BMO NESBITT BURNS

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The Expectations of Service Excellence

As our North American economy has moved swiftly over the last 65 years from a manufacturing-based economy to a service-based economy, the whole notion of service excellence has ramped up to stratospheric levels. Some of this is welcome, as it is truly a gift to go beyond the call of duty for a valued customer/client and see that action recognized with both appreciation and long-lasting loyalty. But in the process of trying to achieve that idealistic, heightened service level, are we somehow failing to simply deliver the goods we were asked? In other words, to perform the basic level of service required in our contractual relationship with our customers?

If you monitor the advertising campaigns of several service-related industries, especially the hospitality industry, you will notice lately that they are all endeavouring to kill you with kindness or worse. The Trump hotel organization recently ran a print ad extolling their philosophy as "If you can dream it, we can do it". Really? Do I seriously need a hotel to fulfill my ultimate dreams? I'm sure that if I asked them to source out magnums of 1965 Dom Perignon champagne and fill my bath with it and put rose petals on top, they would be happy to do so. But whose values are being served? I'm very fortunate to have the occasional treat to stay at very nice hotels. But sometimes they can make me uncomfortable. At a 5 star hotel in Manhattan there was a butler in white tails (I'm not joking) on each floor whose job it was to do any of the guests' bidding (if legal). I'm sure he was a very nice guy but I prefer to unpack my own suitcase, thanks anyway. Similarly, at a 5 star ski resort I stayed at in February of this year, there was a ski concierge who offered to help me put on and take off my ski boots. Laudable, but unnecessary. But in the pursuit of the extraordinary, are some service organizations falling down on the ordinary? Another hotel chain has the annoying slogan, "Whenever, Whatever". I was forced to endure listening to this slogan over and over, as I sat on a long telephone hold waiting for them to deliver a fresh towel to me at their beach, which they finally did, after 45 minutes. My new bottom line… Forget about fulfilling my dreams – just get me a damn towel!

Since I too work in a service-related field, I think long and hard about the service levels and expectations we create at The Dorfman Group, as part of BMO Nesbitt Burns. We don't promise to actualize your dreams. We can't deliver exponential rates of return that are inconsistent with current market conditions. We can't always make your retirement replete with "champagne wishes and caviar dreams". But we can and do promise to get to know exactly who you are and what you are about. We will understand your risk tolerance and put a plan into effect that will protect your capital, grow it in a reasonable way and let you sleep at night. That we can do for you, willingly and happily. Making your dreams come true – that's up to you!

Michael Dorfman

IPPs Remain an Attractive Option for Business Owners

If you are a business owner, incorporated professional or an executive and were looking to increase your retirement assets through an Individual Pension Plan (IPP), you may have been disappointed with the 2011 federal budget proposals that considered substantial changes to the IPP rules. The proposed changes impacted the benefits derived from how IPPs were funded, as well as how retirement benefits would be calculated. Behind these proposals was the perception that by implementing an IPP, there would be a significant "unintended tax deferral".

However, when Parliament passed the Ways and Means motions in December 2011, the final legislation constituted a substantial retreat from the initial funding restrictions proposed in the March and June 2011 federal budgets.

As a result, the changes that were passed into law affect the withdrawal rules for IPPs and only moderately affect funding. The new rules require minimum withdrawals to be calculated as either the greater of the calculated pension amount, or the minimum amount that would be paid out under the RRIF rules and is intended to prevent manipulation of pension plan surpluses which could be shielded indefinitely from taxation.

Part of the appeal of the IPP strategy has been the ability to fund past service, as it often results in considerable tax deductions to the business owner's company. In the proposals, the original formula would have penalized small business owners and individuals who had significant RRSP savings. Contributions to an IPP for past service would have had to be funded from the current assets in the RRSP or by reducing unused contribution room before new past service contributions could be made.

With the new rules, the available IPP past service funding contribution will be impacted by the amount of personal RRSP funds used to calculate the required transfer amount. Though the new rules are targeted towards connected persons planning to trigger a large past service contribution, it's anticipated impact is mainly to individuals over the age of 53 and individuals with exceptionally large RRSP balances. For example, *a business owner 53 years of age or older with 20 years of past service would need an RRSP balance in excess of $700,000 before the corporation would begin to see any reduction in deductible past service contributions on behalf of the individual.* It is anticipated that relatively few individuals will actually be impacted by the new rules.

For those business owners and professionals who have focused their funding efforts on achieving success in their enterprise, often at the expense of saving for retirement, the IPP remains a viable financial planning strategy to achieve greater predictability of future retirement income and enhanced tax deferral.

Reduce Your Taxes With a Prescribed Rate Loan

Under our tax system, the more you earn, the more you pay in income taxes on each incremental dollar earned. With this in mind, it makes sense to spread income among family members who are taxed at lower marginal rates in order to lower your family's overall tax burden. However, the income attribution rules can prevent most income splitting strategies where there has been a transfer to a spouse or minor child for the purpose of earning investment income. The attribution rules transfer the taxation of investment income (and capital gains in the case of a gift to a spouse) back to the person who made the gift regardless of whose name is on the investment. While there are significant restrictions, there are still a number of legitimate income-splitting strategies available to you.

Prescribed Rate Loan

A simple, yet effective income-splitting strategy involves transferring income-generating assets (ideally cash) to a lower-income spouse (or other family member) and taking back a loan (equal to the fair market value of the assets transferred) at the Canada Revenue Agency's (CRA) prescribed interest rate in effect at the time of the loan. Given the current low CRA prescribed rates, implementation of this strategy presents a very compelling opportunity. For loans made to a family member, the rate necessary to avoid the income attribution rules is only 1% effective for loans made in the fourth quarter of 2012 – this continues to be an all time low for CRA's prescribed rate. Most importantly, if structured properly the prescribed rate in effect at the time of the loan will continue to apply until the loan is repaid, regardless of future changes to the prescribed rates. For loans made after December 31, 2012 (i.e. the end of the fourth quarter of 2012), the CRA's prescribed rate at the time of the loan will apply.

How it Works

Briefly stated, an interest-bearing loan is made from the person in the higher marginal tax bracket to a family member (such as a spouse) in a lower tax bracket for the purpose of investing. To avoid the income attribution rules there are a number of requirements that must be met. For example, interest must be charged at a rate at least equal to the CRA's prescribed rate in effect at the time the loan is made. Interest is charged annually at this rate and must be paid by the following January 30th each year. In order for there to be a net benefit, the annual realized rate of return on the borrowed funds must exceed the annual interest rate charged on the loan, which is included in the income of the transferor and should be deductible to the transferee family member, if used for investment purposes. By locking in this strategy at this low rate, long-term benefits of income-splitting can be achieved to the extent future investment returns exceed this low 1% threshold. The impact of increased income to the transferee family member (e.g. loss of spousal tax credit) should also be considered before employing this strategy. Finally, it is important to consider the possible recognition of capital gains or capital losses, which may be denied, when assets other than cash are loaned or transferred to a family member. Given the complexity of the income attribution rules, you should consult with your tax and legal advisors to review and structure any income splitting strategies to ensure that the strategies are implemented and documented correctly and achieve the desired results without any unanticipated implications.

The Random Effects of Positive Feedback

Casino gambling and golf are two activities that absolutely fascinate me. Personally, I love the second one and am indifferent to the first. But that's not the point. They are equally fascinating due to their common elements of providing random positive feedback and the addictive properties that it creates.

Allow me to explain. We all know that casino gambling is structured to allow for a decidedly un-level playing field in which the House has a permanent edge and will win long term. So why do people gamble if they know that long-term they will always lose? The reason is that in the short term, they may actually win. This "randomness" of outcomes creates such a positive jolt to the dopamine levels of humans, that for some people, they would prefer that randomness to the certainty of winning, if they were on the other side of the table with a built-in advantage designed to consistently provide long term winnings. Sounds crazy? But it's not. A very large and profitable gaming industry is built around this very principle.

In a different way, golf pushes some similar psychological buttons. A mid-handicapper like me will usually, over the course of a season, average about 90 shots per 18 holes. But all avid golfers know that in golf, there is no "average". On any given day, nay, on any given hole, one can exhibit either streaks of brilliance that equate us with Tiger Woods, or that make us look like we've never held a club in our hands in our entire life. It's equally maddening and inexplicable. And that level of inconsistency and randomness of outcomes exists in few other endeavours.

It can be so frustrating, it can cause some golfers to quit, drink heavily, or both. But for most, when they catch the club cleanly and purely on the ball, and it flies at its intended target with a true, straight arc and lands softly on the green or fairway, there is no other feeling in the world. And as all golfers say when that happens, "That's what keeps me coming back!"

Michael Dorfman

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