CIBC Wood Gundy

Perspective

Personal Newsletter From Anton Voronoff

Third Quarter 2013

Take A Vacation From The Headlines

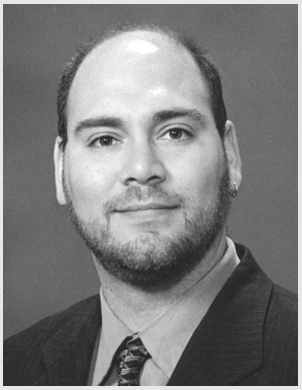
Summer is synonymous with vacation. When it comes to your investments, taking a vacation — that is, from the headlines — may be one way to improve your investing behaviour.

Today, technology has enabled news to travel more quickly and reach more people than ever before. It has also helped to amplify the "noise" and oftentimes increases the potential for people to overreact.

Temporary "market mayhem" resulted in April when a hacked Twitter account of the Associated Press (AP) deceptively reported that U.S. President Obama had been injured in an explosion at the White House. This sent the Dow Jones Industrial Average (DJIA) into a 150-point tailspin within seconds, following strong gains earlier in the day. After it was revealed that the AP account had been compromised, the recovery of the DJIA showed that the market is also very efficient in correcting mistakes. Although high-frequency trading algorithms played a role, the event showed how hastily financial markets can react.

Another problem with following the headlines too closely is that the markets sometimes do not react the way you would expect. Throughout the history of the stock markets, prices have often moved up or down when the prevailing sentiment suggests otherwise. We have seen this more recently with the record-setting performance of the U.S. markets despite the nation's continuing economic struggles and well before any sustained economic growth.

Headlines aside, it is investing for the longer-term that will help to provide the growth and resulting returns to investors. Remember the objectives set out in your personal financial plan as they have been put in place to be your guide. Make sure to keep them working for you, so that you can take a vacation from the headlines.



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At the time of writing, Canadian markets continue to be sluggish, largely driven by lower commodity prices as a result of continued global economic struggles.

As we have seen in the U.S., an upturn can happen at any time. Make sure your hard-earned dollars aren't taking a vacation on the sidelines. Keep them working for you. Have a great summer.

Financial Market Monitor

	Recent 06-10-13	Six Months Ago (12-03)	One Year Ago (06-12)
S&P/TSX Composite Index	12382.70	12169.70	11497.30
Dow Jones Industrial Average	15238.59	12965.60	12573.80
Canadian Interest Rates/Yields			
Canadian Prime Rate	3.00%	3.00%	3.00%
Treasury Bills* -3 month	1.02%	0.95%	0.88%
-6 month	1.05%	1.02%	0.95%
Gov't. of Canada Bonds* -5 year	1.63%	1.28%	1.27%
-10 year	2.20%	1.70%	1.80%

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

In This Issue:

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Estate Planning

The U.S. Estate Tax May Affect You

As a Canadian citizen, you may not think that the U.S. estate tax applies to you. However, Canadians who hold what is termed as "U.S. situs property" may be subject to this tax. This includes U.S. real estate, such as the condos that many snowbirds escape to during the winter season, and shares of U.S. companies, even if they are held in a Canadian brokerage account, including securities held in registered plans.

Canada does not have an estate tax; rather, your estate is subject to tax on the capital gains resulting from the deemed disposition of your assets at death. The U.S. has an estate tax and the rules have recently changed. As of January 1, 2013, the top estate tax rate was raised to 40 percent from 35 percent.

Your exposure to U.S. estate tax depends on the amount of U.S. situs assets you own at death and the size of your worldwide estate. Your worldwide estate is made up of the value of all of your assets regardless of where they are held and can include items such as the death benefit on an insurance policy.

If the value of your U.S. situs assets is less than US$60,000 at death, you will not be subject to U.S. estate tax regardless of the value of your worldwide assets. If the value of your worldwide estate is less than US$5.25 million at death, you will not be subject to U.S. estate tax regardless of the value of your U.S. situs assets. However, if the value of your worldwide estate is greater than US$5.25 million at death and the value of your U.S. situs assets is greater than US$60,000, you may be subject to U.S. estate tax.

If you may be subject to this tax, there are steps that you can take to help minimize the potential effects. Given the complexity of the topic, we suggest seeking assistance from a tax specialist familiar with U.S. estate tax law.

Changes To The Lifetime Capital Gains Exemption

In our last newsletter, we discussed the benefits of the Lifetime Capital Gains Exemption (LCGE). The 2013 federal budget increased the LCGE to $800,000 from the previous level of $750,000, effective for the 2014 taxation year. The LCGE will also be indexed for taxation years after 2014. This continues to be good news for small business owners as it will provide greater tax relief.

Crypto-Currency Mania

Bitcoin Boom? Bubble? Or Bust?

Although it has been around for over four years, the "crypto-currency" known as the Bitcoin (BTC) has been getting a lot of attention lately due to growing concerns about traditional currencies in regions like Europe.

The value of the BTC has fluctuated significantly as its popularity has increased. Earlier this year, the price of a Bitcoin was around $13. In April, the price peaked at $266, crashing to $54 a few days later and then hovering around $130.

What exactly is this currency and how is it created?

The Bitcoin is an online currency that is not controlled by any central authority. Instead, it is underwritten by a peer-to-peer network that uses cryptographic technology to control its creation and transactions. Simply put, Bitcoins are created, or "mined", when a computer solves complex processor-intensive equations by unlocking blocks of data that produce a certain pattern. They can then be purchased from independent exchanges on the internet.

But buyer beware, the Bitcoin has had its fair share of bumps throughout its short life. In 2010, users found that they could create an indefinite number of BTCs, causing a supply increase that significantly eroded its value. Since then, supply has been properly controlled and only a fixed number of BTCs can be introduced each year. Today, over 11 million are in circulation and supply is capped at 21 million.

Many exchanges have failed because of low transaction volumes. Successful exchanges and the virtual wallets of BTC holders often become targets for cyber attacks.

It is also believed that Bitcoins have been used extensively in the illegal drug and gambling worlds. As such, the currency has been under increased scrutiny by government agencies.

Adoption of the currency has been slow with mainstream vendors. A Forbes reporter living in San Francisco recently blogged about her attempt to live using only Bitcoin currency for a week. As a result, she lost five pounds in the struggle to find grocery stores and restaurants that accepted BTCs.

Will this virtual currency play a larger role going forward? Some say that this is just another fad going through a bubble. After all, it's hard to put faith in a currency that has such a volatile market value, inflexible supply and minimal use in trade.

Before It's Too Late...

Trusts: Don't Forget The 21-Year Rule

"Time moves in one direction, memory in another."
– William Gibson

As part of your overall financial plan, you may have set up a trust. Trusts can be a great tool for tax, estate and succession planning. However, one often overlooked component is the "21-year rule", which may sometimes be forgotten over the life of the trust.

In general, under the Income Tax Act, every 21 years a trust is deemed to have sold all of its property at fair market value for tax purposes and the trust must pay tax on any accrued gains. Without careful attention to the "age" of a trust, any benefits that you may have intended to achieve by setting up the trust can potentially be overshadowed by a significant tax liability.

Consider the consequences: assume that a trust holds shares that are worth $100 on its 21st anniversary which originally cost $10. The trust would be subject to tax on a $90 deemed capital gain, even though it still owns the shares. This "prepayment" of tax could potentially create a liquidity issue for the trust.

Fortunately, with advanced planning, it is possible to take the proper steps to avoid a nasty tax bite before 21 years have passed. One way to avoid this situation, provided the trust was properly created taking into consideration the rules of the Income Tax Act, is to distribute the assets of the trust to its Canadian resident beneficiaries at the trust's original cost base, subject to the terms of the trust agreement.

In our example, the trust could distribute the shares to its beneficiary(ies) at the original $10 cost. Now the beneficiary(ies) would have personal ownership and control over the assets and would therefore be responsible for paying tax on the $90 capital gain when the shares are eventually disposed of.

Other solutions are possible but may be more complex and require greater pre-planning with the assistance of an accountant and/or lawyer.

Don't forget about the 21-year rule. We recommend meeting with an advisor well in advance of the trust's 21st anniversary to ensure that the appropriate steps are taken that relate to your particular situation.

The Billionaires Club

Words Of Wisdom From The World's Richest

Each year, Forbes Magazine publishes a list of the world's billionaires. This is the 27th year and, once again, there are more billionaires in the world today than ever before – the list grew by 17 percent and there are 1,426 billionaires with an aggregate net worth of around $5.4 trillion!

What is particularly interesting about this year's list is that many of the new members to this elite club are self-made billionaires. During what has been considered one of the most difficult economic times that we have experienced, the wealth-building accomplishments of these individuals to become billionaires seems even more significant.

What does it take to be part of this elite 0.00002 percent of the population?

Here are some thoughts from the world's most elite group of money makers:

- **#1*: Bill Gates: $67.0B, Source: Microsoft**
  "It's fine to celebrate success but it is more important to heed the lessons of failure."
- **#4: Warren Buffett: $53.5B, Source: Investing**
  "Stocks will do well just as certainly, since their fate is tied to business performance. Periodic setbacks will occur, yes, but investors and managers are in a game that is heavily stacked in their favour. Since the basic game is so favourable, it's a terrible mistake to try to dance in and out of it based upon the turn of tarot cards, the predictions of "experts," or the ebb and flow of business activity. The risks of being out of the game are huge compared to the risks of being in it."
- **#8 (#1 in Asia) Li Ka Shing: $31.0B, Source: Diversified**
  "Set your goals high; make friends with different kinds of people; enjoy simple pleasures. Stand on high ground; sit on level ground; walk on expansive ground."
- **#30 George Soros: $19.2B, Source: Investing**
  "The worse a situation becomes, the less it takes to turn it around, the bigger the upside."
- **#346 George Lucas: $3.9B, Source: Entertainment, Star Wars**
  "You simply have to put one foot in front of the other and keep going. Put blinders on and plow right ahead."

**As of May 2013, Bill Gates became the #1 world's richest individual according to Bloomberg. He is listed as #2 on the Forbes list.*

Source: Forbes Magazine, March 15, 2013 issue.

Federal Budget 2013: Staying The Course

The federal budget was unveiled at the end of March during the printing of our last newsletter. It outlines the intent of the federal government to achieve a balanced budget by 2015-16. There were very few surprises in this budget and the measures introduced were modest, with a focus on improving tax fairness, closing tax loopholes and addressing aggressive tax planning.

Some of the more notable changes (most of which came into effect after March 20, 2013) that may directly impact individual taxpayers include:

Enhancements To Tax Credits/ Deductions

The budget includes a few enhanced tax credits/deductions:

- ***Lifetime Capital Gains Exemption (LCGE)*** — (See page 2 of this newsletter.)
- ***First-time donor credit*** — A temporary "Super Credit" will supplement the existing charitable donation tax credit with an additional 25 percent tax credit on donations up to $1,000 if the individual is a first-time donor (i.e., neither the individual, nor a spouse/partner, has claimed a donation tax credit in any taxation year after 2007).
- ***Adoption expenses*** — For adoptions finalized after 2012, the adoption period for which eligible related expenses can be claimed is extended.
- ***Mineral exploration*** — The mineral exploration tax credit is extended by one year for flow-through share agreements entered into before April 1, 2014.

Changes To Existing Tax Credits/ Deductions

There are a number of changes to existing tax credits/deductions:

- ***Dividend Tax Credit (DTC): Non-eligible dividends*** — There are adjustments to the gross-up factor applicable to non-eligible dividends from 25 percent to 18 percent and the corresponding DTC from 2/3 of the gross-up amount to 13/18. As a result, the federal non-eligible dividend tax rate increases from 19.58 percent to 21.22 percent. The combined federal and provincial rates applicable to non-eligible dividends depend on the outcome of each of the individual provincial budgets.
- ***Safety deposit boxes*** — The rental cost of a safety deposit box will no longer be deductible for income tax purposes.
- ***Labour-sponsored venture capital corporation tax credit*** — This tax credit will be phased out beginning 2015 and will be completely eliminated by 2017.

Elimination Of Tax "Loopholes"

The budget attempts to continue to minimize the opportunity for individuals to pursue arrangements that result in unintended tax benefits, including:

- ***Charitable donation tax shelters*** — To discourage potential misuse of certain tax shelters, the Canada Revenue Agency (CRA) will be permitted to collect 50 percent of the taxes in question when a taxpayer has objected to an assessment related to a charitable donation tax shelter.
- ***Leveraged life insurance*** — The federal government intends to block the unintended tax benefits from the use of two leveraged life insurance products: leveraged insured annuities and 10/8 arrangements.
- ***Character conversion transactions*** — Rules have been introduced that would effectively eliminate the ability to convert fully taxable income into capital gains that are only 50 percent taxable. These changes could impact mutual funds that use forward derivative contracts to convert the income distributed to investors.
- ***Graduated tax rates on trusts and estates*** — The government has announced its intention to consult on possible measures to eliminate the graduated tax rate benefits that result from trusts created by wills and estates.

With the compliments of...

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