CIBC Wood Gundy

Perspective

Compliments Of Voronoff Private Wealth Management

Third Quarter 2014

Back To Basics

From time to time, it may be beneficial to remind ourselves of some basic concepts that may lead to financial success. Saving and time are fundamentally important because they can significantly influence future wealth accumulation. Beyond reminding ourselves of the impact, teaching these basic concepts to future generations may make a difference in their financial well-being.

In many cases, building a solid foundation for financial success starts with saving. One of the best ways to encourage saving is to adopt a "pay yourself first" mentality. Saving can also be increased by making lifestyle changes such as reducing non-essential spending or making trade-offs.

Consider the impact of an individual eliminating an afternoon coffee. Over a 40-year period, foregoing a daily latte that costs $4 today and instead investing that amount annually would yield almost $250,000 before taxes (assuming a 5 percent return and 2 percent inflation), a significant amount by any standard.

Time also plays an important role in investing success. The effect of compounding over time can be so profound that it was once referred to as the "eighth wonder of the world" by Albert Einstein. It's no wonder. A 20-year old who saves $2,500 per year for the next 10 years and stops contributing will have around $232,000 before taxes by the age of 70 (at an annual compounded rate of 5 percent). Starting at the age of 40 and contributing $2,500 per year for each of 30 years would only yield around $174,000 by the age of 70 — a return of 25 percent less, despite contributing for 20 additional years!

Good saving habits and starting early are two financial concepts that seem simple enough, but their significance is often overlooked. We all need a reminder sometimes.

Voronoff Private Wealth Management

Passing along these basic lessons can also help future generations prepare for the journey to financial success.

Speaking Personally: It's hard to believe that we are already at the halfway point of the year. We hope that you are well on your way to achieving the goals set for this year.

As we strive to make progress, whether it be with our investments or in other aspects of our lives, the summer often allows for a break from hectic business or personal schedules to reflect. When it comes to your portfolio, we're always here to assist.

Financial Market Monitor

	Recent 06-03-14	Six Months Ago (12-02)	One Year Ago (06-10)
S&P/TSX Composite Index	14734.69	13419.57	12382.67
Dow Jones Industrial Average	16722.34	16008.77	15238.59
Canadian Interest Rates/Yields			
Canadian Prime Rate	3.00%	3.00%	3.00%
Treasury Bills* -3 month	0.93%	0.94%	1.02%
-6 month	0.95%	0.97%	1.05%
Gov't. of Canada Bonds* -5 year	1.60%	1.77%	1.63%
-10 year	2.34%	2.60%	2.20%

* Approximate annual rates.
Subject to transaction volumes, availability of specific issues, and other important factors.

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Estate Planning: Upcoming Changes

Treatment Of Donations Upon Death

A positive change announced in this year's federal budget that may help to save taxes relates to the tax treatment of charitable donations made through a will.

Currently, qualifying donations made by an individual's will or through beneficiary designations, (including through insurance policies, Registered Retirement Savings Plans (RRSPs), Registered Retirement Income Funds (RRIFs), Tax-Free Savings Accounts (TFSAs)), are, for tax purposes, considered to have been made immediately before the individual's death.

This means that donations would be claimed in the deceased individual's terminal tax return or the year immediately prior to death to the extent that the entire donation tax credit is not used in the year of death.

Ordinarily, the amount of the donation that qualifies for a tax credit is limited to 75 percent of net income; however, in the year of death and the year immediately prior to death, the limit is increased to 100 percent of net income.

The 2014 federal budget proposes* to change the rule for deaths that occur on or after January 1, 2016 such that the qualifying donation will be considered to have been made by the estate at the time that the property is transferred to the donation's recipient, provided that the transfer occurs within 36 months after death. The administrator of the estate will have the flexibility to decide whether to allocate the donation to: i) the taxation year of the estate in which the donation is made; ii) an earlier taxation year of the estate; or, iii) the last two taxation years of the deceased.

Depending on the situation, this change may provide additional flexibility in minimizing the combined taxes paid by both the deceased individual and their estate.

*At the time of writing, the bill containing the budget has not yet been passed.

Please note that comments included in this publication are not intended to be a definitive analysis of tax law. The comments contained herein are general in nature and professional advice regarding an individual's particular tax position should be obtained in respect of any person's specific circumstances.

Consider The Impact

Changes To Testamentary Trusts

This year's federal budget announced changes to testamentary trusts that will take place starting in 2016 (once the bill containing the budget has been passed*). If you are a trustee or a beneficiary of a testamentary trust or your will contains provisions to create such a trust, you may be wondering how these changes may affect you.

A testamentary trust is a trust that is created upon the death of an individual by the terms of their will, whereby the trustee(s) of the trust holds and manages the trust's assets for the benefit of the beneficiary(ies).

Prior to the budget changes, testamentary trusts were beneficial tax planning tools because income within the trust was taxed at the same graduated rates as individuals. Potential tax savings were achieved when a beneficiary of the trust had other income that placed him/her in a higher tax bracket than the trust.

The most significant change implemented by the 2014 budget was to eliminate, beginning in 2016, the graduated tax rates for existing and new testamentary trusts (except for testamentary trusts with beneficiaries eligible to claim the federal Disability Tax Credit). However, a grace period for the first 36-months after death will apply where testamentary trusts are subject to tax at the graduated rates.

In addition, starting in 2016 two administrative changes will apply. Testamentary trusts will be required to make quarterly tax instalment payments and have a December 31st year end.

While these changes may impact tax benefits, testamentary trusts can still be a useful estate planning tool. Here are some other benefits:

Protection From Creditors — Assets held in trust may be protected from claims of beneficiaries' creditors, including former spouses.

Control — Testamentary trusts may help to provide protection for the estate's assets by ensuring they are under the control of a responsible trustee. This may be helpful in situations where beneficiaries of the estate may be considered spendthrifts, or include minors or other individuals who may not yet be financially responsible. The terms of the trust can specify the timing and the amount of distributions to be made to the beneficiaries.

Tax Savings — A testamentary trust can still provide income splitting opportunities and may provide protection from probate fees, in applicable provinces.

Revisit Your Trust

If you currently have a testamentary trust in place in your will, given the proposed changes, you may wish to revisit it with a professional to ensure that it continues to provide its intended objectives.

*At the time of writing, the bill containing the budget has not yet been passed.

Differing Opinions

Share Buybacks: Good Or Bad?

In today's environment of historically low interest rates and low returns on cash investments, many companies are finding that share buybacks/repurchases are a good use of excess cash. Are share buybacks good or bad for investors? There are differing viewpoints.

Share repurchases may reduce the overall shares that are outstanding in a company, usually resulting in a greater proportionate stake in the company for investors who retain their shares. This means that the company's earnings per share metric may generally increase following a buyback.

Compared to other methods of distributing cash such as dividend payouts, share buybacks may be more tax-efficient for investors. In most cases, repurchases do not trigger a taxable event for continuing shareholders unlike dividends which are taxable in the year that they are paid (although taxes on dividends paid by Canadian corporations are somewhat minimized by the dividend tax credit). However, dividends may result in immediate liquidity since they are paid directly to the investor, whereas increased share value is only realized when shares are sold.

Yet, some criticize share buybacks as negative for investors because companies that purchase their own shares are foregoing capital that should have been spent on productive activity to potentially raise profits and improve shareholder value.

In some cases, a company may overpay for its share repurchase. There have also been instances where companies issue new shares or options to employees at the same time of the repurchase which results in no increase in value to outside investors.

Financial Concept Review:

Understanding Rates Of Return

The rate of return calculation is one of the best metrics for comparing the performance of investments. In its basic form, the rate of return is simply the change in the value of an investment, generally net of fees, divided by the original amount of the investment expressed as a percentage.

Rates of return are usually calculated over the time period of one year to generate an annual rate of return. Over longer time periods, the rate of return is calculated as an annualized figure. This is often seen with mutual funds which may quote performance for one, three, five and ten-year time periods. The annualized figure provides an estimated annual return and can be used to compare the performance of different investments over different time periods.

Don't Forget Volatility

Annualized returns don't necessarily tell the whole story. Two investments that have the same annualized rate of return can have completely different return profiles. An annualized rate can disguise any volatility that may have occurred over a specific period.

As an example, a less volatile investment that provides a steady return of 5 percent each year for three years will have an annualized return of 5 percent. But another more volatile investment may have annual returns of 1, -10, and 24 percent over the same time period but will have the same annualized return of 5 percent.

Investors should be careful to not only consider annualized returns when comparing investments. In many cases, an investment yielding reasonable annualized returns with lower volatility will be preferred over one with higher volatility.

Calculating Your Rate Of Return

When determining your rate of return on an investment or portfolio, keep in mind that the calculation may become more complicated if you need to consider any contributions or withdrawals that occur during the period of time for which you are calculating your return.

A Handy Tool: The Rule Of 72

The Rule of 72 is a great way to estimate how long it takes an investment to double. Dividing the number 72 by an investment's rate of return gives a rough idea of how many years it takes for an investment to double.

Take, for example, an investment that yields 5 percent. Dividing 72 by 5 results in a figure of around 14.4. So, for a $10,000 investment, it will take approximately 14.4 years to become $20,000.

The Value Of Advice

The investment industry has attracted much attention lately with negative press and scrutiny relating to the costs associated with investing. It's understandable — investors have many options when seeking financial advice and, often, clearly differentiating between the alternatives is difficult.

But, the old adages "knowledge is power" and "you get what you pay for" may be especially relevant in our industry and we believe that more transparency relating to the cost of business can only help investors as they plan for their financial future.

Why Is There A Cost?

At a very basic level, investors pay for the financial planning and advice we provide. Our financial plans are tailored to take into account your particular goals and risk tolerance and we are here to help you adapt as situations change through different stages of life or when the marketplace changes. Good investment advice helps to keep you on track towards meeting your goals.

We have a team of qualified experts focused on managing your wealth and we strive to deliver a very high standard of advice and service. Our advice is complemented by a wide range of research and information services, as well as simplified and consolidated reporting.

Today, investors have many more investing resources available, but investing has also become much more complex. Professional money managers have access to company management and analytical tools that most investors do not. The best advisors spend a great deal of time and resources making informed and disciplined investing decisions.

In most cases, a comprehensive approach to wealth management means more than just providing investment recommendations. This includes tax planning strategies or intergenerational and estate planning.

Why Do Some Investment Products Incur Higher Costs?

Additional fees may be incurred with specialized investment products. For example, mutual funds are actively managed and require a team of professionals who make investment decisions based on a fund's investment objectives and continuous in-depth research. Active management means that adjustments are made in response to changes in the portfolio's securities or the marketplace over time. During periods of high market volatility, the portfolio manager may change the portfolio's holdings to reduce risk or volatility. The associated costs make up the management fee.

Certain index funds, such as exchange-traded funds (ETFs) that are not actively managed, will not incur the same management fees. However, these index funds do not mitigate risk and are designed simply to mirror an index.

Mutual funds also charge an administrative fee that includes operating expenses such as marketing, record keeping, tax/client reporting, legal, auditing and filing charges.

Where Do Advisors Add Value?

During financial market downturns, it may be easy to focus solely on returns and overlook the value provided by an advisor. Likewise, when times are good, it may seem as though anyone can make money investing in the markets. But managing a financial plan can be complex and time consuming. Many individuals may not have the time to do this on their own or can benefit from an additional level of support or discipline.

An advisor will work closely with you to extract current facts and information, review investment alternatives and identify potential risks and rewards so that you can make informed investment decisions.

Many studies, including a 2012 report by the Investment Funds Institute of Canada, show that Canadians who use professional advisors have substantially higher investible assets than non-advised households, regardless of household income level. These individuals also have greater financial literacy and better savings patterns. Most importantly, investors working in partnership with their advisors are more confident about their financial future.

One of the most important parts of our job is helping you to prepare for the future and meet your financial objectives. We strive to prove our value to you by supporting you and your investments. If you ever have any questions or concerns, please don't hesitate to call.

With the compliments of...

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