Investment Insight

Are You Checking Too Frequently?

Autumn 2021

According to recent reports, investors using a U.S. discount brokerage platform are checking their portfolios at an alarming rate of seven times per day.[1] It's not difficult to do. Today, often all it takes is one quick swipe on our smartphones. However, frequent portfolio checking may be hazardous to your investing health.

Modern behavioural scientists have shown that our cognitive biases can cause investors to make decisions that may not be in our best interests. By checking portfolios frequently, there is a greater chance that we will trigger these biases. One reason is that frequent checking means a higher probability of seeing a loss, which can drive emotional reactions. By checking S&P/TSX Composite Index performance on a daily basis, there is a 48 percent likelihood of seeing negative performance. If you were to check only once per year, this would decrease to 28 percent.[2] However, even seeing positive performance may cause us to act in haste, such as selling a well-performing investment too early.

How about you: do you check your portfolio too frequently?

In his latest book, Nobel laureate Daniel Kahneman, a father of behavioural finance, suggests that it's not just our biases that can influence our decision making, but also the "noise" around us. And, as the markets continue to climb the wall of worry, there has been no shortage of noise.

Consider one of the more recent topics to consume financial circles: inflation. There has been significant unwanted variability in opinion, or noise, on the path forward. Some have warned that an inflationary era is upon us. Others support a more transitory view and suggest we may be too quick to ignore the deflationary forces. Consider the impact technology has had on lowering our cost of living. One example: the lithium-ion battery costs 97 percent less than three decades ago and is far more efficient.[3]

Market reactions have been mixed. Bond yields usually rise with rising inflation expectations, as inflation erodes the purchasing power of a bond's future cash flows so a higher yield compensates for this risk. However, over the summer, despite rising inflation rates, bond yields remained low and actually fell. Even gold, considered a hedge against inflation, was down at the halfway point of the year.

All this to suggest that predicting the course of near-term markets and economies has always been difficult. We've also never experienced a situation of this magnitude: the unprecedented actions to combat the pandemic have helped to distort market and economic cycles. In many ways, the path ahead will be understood only in hindsight. As your advisor, I am here to help cut through the noise to focus on what is important. Also important is being aware of the effects of paying too much attention to your portfolio or to the noise. Continue to look forward and leave the focus on your portfolio to those of us who are here to manage it.

1. On average. www.reuters.com/breakingviews/chancellor-robinhood-is-more-sheriff-than-rebel-2021-07-15/; 2. S&P/TSX Composite index 1985 to 2020; 3. https://news.mit.edu/2021/lithium-ion-battery-costs-0323

In This Issue

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To My Clients:

Perhaps a result of the time that many of us had during the lockdowns earlier this year, I have been receiving more questions about life insurance and estate planning. I welcome your queries and can work with you to suggest options relating to your particular situation. Don't let this fall down the list of priorities. As the end of the year quickly approaches, I can coordinate calls or meetings to keep this top of mind.

It is also the start of the season of giving and in this issue I have included some thoughts to support a giving strategy. If you are looking for help with this, or any other investing matters, please don't hesitate to call. Enjoy the fall colours!

Liz

TFSA Overcontributions & the Importance of Checking Email

A recent article in the *Financial Post* highlighted the potential consequences of not paying attention to electronic communications relating to Tax-Free Savings Account (TFSA) overcontributions.

If you contribute beyond your TFSA limit, the penalty can be significant — equal to one percent per month on the excess amount for each month that you are over the limit. In recent years, the Canada Revenue Agency (CRA) has provided some leniency: you may request a waiver of the penalty tax due to "reasonable error" and if the overcontribution is withdrawn "without delay."

The article discusses a taxpayer who was sent a warning letter electronically to his CRA "*My Account*" due to excess TFSA contributions. The taxpayer claimed he never saw this letter. Two years later, when his *Notice of Assessment* (NOA) detailed the penalties and interest owed, he took action to remove the excess amount and wrote the CRA to request relief. However, this was denied as the CRA asserted that he had not withdrawn the excess within a reasonable time, when the warning letter was first sent. The taxpayer then took the issue to a federal court, yet the judge sided with the CRA in upholding the decision not to waive the penalty. The article is a good reminder to not only be aware of your TFSA limit, but also check for notifications if you sign up for electronic communications.

This may be especially important to remember as the world continues to go digital. The 2021 federal budget proposed changes to improve the CRA's "ability to operate digitally," to allow the CRA to send NOAs electronically without the taxpayer having to explicitly authorize them. This may apply to those who file income tax returns electronically. Those who file paper returns will continue to receive a paper NOA.

Keep Good Records: *My Account* Updates May Be Lagging

It's prudent to keep good records of your TFSA transactions. Taxpayers should be careful when checking *My Account* for contribution room information as there may be delays in updating TFSA contribution amounts, especially early in the calendar year when the previous year's information may not be fully accounted for. Some taxpayers have also noted that historical information may not always be correct. In this case, you will need to contact the CRA to update these records.

1. financialpost.com/personal-finance/taxes/missing-a-message-from-cra-doesnt-let-taxpayer-off-the-hook-in-tfsa-overcontribution-case

In Short: Tapping the Registered Education Savings Plan (RESP)

If you have a (grand)child who has headed to college or university this fall, congratulations! Now is the time to take action and tap the fruits of your labour: the RESP.

In short, here are four considerations as you plan your withdrawal strategy:

Track the three "buckets" — Track your RESP balances according to their source: i) grants, ii) contributions and iii) accumulated income (AI), which consists of income or gains made on contributions and grants. Grants and AI may be paid out to the beneficiary as an Education Assistance Payment (EAP), which is taxable in the student's hands. Original contributions can be withdrawn, tax free, at any time or paid tax free to a qualifying beneficiary. When withdrawals are made, you will need to specify how much comes from each bucket. Unused grants may be clawed back and unused AI may be subject to a penalty tax.

Think tax efficiency — While you can only withdraw $5,000 of EAPs in the first 13 weeks of enrolment, there is generally little restriction after that period while a beneficiary is registered in an accredited program. Consider drawing EAPs early to help ensure they are used. It may be beneficial to spread EAPs out over several years to use a child's tax credits, such as the basic personal amount and the credit for tuition paid, or to offset any income from summer jobs or co-op programs.

Deplete, before it's too late — Once a beneficiary is no longer enrolled, unused grants may need to be repaid and accumulated income payments may be subject to a 20 percent penalty tax. A six-month grace period after enrolment has ended allows for withdrawals to qualify as EAPs.

Consider alternatives, if it won't be used — The RESP can remain open until the end of the calendar year that includes the 35th anniversary of the plan's opening should a beneficiary decide to pursue future qualified studies. If plans have changed, consider the option to transfer the RESP to a sibling or transfer AI to a parent's Registered Retirement Savings Plan. Keep in mind that both are subject to various conditions.

For more information, see: canada.ca/en/revenue-agency/services/tax/individuals/topics/registered-education-savings-plans-resps.html

Business Owners: Good News for Family Succession — Bill C-208 Receives Royal Assent

With the passing of Bill C-208 over the summer, keeping a business in the family has become easier and less costly. Previously, the Income Tax Act treated the proceeds of intergenerational sales as deemed dividends to the vendor, whereas sales to third parties were treated as lower-taxed capital gains that could be used against the LCGE.* Bill C-208 eliminates this treatment and enables corporate reorganizations among siblings without being subject to anti-avoidance rules in certain circumstances.

*Lifetime Capital Gains Exemption. However, Bill C-208 reduces access to the LCGE if taxable capital involved exceeds $10 million; at $15 million or more, there is no access at all.

The Giving Season is Upon Us: Charitable Considerations

As we enter the final quarter of the year, we are once again approaching the season of giving. Here are just a handful of ideas to support a giving strategy.

Many of us wish to support charities that are important to us. In "doing good," it can also work to your benefit in the form of a tax credit. If you make donations to qualified charities, the federal credit is 15 percent of the first $200 donated per year and 29 percent (or 33 percent*) beyond this threshold. After taking provincial tax into account, the total benefit may exceed 40 to 50 percent, depending on province of residence. Deductions can be pooled with spouses and may be carried forward for up to five years. Here is a sample of options available to you for charitable giving:

Gifting Appreciated Securities — Gifting publicly-traded securities with accrued capital gains to a registered charity not only entitles you to a tax receipt for its fair market value, but also eliminates the associated capital gains tax. If you wish to benefit your 2021 taxes, eligible charitable donations must be made before December 31st so remember to let us know well in advance of the year end as settlement times may vary.

Bequests in Your Will — Providing for a charity in your will may be one way to leave a legacy. Up to 100 percent of your net income in the year of death and year preceding death can be claimed for tax credit purposes.

Private Foundations — Individuals with more substantial assets may consider establishing a private foundation as a vehicle for charitable activities. Money paid into the foundation may result in an immediate tax benefit while the foundation can direct future gifts as it sees fit. However, the ongoing cost of the foundation may be a considerable disadvantage.

Donor-Advised Funds or Community Foundations — Giving through a donor-advised fund or a community foundation may be a cost-efficient alternative to establishing a private foundation as they may eliminate certain legal and administrative fees, while still allowing you to direct donations and achieve tax benefits. The benefit of a donor-advised fund is that the contribution is tax deductible in the year it is made, but funds can be distributed in future years and the donor may be able to direct how funds are invested until their eventual distribution.

Get More Information

These are just a handful of ideas. We can help to provide perspectives on these or other options and have resources here to support these types of endeavours. As well, many major charitable institutions have established planned giving offices to support individuals who wish to make substantial donations. Call them for more information. As always, consult a tax advisor to ensure your priorities are respected with any plan you devise.

*The federal donation tax credit rate for donations over $200 increases to 33 percent to the extent that an individual has taxable income that is taxed at 33 percent.

Inflation: How Has Purchasing Power Changed?

Over thirty years ago, a Big Mac hamburger would put you back around $2. Today, it costs over triple the price. Yet over that period, average family income has only risen by 91.8 percent and the Consumer Price Index (CPI), the official measure of inflation, increased by 107 percent, or just 2.2 percent per year.

One of the most pressing questions in financial circles today is whether inflation will become a problem, or if current inflationary pressures are temporary as the central banks would like us to believe. Those who believe inflation may be more pervasive cite various factors that signal a potential shift: significant government stimulus, aging demographics in low-cost manufacturing geographies and empowered labour that puts upward pressure on wages and prices. Others suggest that inflation won't be able to maintain its recent pace after struggling to climb for many years, largely attributing it to pandemic-depressed prices.

How has purchasing power really changed? The chart shows the prices for select items in 1987 and today. While prices for many things have gone up, technology has made others more affordable: TVs are not only larger and thinner, but cheaper! What about your personal experience?

Changes in the Prices of Select Items: 1987[1] & 2021

	1987	2021	Change
Cdn. Family Income (Avg.)[2]	$37,118	$71,200 (2019)	+91.8%
Cdn. House (Avg.)[3]	$129,702	$716,000	+452.0%
Flat Screen Television[4]	$1,599 (32")	$750 (55")	-53.1%
Top Apple Computer[5]	$9,150	$7,400	-19.1%
Microwave[4]	$580 (680W)	$140 (1100W)	-75.9%
Bottle of Dom Perignon[6]	$85.25	$267.95	+214.3%
Big Mac Hamburger[7]	$2.05	$6.77	+230.2%
University Tuition[2]	$1,137	$6,580	+478.7%
Consumer Price Index[8]	67.5	139.6	+106.8%
S&P/TSX Composite Index[9]	3,729.30	20,035.30	+437.2%

1. 1987 data from Report on Business Magazine, Apr. 2012, pg. 13; 2. Statistics Canada T-1110019101; Undergrad tuition www150.statcan.gc.ca/n1/daily-quotidien/200921/dq200921b-eng.htm; 3. CREA data; 4. Sony HD TV, bestbuy.ca; 5. MacPro, apple.ca; 6. LCBO data; 7. economist.com; 8. bankofcanada.ca/rates/related/inflation-calculator/, Mar. 1987 & 2021; 9. At close on 6/7.

Statistics Canada has released a personal inflation calculator at: https://www150.statcan.gc.ca/n1/pub/71-607-x/71-607-x2020015-eng.htm

Regardless of the path forward, the good news for investors is that the S&P/TSX Composite Index has gained over 430 percent throughout this time. If history is any indicator, equity markets continue to be a great way to grow funds for the future.

Have You Reviewed Your Life Insurance Needs?

One of the lessons that the pandemic has taught us is the importance of preparing for unexpected events before they happen. As part of that planning, have you considered whether your life insurance meets your needs? It's never too late!

As life insurance is often more difficult and costly to obtain in the later years, it's worth considering at a younger age and while an individual is in good health. Yet, even if you haven't planned in advance for insurance as part of your wealth plan, it may not be too late. We often see individuals in their 60s and 70s purchase life insurance as a planning tool and certain insurance companies will even issue life insurance to individuals up to age 85.

Beyond the protection element, here are four areas where it may prove valuable in your planning:

Complement Investment Returns — Many insurance products blend certain aspects of insurance with investing. Depending on the type of insurance and the policy, there may even be choice in how the investment portion is invested, and the potential for a certain amount of growth to be on a tax-sheltered basis. This may be one way to complement investment returns, acting as part of the conservative portion of an investment portfolio, especially in situations in which the cost of managing the policy is reasonable. Upon death, the proceeds will pass to beneficiaries on a tax-free basis. While older individuals will be subject to higher premiums, there may still be a benefit gained from the tax-sheltering opportunity and the eventual tax-free benefit payout.

Support Philanthropic Efforts — Insurance may be used to create a legacy and, in some cases, provide benefits even while you are alive. For example, you could have a charitable organization purchase an insurance policy on your life while you donate the cash annually to pay the premiums. This way, you would receive a tax credit for the annual cash donated. Alternatively, you could own a life insurance policy and name the charity as the beneficiary or donate appreciated shares to fund an insurance policy. There are a variety of tax-effective ways to use insurance to support your charitable endeavours.

Cover Taxes on Death — Many estates incur a considerable amount of taxes on death and this situation may be complicated by the presence of illiquid assets such as real estate or a family corporation. A life insurance policy may help to effectively cover those taxes, so that your estate isn't left with a shortage of cash when these taxes come due. For example, there may be a significant capital gains tax liability upon the transfer of a cottage or cabin and the proceeds from an insurance policy can help to cover these taxes and keep the property within the family.

Equalize an Estate — In cases where you wish to leave your estate to multiple beneficiaries and it is important to provide assets of approximately the same value, life insurance can help to provide that equalization. You may have assets that are better left to certain beneficiaries, rather than being shared, such as a family business. In these instances, the insurance death benefit can be used to help equalize the inheritance for those heirs who may not be the beneficiary of these assets.

We Can Assist

Regardless of your age, consider exploring the opportunities for insurance to play a role in retirement and beyond. There are many products available to support a variety of investment, tax, retirement and succession planning solutions. For a broader discussion, please call the office.

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