CIBC Wood Gundy

Perspective

Personal Newsletter from the Boychuk Knoblauch Financial Group

First Quarter 2017

The Power of Perspective

It's no surprise that human emotions can have an impact on investing. Understanding the psychology behind why we make certain decisions can provide some perspective as we pursue the task of wealth building.

Richard Thaler, a University of Chicago professor, is one of the pioneers of behavioural economics, a field that studies how emotional factors can affect economic decision making. Neuroeconomics explains that we are not biologically wired to make the best financial decisions because the part of our brain that tells us to act rationally can easily be overtaken by powerful emotional impulses. Thaler points out that people tend to be in one of two emotional states: hot or cold. Irrational decisions tend to be made when we are in our hot state. This may explain why we make certain choices: when we aren't hungry (cold state) we might choose a healthy salad. But once dinner rolls around and we are hungry (hot state), we may select a big bowl of pasta instead. We often overestimate the self-control that is necessary in a hot state.

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Likewise, our brains can react the same way when we are investing. Some examples? We may be fixated on a particular sell-price target and refuse to sell a losing position, called anchoring, even though new information changes the target. Or, we may be led into herd behaviour, mimicking the actions of a larger group, when we wouldn't necessarily make the same decision on our own. This is why investors sometimes fall into the trap of buying high and selling low. Behavioural finance can also help to explain other peculiarities of human behaviour, such as why we don't always put away enough for retirement, despite knowing how important it is.

Can we use this knowledge to improve our own investing ways? Being aware of our emotions can help to better regulate them. Experts in behavioural economics claim that many of the best investors have mastered the art of treating their own feelings as reverse indicators. Excitement becomes a cue that it's time to consider selling, while fear tells that it might be time to buy.

Equally important, decisions should be made before entering into potentially emotional situations. This may include sticking to a financial plan during difficult times or refusing to succumb to emotions when the media gets heated. We are also here to provide support to keep you on course.

In this season of resolutions, why not resolve to be aware of the effects that emotions can have on your investing ways? Use the power of perspective to your benefit.

BOYCHUK KNOBLAUCH
FINANCIAL GROUP

Speaking Personally: Best wishes to you as we start another year! Last year brought unprecedented change, including the unexpected results of both the Brexit and U.S. presidential election votes. Looking forward, we continue to face many of the same challenges: slow growth and low interest rates will likely persist.

Will you benefit from the market opportunities that will arise this year? We are here to support you and help position your portfolio to its best advantage.

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Retirement Planning

Dreaming of Warmer Climates?

Now that winter weather has gripped most parts of the country, many of us may be dreaming about retirement life in warmer climates. Whether it is a permanent move, or just a temporary retreat for part of the year, Canadians who live or travel for extended periods abroad should be aware of the potential financial implications.

One important factor to consider when spending extended periods abroad should be the tax consequences, both in Canada and in the chosen destination. In Canada, income tax obligations are determined by your residency status, which is determined on a case-by-case basis and can be affected by things such as Canadian residential ties (e.g., a home in Canada), the purpose for your time abroad and your ties abroad.

As many snowbirds who travel to the U.S. are aware, keeping accurate travel records is important for tax purposes. Over recent years, both Canadian and U.S. border services have become increasingly strict about tracking the movement of visitors through border crossings. A person may be considered a U.S. resident for tax purposes if they spend significant time in the U.S. each year. The "substantial presence test" determines an individual's tax residency status, using a formula that considers the days spent in the U.S. in the current and prior two years. Being a U.S. resident for tax purposes can have significant consequences, such as subjecting worldwide income to U.S. taxation or exposing Canadians to the U.S. estate tax at death.

In addition to tax implications, consider the impact that an extended stay abroad may have on provincial health coverage. Although the rules vary depending on province of residence, provincial medical coverage may become invalid as a result of extended periods spent out of province. Even if your health care coverage remains valid, remember that health care services received abroad are usually

not covered by provincial health care plans, so having adequate private coverage prior to leaving the country is important. Given the broad coverage we have at home, it may be easy to overlook the significant costs associated with healthcare outside of Canada.

There may be other financial implications: Old Age Security benefits may be affected and investment accounts like the Tax-Free Savings Account may be subject to certain restrictions. Even current estate plans, such as power of attorney or will documents, may be affected by your residency status.

A bit of forward planning can go a long way to help prepare you financially. The Government of Canada website may be a worthwhile starting point: www.fcac-acfc.gc.ca/Eng/forConsumers/lifeEvents/livingRetirement/Pages/livingor-vivreouv.aspx. Beyond financial considerations, be sure to have a good understanding of the laws, customs and regulations of the host country. A good resource for international travel is https://travel.gc.ca.

As always, we recommend consulting legal and tax advisors who are familiar with living abroad to understand the implications for your particular situation.

Keep Time on Your Side

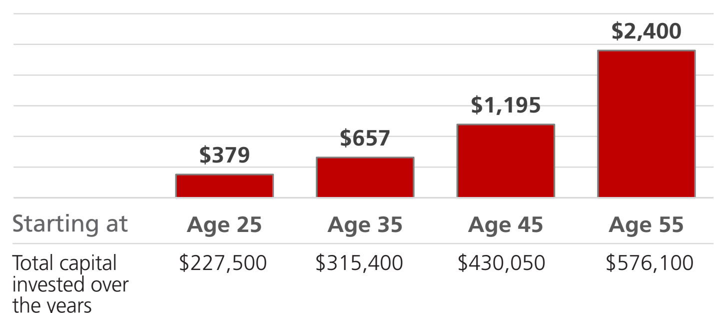
"You may delay, but time will not." - Benjamin Franklin

It is often said that procrastination is the thief of time. As we begin another year, don't let procrastination preclude you from using time wisely to generate wealth.

Perhaps there is an opportunity to put funds to work that are currently sitting on the sidelines. Or how about passing along some financial wisdom to younger generations to teach the value of time and compounded growth? The chart to the right shows the impact that time can have on generating retirement savings. In order to accumulate a $1 million nest egg by the age of 75, an investor would need much less capital the earlier the start.

Remember that time can be one of an investor's greatest allies.

Monthly Amount Needed to Accumulate $1M by Age 75
(Assuming a 5% Compounded Annual Rate of Return)



Note: Assumes a return of 5% compounded annually on the total annual amount invested, with taxes and expenses ignored. Monthly amount = annual amount divided by 12. For illustrative purposes only.

Forward Planning

RRSP, ASAP: Thinking Ahead for Children

If you have teenage children or grandchildren, they may have a part-time job that provides them with spending money or a means to build up savings for their post-secondary education. These jobs can provide financial lessons at an early age, and teaching the value of investing in a Registered Retirement Savings Plan (RRSP) should not be overlooked.

Often, the income earned within a part-time job is less than the basic personal amount for tax purposes. As such, an income tax return may not be filed because no taxes are owed. However, if this earned income is not reported, it results in a lost opportunity to generate RRSP contribution room. This means that the child loses the potential opportunity to compound savings for additional years on a tax-deferred basis and reduce a future personal income tax liability through annual tax deductions.

If the child doesn't contribute to the RRSP in the current year, the unused RRSP contribution room carries forward. This can have a benefit as it can be used to make a contribution in future years to reduce taxes. Even if they do contribute to their RRSP and their taxable income is below the basic personal exemption, they can elect not to claim the RRSP deduction until a future year when they are in a higher tax bracket, since non-deducted RRSP contributions carry forward indefinitely.

Having built up an RRSP balance while children are young may provide additional benefits as they grow older. They could potentially access up to $25,000 from the RRSP under the Home Buyers' Plan to aid in the purchase of a home, or they could time withdrawals to create a tax-efficient income-replacement strategy to match a maternity leave or a sabbatical from work. Don't overlook the value of an early start!

Reminder: RRSP contributions for the 2016 tax year must be made by **March 1, 2017**. Contribution limits are 18% of the previous year's earned income, to a maximum of $25,370 for 2016, less any pension adjustment or past service pension adjustment and plus any pension adjustment reversal and unused contribution room carried forward. For the 2017 tax year, the RRSP contribution limit increases to $26,010.

Note that the 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.

Changes May Affect You

New Rules to Address the Hot Housing Market

Last fall, the federal government took action to respond to concerns over the rise in housing prices, largely driven by the Toronto and Vancouver markets. A look back in time shows just how pronounced the increase in the average price of a home in these markets has been over the past 20 years:

	2016	1996	% Change
Canada	$474,590	$150,899	215%
Toronto	$755,755	$196,476	285%
Vancouver	$864,566	$288,268	200%

Source: Canadian Real Estate Association (2016 figures are Sept. 2016).

In an attempt to cool the market, here are some of the changes:

Principal Residence Exemption (PRE)

It has been proposed[1] that as of the 2016 tax year, all home sales for which the PRE is claimed must now be reported to the Canada Revenue Agency (CRA). In the past, when a principal residence was sold it did not need to be formally reported to the CRA if the capital gain was fully exempt due to the PRE. Although the PRE rules have not changed and gains from the sale of a primary residence remain tax free, this change is intended to improve compliance.

New Mortgage Stress Test

Starting Oct. 17, 2016, a stress test that used to apply to only variable rate mortgages or fixed rate mortgages with terms less than five years will now be used for all home buyers who have less than a 20% down payment. Borrowers must be able to qualify for their mortgage using a higher interest rate than they will actually be paying. It is expected that first-time homebuyers will be most affected. New mortgage insurance rules will also apply for low-ratio mortgages.

How Does This Affect You?

If you are selling your principal residence, you will need to report it on "Schedule 3, Capital Gains" of the CRA *T1 Income Tax and Benefit Return* for the year of sale. Penalties may apply if you fail to report the sale.

If you have a personal trust that was created with the intent of using the PRE, be aware that only certain trusts will be able to claim the PRE as of the 2017 tax year. Transitional relief will be provided, so seek assistance from a tax expert if you may be affected.

Note: 1. At the time of writing, changes have not received Royal Ascent.
Source: fin.gc.ca/n16/data/16-117_2-eng.asp

Planning for Care of the Elderly

Like many aspects of financial planning, starting early can have benefits and this is no exception when it comes to planning for elderly care. All too often, planning is put off until too late because conversations are difficult or uncomfortable. However, a crisis can force the need to make quick decisions, under stressful conditions and with insufficient information. Planning well in advance is not only important from a financial perspective – it can also help to maintain familial harmony, by helping family members to agree on a suitable path forward.

Having the Discussion

As you plan for the discussion, here are some things that should be addressed with aging family members:

Power of Attorney — Power of attorney documents are important to have in place for a time when an individual may need help managing their affairs or in the event of incapacity. Remember that in order to sign any type of power of attorney document, a person must be mentally capable, so planning ahead is important.

Estate Planning — A basic estate plan should be in place, including an up-to-date will and naming an estate administrator/ executor. Financial information for aging individuals should be kept in a place where a trusted person has access. Helping the elderly to get the support to construct a comprehensive estate plan can also have its benefits. Even after retirement, putting a proper plan in place can help to minimize taxes or create a legacy, as examples.

Types and Cost of Care — Understanding what types of care are available, the associated cost and what is desired by the individual in question is an important start. There are many options for caregiving support, from assisted-living facilities to full-time, live-in caregiving. The cost can widely vary depending on whether the care is government-supported or private.

Many families are not prepared for the potential future cost of care; some may not be aware that government programs do not fully cover long-term care costs. Across the provinces, the out-of-pocket cost for basic, long-term care can average around $1,500 per month for government-supported facilities and rise to in excess of $4,000 per month for private facilities.* By planning ahead, potential costs can be better managed, such as by building them into a financial plan or using long-term care or critical illness insurance.

Support for Caregivers

Many informational resources and organizations are available for support, depending on your place of residence. Keep in mind that there are also various forms of government support for caregiving. Under certain conditions, the federal family caregiver tax credit may be available if you are caring for an elderly family member in your home. As well, some caregiving expenses may be claimed under the medical expense tax credit. The disability tax credit may also provide significant tax benefits. Provincial tax relief may also be available. The Employment Insurance compassionate care benefit may provide some assistance to those who have temporarily left work to provide care to a gravely ill family member. We recommend working with a tax accountant that can advise on your particular situation.

Planning for elderly care can be stressful, but starting the process early can help you to find the best resources available and help to minimize any associated anxieties. We remain here to provide support with any financial or estate planning matters.

Source: *Varies by province of residence. Sun Life Financial "Long-Term Care Costs", 2016.

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