be the higher of: (a) the actual cost paid by the taxpayer (in cash or assets); and (b) the deemed cost for income tax purposes. Cost will *not* be reduced by any capital cost allowance, depreciation or asset impairment(s). Since cost is readily available, using cost when FMV is difficult to ascertain is essential for reducing the compliance burden.

For example, if an individual transfers $100M of public company stock to a private company using a tax-free rollover (e.g., section 85 of the Income Tax Act) and receives private company shares, and elects at a lower value of say $20M, then the cost of the new private company shares, for wealth tax purposes, will be the higher of: (a) the actual cost paid (i.e., $100M paid in public company shares); and (b) the deemed cost for income tax purposes (i.e., the $20M elected amount). Hence in this example, the cost will be $100M for wealth tax purposes.

Liabilities

Secured debts can be subtracted from the FMV of assets to determine the net assets subject to tax. Only debts owing by the taxpayer (or spouse or minor child) that are secured by assets that are included on his/her wealth tax return, can be subtracted when computing net assets subject to the wealth tax.

Other liabilities will *not* be subtracted from assets. The large exemption will help offset some of a wealthy individual's non-secured liabilities (which are not subtracted from assets).

Exemption ($20M)

A large exemption, i.e., $20M, is needed to have administrative simplicity, i.e., only the wealthy will need to pay this tax, and to avoid discouraging hard work and savings. Building up wealth is good and should be encouraged. However, money is needed to fund government programs and the wealthy can afford to help fund those programs. A 1% wealth tax, with a $20M exemption, can bring about significant revenues (as discussed below).

Since only individuals with more than $15M in assets need to file a return, it should be relatively easy for the Canada Revenue Agency (CRA) to audit the small number of returns to ensure compliance.

While annual indexing for inflation should not occur so round numbers can be used, approximately every 5 to 10 years the exemption should be increased to account for inflation. For example, in 5 to 10 years the $20M exemption will likely need to be raised to $25M.

The proposed wealth tax will raise billions of dollars of much needed revenue for the federal government each year and will be relatively easy to comply with and administer.

Tax Rate (1%)

While governments have a habit of increasing taxes when they want to increase spending, this new tax should clearly state that the rate will never rise above 1%. The wealth tax rate should never increase above 1% for the following reasons:

- One percent is not really a small number when you consider that this tax is paid every year. Hence, 1% of the FMV of assets, each year, can add up to significant tax.
- A higher rate will lead to more planning to reduce this tax, and may cause wealthy individuals to leave Canada taking their much-needed capital and job creating businesses with them.[3]

Administrative Matters

Any wealth tax paid will *not* be deductible for income tax purposes to ensure more funds for government and less concentration of wealth. No instalments will be required for this new wealth tax.

A late filing penalty of 5% of any wealth tax owing, plus 1% for each full month late will be owing (to a maximum of 12 months late), if the return is filed late. Hence, if one year's return is not filed at all, the penalty will equal 17% (i.e., 5% + 12% for each full month late).

Tax Planning

Some wealthy taxpayers will gift assets to reduce their annual wealth tax. Subject to the anti-avoidance rules (discussed in Appendix II), this is allowed, as it will reduce the concentration of wealth, which is one of the goals of this new tax. Note: gifting assets will lead to a deemed disposition at FMV for income tax purposes, which typically leads to income tax owing. Furthermore, the person who receives the gift will now include that asset in his/her annual wealth tax return (if they are an individual resident in Canada with assets above $15M).

While this tax is designed to keep taxpayers in Canada, *if* an individual becomes a non resident of Canada, for income tax purposes, departure tax rules apply, which lead to a deemed disposition of capital assets at FMV (which typically leads to income tax owing).

Examples

---

[3] See the Fraser Institute's "Wealth tax would make Canada's bad situation even worse" (appeared in the *Financial Post*, October 7, 2021) for arguments against a wealth tax.

A married couple with worldwide assets of $50M (net of secured liabilities) would pay the 1% annual wealth tax on $10M of assets (i.e., $50M - $20M - $20M). Hence, this couple would owe $100,000 (i.e., $10M x 1%) of wealth tax for the year.

An individual with worldwide assets of $1B (net of secured liabilities) would pay the 1% annual wealth tax on $980M of assets (i.e., $1B - $20M). Hence, this person would owe $9.8M (i.e., $980M x 1%) of wealth tax for the year.

Tax Revenue Raised

As an approximation of the minimum annual federal revenue raised by this proposed new tax: according to Wikipedia Canada has 64 billionaire families with an average annual wealth of $5B.[4] Hence, each of these families would have, on average, assets of $4.96B (i.e., $5B - $20M - $20M exemptions, assuming they are all married). Each would then pay an annual wealth tax of $49.6M (i.e., $4.96B x 1%).

Just counting these 64 families, this wealth tax would raise annual revenue of $3.2B (i.e., $49.6M x 64). There are many more Canadians with a wealth above $20M who would also pay this proposed annual wealth tax.[5] Hence, significant annual revenue will result.

Deceased Taxpayers

Taxpayers who pass away in the period December 31st to June 30th will have their wealth tax return filing, and payment, deadline extended by six months (i.e., to December 31st). Taxpayers who die prior to December 31 will *not* owe any wealth tax (and will not need to file a wealth tax return) for that particular year.

Conclusion

This 1% proposed wealth tax will raise billions of dollars of much needed revenue for the federal government each year and will be relatively easy to comply with and administer. This tax will also reduce the concentration of wealth. Since only individuals with more than $15M in assets ($30M if married) will need to file, and only taxpayers with more than $20M in assets ($40M if married) will need to pay this new tax, it will *not* apply to the vast majority of Canadians.

The government should simplify the income tax system and remove the employer payroll tax prior to creating this (or any) new tax. The government should also clearly signal that the 1% wealth tax rate will *never* increase, and the $20M exemption will never decrease, so as to avoid discouraging hard work and success, and to avoid encouraging wealthy Canadians to leave Canada.

---

[4] From Wikipedia (October 25, 2023) (https://en.wikipedia.org/wiki/List_of_Canadians_by_net_worth). Data is originally from *Forbes Magazine* from 2021. I converted the U.S. figures to Canadian dollars using a 1.3731 exchange rate (which was the exchange rate on October 24, 2023).

[5] A July 8, 2020 Parliamentary Budget Officer's report *Net Wealth Tax on Canadian Resident Economic Families*, estimates 13,800 Canadian economic families would pay a net wealth tax (on wealth above $20M), and net revenue raised would be $5.6B in 2020-2021.

Appendix I (Proposed 1-page Wealth Tax Return)

Year ___________ **Wealth Tax Return**

Thank you for helping fund Canada's social programs. This return and any tax owing are due by June 30 of the following year. A late filing penalty of 5% of any tax owing, plus 1% for each full month late will be owing (to a maximum of 12 months), if filed late. Report using the closest: investment statements or real estate assessed values prior to December 31st. Cost is the higher of: (a) the actual cost paid; and (b) the deemed cost for income tax purposes. Cost will not be reduced by any capital cost allowance or depreciation. Personal effects (such as furniture, clothes, etc.) that are personal use property can be ignored. If your wealth (line 13) is $15M or less ($30M if married and filing 1 joint return) you do not need to file this return. Report amounts in Canadian dollars.

Name: ________________________ Address: ________________________
SIN: ________________________ ________________________
Spouse's name (if married): ________________________ Spouse's SIN______________________

Assets Owned on December 31st

Report world-wide assets beneficially owned by you, your spouse if married, and your minor children.

Public company investments (e.g., FMV of public: stocks, mutual funds, options and other derivatives, trust or partnership units) ___________ (1)

Private company investments (valued at cost) ___________ (2)

Real estate (including your home, valued at assessed value) ___________ (3)

Cash, bonds, GICs, T-bills, etc. (valued at cost) ___________ (4)

Personally owned business assets (e.g., inventory, equipment; valued at cost) ___________ (5)

Whole-life/Universal-life insurance (valued at cash surrender value) ___________ (6)

RRSP/RRIF/TFSA assets, and RCAs (public co. investments are valued at FMV) ___________ (7)

Personal Trust/Partnership assets (public co. investments are valued at FMV) ___________ (8)

Automobiles and LPP (such as art and jewelry; valued at cost) ___________ (9)

Other assets (Please list ____) ___________ (10)

Assets add lines 1 to 10 ___________ (11)

Less: Secured debts (only report liabilities secured by an asset included above) ___________ (12)

Wealth (subtract line 12 from line 11) ___________ (13)

Exemption $20M (14)

Less spouse's exemption (if married and filing jointly, enter $20M) ___________ (15)

Wealth subject to tax (line 13 minus lines 14 and 15, if negative = $0) ___________ (16)

Wealth tax (1% x line 16) ___________ (17)

Appendix II (Some Complexities)

Trusts and Partnerships

The FMV of a personal trust's assets will be split equally with all the named (income or capital) beneficiaries of the trust, if the trust is discretionary. If the trust is not discretionary, each named (income or capital) beneficiary of the trust will include their share of the trust's assets as of December 31st. Future or potential beneficiaries (e.g., future children) will be ignored. Only specific beneficiaries known (i.e., named beneficiaries) as of December 31st will be included.

In the unlikely situation where there are no named beneficiaries, then the settlor (or settlors) will be deemed to own the assets of the trust (based on respective contributions to the trust).

To simplify reporting and to avoid double counting, a trust's income and capital beneficiaries' share of trust assets will be equal. For example, if a discretionary trust has 3 beneficiaries: A (income), B (capital), and C (both income and capital); then:

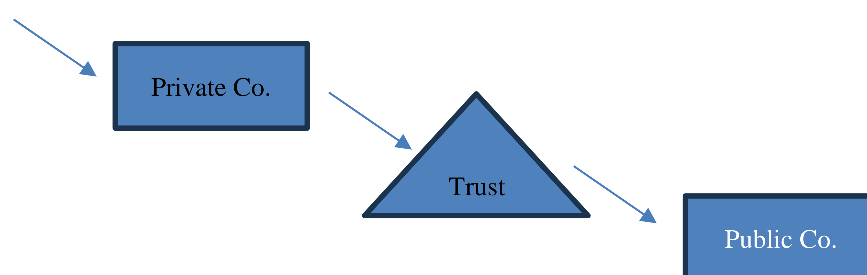
- person A will be deemed to own 50% (of the income) of 200% (i.e., 100% income + 100% capital) = 25% of the trust's assets
- person B will be deemed to own 50% (of the capital) of 200% (i.e., 100% income + 100% capital) = 25% of the trust's assets, and,
- person C will be deemed to own 100% (i.e., 50% income + 50% capital) of 200% (i.e., 100% income + 100% capital) = 50% of the trust's assets

Partnership assets will be deemed to be owned by the partners based on their respective share of the partnership assets (as per above; i.e., public company investments are included at FMV while private company investments are included at cost).

Flow-Through Rules

One complication will arise with complex structures, which are common. For example, Mr. X may own all the shares of a private company (with a low cost), which is a beneficiary of a trust that owns public company shares (with a large FMV), as can be seen in the diagram.

Mr. X



To ensure these structures cannot be used to avoid the wealth tax (by putting public company shares that are valued using FMV into a private company that is valued using cost), flow-through rules are needed.

A chain of any combination, of any number of: non-arm's length private investment holding companies, non-arm's length trusts and non-arm's length partnerships, will need to be looked through to determine the taxpayer's asset values on December 31st (using the rules above, i.e.,

public company investments are included at FMV, real estate is valued using assessed value, and private company investments are included at cost).

Assets will not flow through:

- arm's length entities,
- public companies, or
- private corporations that are not investment holding companies.

An investment holding company will be defined as any private company with a FMV of public investment assets, or real estate investments, that is more than 50% of the company's total assets on December 31st. A private company with 50% or more active business assets will *not* be considered an investment holding company. Hence, private company businesses will not be subject to this flow-through rule (unless their business assets are less than 50% of their total assets). The assets of a private company that is not an investment holding company will not flow through.

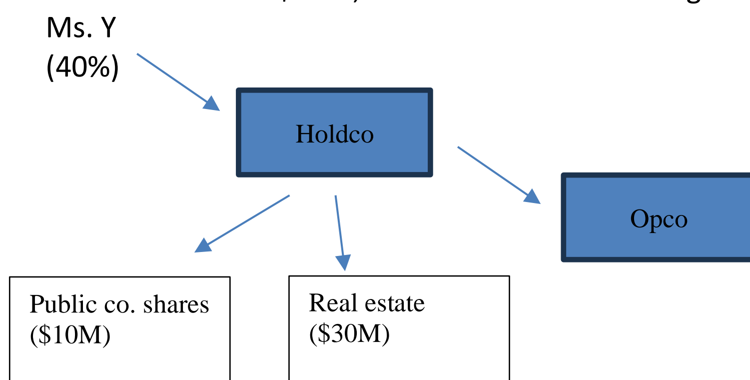
Examples of Flow-Through Rules

1) Mr. X's only asset is 80% of the shares of a private company that is running an active business. The private company is also a beneficiary of a trust (or a partner in a partnership) that owns public company shares worth $1B. As long as the FMV of the private company's business assets are 50% (or more) of its total assets, on December 31st, Mr. X's private company shares will be included in his wealth tax return at his cost of his private company shares. No complex flow through is required.

2) The facts are the same as in (1) except now the private company's assets are mostly investment assets. Starting at the bottom of the diagram, the $1B worth of public company shares owned by the trust would flow through to the private company as discussed above. Hence, if the private company is the sole beneficiary of the trust, it would be deemed to own all of the public company shares (owned by the trust). These public company shares would flow through the private company (for wealth tax purposes) and Mr. X will be deemed to own 80% of the public company shares (since he owns 80% of the private company). Hence, for Mr. X's wealth tax for the year, he would report $800M of public company investments, i.e., 80% of $1B. Other investment assets of the trust, such as other private company investments owned by the trust will also be flowed through to Mr. X (at cost) in the same way.

3) Ms. Y's only asset is 40% of the shares of an investment holding company (Holdco), with a low cost. Holdco owns three assets: (a) 100% of a private company that is running an active business, Opco (50% or more of the FMV of its assets are active business assets), with a cost of $100 and a FMV of $90M; (b) public company shares worth $10M; and (c) real estate with an assessed value of $30M, as can be seen in the diagram:

Ms. Y
(40%)



Since more than 50% of Holdco's assets are investment assets (all its assets are investment assets), its assets will flow through to Ms. Y for purposes of the wealth tax. Ms. Y's assets will consist of her share, i.e., 40% of: the $100 cost of the Opco shares (cost is used since Opco is a private company that is not an investment holding company); the $10M worth of public company shares; and the $30M worth of real estate, which flow through to Ms. Y.

Hence Ms. Y's assets will be just over $16M; i.e., $40 (i.e., 40% of $100) + $4M (i.e., 40% x $10M) + $12M (i.e., 40% x $30M). The assets of Opco do not flow through to Ms. Y since it is *not* an investment holding company.

When assets are flowed through, as in examples 2 and 3 above, the cost of the top private company shares will not need to be included in the individual's assets (to avoid double counting). Hence, in example 2 the cost of Mr. X's assets will not include his cost of his private company (Private Co.) shares. In example 3 the cost of Ms. Y's assets will not include her cost of her investment holding company (Holdco) shares.

Anti-avoidance Rules

None of the following transactions will be subject to the anti-avoidance rules:

- arm's length transactions,
- transactions at FMV,
- transactions that occurred prior to the enactment of this wealth tax.

To avoid this tax, some taxpayers will transfer assets to others to reduce the FMV of their assets. Actually, gifting assets to others is allowed and will *not* be subject to anti-avoidance rules. If, however, assets are gifted prior to December 31st and then gifted back to the taxpayer after December 31st, and one of the reasons for this gifting arrangement is to avoid the wealth tax, the asset will be deemed to be owned by both the taxpayer who initially gave the gift and the taxpayer who now legally owns the gift (i.e., double counting).

Any gifts that will revert back to the taxpayer will be deemed to be owned by both the taxpayer who initially gave the gift and the taxpayer who now legally owns the gift (i.e., double counting). For example, if a taxpayer gives assets to a trust, or private company, but has the right to get those assets back at any time in the future, then this anti-avoidance rule will apply.

Hence, real gifts are an acceptable way to reduce or avoid this wealth tax but "temporary" gifts are not.

Similarly, while most personal use property (PUP) is excluded, if an unreasonable amount of PUP is purchased prior to December 31st to lower the value of cash, or other assets, and then converted back into cash or other assets after December 31st, then *these* assets will be included in the taxpayer's assets at cost.

Finally, if a private company structure is used to own public company shares (perhaps through a chain of entities as discussed above), and if investment assets are sold shortly before December 31 and used to buy active business assets, and then the transaction is reversed shortly after December 31st, and one of the main reasons for these transactions is to ensure the private company meets the 50% test described above to avoid the flow-through rule, then the transaction will be ignored for wealth tax purposes and the flow-through rule will apply.