Quarterly Exchange

Q4 2014

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Through the *Quarterly Exchange,* we'll keep you up-to-date on current investment trends and strategies. We are committed to working one to one with you to help you achieve your financial goals. Please contact us if you have any questions or wish to discuss any of the articles in this newsletter.

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NORTH AMERICAN & INTERNATIONAL ECONOMIC HIGHLIGHTS

By Benjamin Tal, Deputy Chief Economist, CIBC World Markets

A few observations regarding the current situation:

Oil – There is little doubt that a year from now, most people will not remember the amount by which the S&P 500 and the TSX fell during the October correction. But they will remember how quickly oil prices fell. The recent softening in the oil market is a surprise. So what is a reasonable working assumption here? While many suggest that OPEC is engaged in a market share war, the reality is that to date, OPEC did not lose market share globally. Any market share lost in the US was offset by increased sales to emerging markets. The decision by OPEC to not cut production at this point is a major development. But to what extent will Saudi Arabia be happy with, say US$65-US$70/bbl oil? Note that in 2012, we have also seen a dramatic price decline (from US$105-US$80/bbl) and back then the Saudis were also slow to respond. At this point, sentiments in the market are negative, and oil prices can visit new lows. But given that markets tend to overshoot, a reasonable assumption is that during the course of the coming year, oil prices will find their way to the US$80-US$90/bbl range.

The Fed – The Fed is becoming a bit more aggressive. There is growing realization that rates should rise at one point in 2015. The Fed is facing the following twin risks: move too quickly and kill the recovery or move too late and allow inflation to get out of hand. From a risk management perspective, the Fed might try to deal with those risks by raising rates very slowly (using a repo rate to soften the market) and probably pausing at, say around 1%, to assess the situation. At this point, a reasonable working assumption is that the Fed will move in late Q1 or in Q2. Note that at this point the market is not pricing in any move by the Fed.

The Bank of Canada – The Bank of Canada must be in a bit of disarray at this point. The main communication from the Bank until recently was that the economy is still operating with a significant amount of slack, and thus there is no urgency to raise interest rates. Since then, however, indicators such as GDP growth, the job market, inflation and exports went against the Bank's forecast and surprised on the upside. The reality is that if it were not for the recent decline in oil prices, the Bank probably would have changed its language in a significant way. However, lower oil prices are a net negative for the Canadian economy and inflation – a factor that will provide the Bank with an excuse to lag the US in raising rates.

So the Bank might get what it wants but for the wrong reasons. We expect the Bank to move 3-4 months after the Fed. In their communication next week the Bank, in all likelihood, will focus on the negative impact of lower oil prices on the economy. We estimate that at this point, the decline in oil prices (if sustained) will cut GDP growth in the coming years by roughly 0.3%. But of course the damage will be felt mainly in the west.

CRA Settling Audits Over Iffy Tax Shelters

By Jamie Golombek, Managing Director, Tax & Estate Planning, CIBC Wealth Advisory Services

As we get closer to year end, you may be approached by someone trying to sell you a tax shelter. In the past, such shelters were often based on questionable donation schemes in which you made a cash payment and acquired some property in return.

These were then gifted to a charity with the result that you received a donation receipt that was much higher than the amount of cash you actually "donated."

Some of these "gifting tax shelter arrangements" involved the issuance of promissory notes while others involved donation of "in-kind" property.

In all such cases, however, the Canada Revenue Agency has reassessed all participants and denied the donation tax credits claimed.

These cases have also gone to court, with three of them reaching the Federal Court of Appeal.

In each of these cases, the tax shelter arrangements promised a "profit" to participants in return for a payment and in each case, the cash benefit for the taxpayer exceeded the cash outlay.

While each taxpayer tried to argue in court that their specific arrangement was legal, in each case, the Appeal Court concluded that the taxpayer's donation tax credit be denied entirely and it was reduced by the Court to zero. Earlier this month, the CRA issued a statement warning Canadians who may have participated in these gifting tax shelter arrangements that such gifts "do not necessarily result in a donation tax credit."

As a result of this, the CRA has issued reassessments to numerous taxpayers denying their donation tax credits. The CRA also reminded us that it audits every gifting tax shelter arrangement.

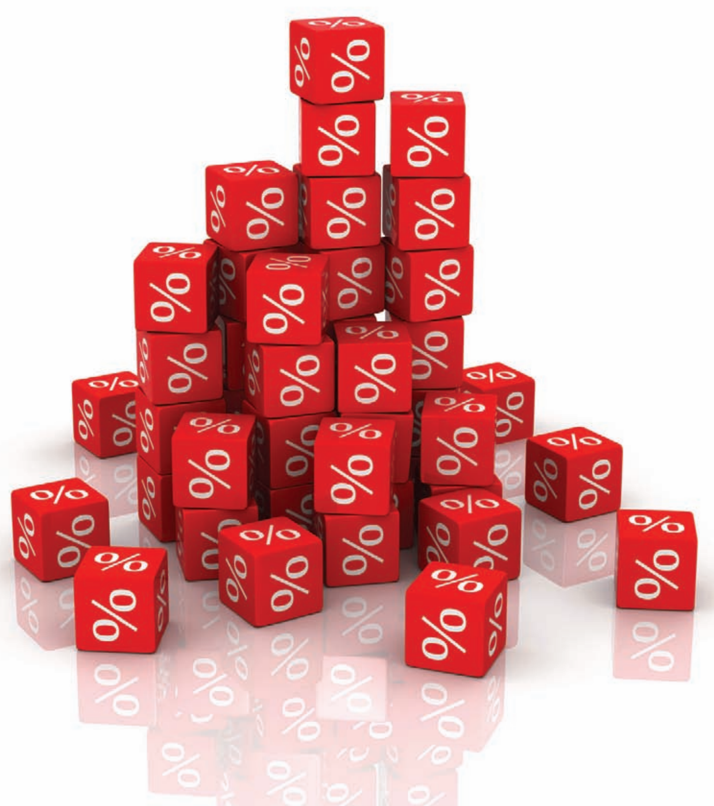
If you've previously participated in one of these arrangements and had your donation claim denied, you may have filed a notice of objection. Recently, the CRA has been sending letters to affected taxpayers offering to resolve your objection.

If you accept the offer made by the CRA, your objection(s) will be resolved and your return will be reassessed, concluding the dispute process. You would then avoid costs associated with going to court. The CRA stated that it "is not considering changes to the terms it has offered and will not make another offer containing more favourable terms. Any suggestion to the contrary is false."

If, on the other hand you refuse the CRA's offer, the CRA warns that it will maintain its position that you aren't entitled to the donation tax credit you claimed and that it will take "further action on your objection without advance notice," meaning that you will likely end up in Tax Court.

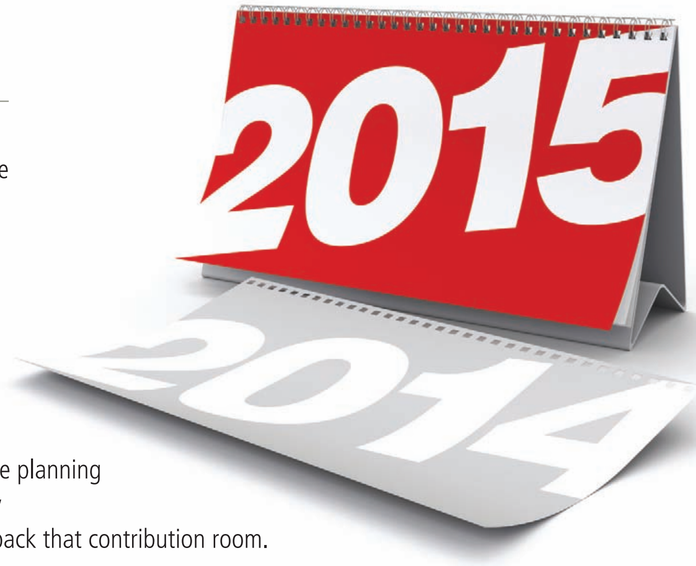
If you've filed an objection but still haven't heard from the CRA, be patient, as the CRA is continuing to issue these resolution letters in the months ahead and may still contact you to resolve your objection.

If you participated in one of these shelters, you should have your own, independent legal and tax advice before deciding to either accept the CRA's offer or reject it and try your luck in court.



This article originally appeared in The National Post on November 15, 2014

2014 Year-End Tax Tips



The end of the calendar year is coming up quickly, so now is the time to consider some year-end tax planning options:

Be strategic with your TFSA

If you haven't already contributed to your existing Tax-Free Savings Account (TFSA), do it before year end. Canadian residents 18 years of age and older can contribute up to $5,500* to their TFSA in 2014, plus any unused contribution room and any eligible amounts withdrawn in previous years. Alternatively, if you are planning a TFSA withdrawal in early 2015, consider withdrawing the funds by December 31, 2014, so you will not have to wait until 2016 to get back that contribution room.

Consider donating securities to charity

Are you thinking of donating money this year? Gifting publicly-traded securities, including mutual funds, with accrued capital gains to a registered charity or a foundation not only entitles you to a tax receipt for the fair market value of the security being donated, it offsets capital gains tax too.

RRSP contributions

Although you have until March 2, 2015 to make RRSP contributions for the 2014 tax year, contributions made as early as possible will maximize tax-deferred growth. If you have maximized RRSP contributions in previous years, your 2014 RRSP contribution room is limited to 18% of income earned in 2013, with a maximum contribution of $24,270, less any pension adjustment.

Review your asset allocation

Investment income can be taxed in different ways, depending on the types of income and type of account in which the investments are held. Year end is an excellent time to review the types of investment that you hold, and the accounts in which you hold them.

Salary vs. dividends for business owners

If you are a business owner, it's important to sit down with your accountant and determine the best combination of salary and dividends to pay yourself. These two forms of income are taxed very differently.

*The annual contribution limit from 2009 to 2012 was $5,000.

Understanding Risk

Risk is one of those four-letter words that people try to avoid, particularly when it comes to investing their hard-earned dollars. Because although risk does not necessarily mean that you're going to lose all your money, it's this image that often springs to mind when the subject is first broached.

Having said that, it's impossible to completely eliminate risk since all investments carry some degree of it. The key to being a successful investor is to determine the level of risk that you are prepared to tolerate, and then invest accordingly. But before doing this, you need to understand risk and the various forms in which it can appear.

Broadly speaking, risk is the possibility that the expected return on your investment may not be fully realized. This includes the possibility that you may lose some principal. However, there are risks that you may consider when assessing an investment.

- **Inflation Risk:** The danger that rising prices will reduce the purchasing power and real rate of return on your investment over time.
- **Interest Rate Risk:** The possibility that a change in interest rates may dictate a drop in the value of your investments. For example, rising rates can make dividend yields on current investments less attractive.
- **Economic Risk:** The danger that a downturn in the economy, or other significant economic event, will depress the value of your investments by reducing earnings capabilities.
- **Market Risk:** The possibility that events in the market itself may have an adverse effect on the value of your investments.
- **Specific Risk:** Relates more directly to the individual investment itself. It covers such elements as new technology making a certain firm's products obsolete, or greater competition reducing earning capabilities.

With a greater understanding of the various forms of risk, you'll be in a better position to find ways to help reduce risk.