Macquarie Private Wealth
A world of opportunities

MACQUARIE

OUR**VIEW**

VOLUME 1, EDITION 2

THE PAYOFF OF PLANNING

David Bassett, BA, CFP
Investment Advisor
E: david.bassett@macquarie.com
T: 604 640 0322

Gigi Yiu, BA, FMA
Investment Services Associate
E: gigi.yiu@macquarie.com
T: 604 640 0324

Stephanie Falcon
Investment Services Assistant
E: stephanie.falcon@macquarie.com
T: 604 640 0325

Macquarie Private Wealth Inc.
550 Burrard Street, Suite 500
Vancouver, BC V6C 2B5
F: 604 640 0300

Don't forget to make your 2010 Tax Free Saving Account contributions.

☎ Toll-free 1 866 640 0400

▶ macquarieprivatewealth.ca

The Greek debt crisis has been a stark reminder that complacency and lack of planning can lead to disaster. Rewinding the clock back to the 1990s, we should be reminded that Canada and Greece were in a similar debt position. Net government debt as a percentage of gross domestic product (GDP) had exceeded 70 per cent in both countries. At that time, Canada's sovereign debt was downgraded from its AAA credit rating.

So, where did Canada "go right"? Beyond learning the important lesson of not spending beyond one's means, Canada's success in more quickly responding to its national debt issue has helped it to emerge as one of the more healthy financial economies in the world today. In the early to mid-1990s, the Canadian government took active measures to cut federal spending and balance the budget. Increased tax revenues and falling unemployment also contributed to reducing the deficit. At the same time, falling interest rates and increased purchases of Canadian goods and services by the U.S. helped to boost Canada's economy. As a result, by the late 1990s, Canada was producing federal budget surpluses.

Contrastingly, Greece continued to spend using borrowed funds. This, complicated by a lack of internal revenue generation, an over-reliance on the public sector for employment and other factors, has led to net government debt ballooning to well over 100 per cent of GDP almost 15 years later. Canada's decision to reduce debt and restore financial stability helped to prevent a crisis similar to what we are now seeing in Greece and in other European economies. In these stressful times of market uncertainty, it may be helpful to remember the longer-term virtues of good planning. Your investment portfolio has been built from a carefully constructed plan and your investments are designed to meet your needs over the longer term. As such, keep to the principles set out in that plan — these form the strong foundation necessary to meet your long-term goals. Should you wish to consider fine tuning or rebalancing your portfolio, please don't hesitate to contact us. We can help to identify opportunities or provide the advice that you might need.

FOLLOWING UP

POST TAX SEASON REMINDERS

Now that the personal income tax season is over, you may be breathing a sigh of relief. But just because you've filed your tax return, you may not be off the hook just yet. Here are a few things to remember:

Notice of Assessment

Once a tax return has been filed, Canada Revenue Agency (CRA) will send a Notice of Assessment (NOA). This contains useful information and should be reviewed when received. The text portion of the NOA notifies the taxpayer of any unused capital losses, unused tuition carry-forwards for students, etc. The NOA will also indicate any unused Tax-Free Savings Account (TFSA) contribution room. In addition, the NOA contains a box with Registered Retirement Savings Plan (RRSP) deduction limit information that indicates contributions made during the tax year, any unused contribution room available, and the total limit for the next tax year. As your 2010 RRSP deduction is limited to 18 per cent of 2009 earned income (to a maximum of $22,000), minus any 2009 pension adjustment, the retirement income that will be provided by your RRSP may not be sufficient to meet your expectations for retirement. We can help with this planning, or with any other investment opportunities identified by the NOA such as unused TFSA or RRSP contribution room. Taxpayers should remember that the NOA does not mean that CRA agrees with your tax return. As such, CRA may conduct a further review of your tax return and issue a Notice of Reassessment should discrepancies be identified.

Review of your return by CRA

Each year, CRA conducts reviews of various tax returns. Some returns are selected randomly; others are selected after comparing tax return information to third-party sources or because the individual may have a history of review. Reviews do not necessarily constitute an audit. Audits involve a more in-depth process that occurs after an income tax return has been processed and has undergone a review. In this case, CRA will often assign an auditor to conduct further examination of the taxpayer's books and records.

Retaining supporting documents

Remember: all persons required to pay or collect taxes must legally retain supporting documents in the event that CRA requests them. Books and records are required to be retained as they permit taxes payable to be determined and supported by source documents (e.g., sales invoices, credit card receipts, formal contracts, work orders, etc.). Any supporting documents, such as accountants' working papers used to determine taxes payable, are also considered part of the books and records. Books and records must generally be stored in Canada. The Income Tax Act requires individuals to keep these records for at least six years from the end of the last taxation year to which they relate (not the year of the transaction, but the year of the tax return in which the claim has been made). Failure to provide the requested information may result in prosecution and individuals convicted may be subject to a fine and/or imprisonment.

If you do not agree with CRA

If you have filed taxes and do not agree with the NOA, contact CRA by phone. Should the issue still not be resolved, taxpayers may file an objection online (for registered accounts), by writing to the Chief of Appeals of the appropriate tax services office, or by completing the form T400A, "Objection —Income Tax Act."

BETTER PLANNING

"MINIMIZE" YOUR REFUND

Did you receive a tax refund this year? If you consistently receive tax refund cheques each year, it may be a sign of poor planning. Why provide the government with an interest-free loan each year in the form of excess tax payments when you can invest that amount instead? If you are earning a salary, your source deductions may not properly reflect your circumstances. Consider filing CRA Form T1213 with your employer to request a reduction in taxes deducted if you anticipate claiming certain deductions that will give rise to a refund.

A good example of this would be RRSP contributions. You usually need to file Form T1213 every year; however, you may make a request to reduce taxes deducted for a period of two years if you have deductible support payments that are the same or greater for more than one year. If you are self-employed, or are otherwise required to make tax payments quarterly, you may wish to consider changing the basis on which you calculate your payments. Either way, this will help you to optimize your tax payments over the year.

The comments contained herein are general in nature and are not intended to be, nor should be construed to be, legal or tax advice to any particular individual. Accordingly, individuals should consult their own tax advisors for advice with respect to the tax consequences to them, having regard to their own particular circumstances.

CHANGES COMING

YOUR CPP BENEFITS MAY BE AFFECTED

At the end of last year, changes were made to the Canada Pension Plan (CPP) that may make starting early CPP payments less attractive. These changes begin to take effect next year but will not affect those who have already started to receive their CPP retirement pension before the end of 2010. Some of the main changes include:

Adjustments for early/late payments

Downward or upward adjustments made to the monthly pension amount received by individuals who decide to start receiving CPP pensions before or after the age of 65 will change. Currently, CPP pension benefits are permanently reduced by 0.5 per cent per month (6.0 per cent per year) for each month before an individual's 65th birthday that the pension is started, to a maximum of 30 per cent. Over a five-year period beginning in 2012, this will increase to 0.6 per cent per month (7.2 per cent per year) to a maximum of a 36 per cent reduction in pension benefits. Conversely, after age 65, CPP pension benefits are currently increased by 0.5 per cent per month (6.0 per cent per year) for each month that the pension is taken after age 65 and up to the age of 70, to a maximum of 30 per cent. Over a three-year period beginning in 2011, this will increase to 0.7 per cent per month (8.4 per cent per year) for each month that the pension is started after the age of 65 and up to the age of 70, to a maximum of a 42 per cent increase in pension benefits. A greater reduction in pension benefits for early receipt of payments and a greater increase in benefits for late receipt of payments may influence the timing decision of when to apply for the CPP pension.

Elimination of work cessation test

Currently, in order to apply for early receipt of CPP payments an individual must stop working by the end of the month before and during the month in which the CPP retirement pension begins or the individual's earnings must be less than the current monthly maximum CPP retirement pension payment (currently $934.17 per month) in the month before and during the month in which the pension begins.

Beginning in 2012, this test will no longer apply. The elimination of this rule may better assist those between the ages of 60 and 65 to plan for retirement by allowing employment earnings to be supplemented by CPP benefits.

Required contribution under age 65

Currently, individuals who receive CPP pension benefits and choose to return to work are not required to restart CPP contributions.

Beginning in 2011, those under the age of 65 (and their employers) receiving CPP pension benefits while continuing to work will be required to make CPP contributions but will earn additional pension benefits based on the rate of pensionable earnings. Those between the ages of 65 and 70 who are working and receiving CPP benefits will have the option to contribute, which will also result in increased retirement benefits.

Remember: you must apply to receive your CPP benefits; they are not paid to you automatically. For an estimate of your CPP retirement pension, a CPP Statement of Contributions is available. Consult www.servicecanada.gc.ca for more information.

TAX STRATEGIES FOR BUSINESS OWNERS

CONSIDER SETTING UP A HOLDING COMPANY

A holding company may be structured to own the shares of an operating company that conducts day-to-day business. There are a variety of benefits associated with creating a holding company for your business:

- **Tax-free dividends** — The holding company may be allocated earnings from the operating company as an intercorporate dividend, which generally is a tax-free transaction, versus paying out the dividends to an individual who is personally taxed. The holding company can then use these non-taxed funds for investment purposes, which maximizes the initial principal being invested.
- **Income splitting** — The holding company may facilitate income splitting by paying income to others, such as family members. This can be done via salary payments, if the individual is doing work for the company, or dividend payments. Children up to 18 years of age are taxed at the highest marginal tax rate for dividends. However, once they reach 18, they may be eligible for the significant tax breaks that may be associated with dividend payments.
- **Ability to time payments** — Dividend payments from the holding company may be timed to optimize the personal tax situation of the individual. In years where personal tax liabilities may be high, the individual may opt not to pay out dividends from the holding company. If you believe that there may be tax advantages to setting up a holding company, we recommend seeking advice from a tax professional.

The comments contained herein are general in nature and are not intended to be, nor should be construed to be, legal or tax advice to any particular individual. Accordingly, individuals should consult their own tax advisors for advice with respect to the tax consequences to them, having regard to their own particular circumstances.

HIGH-YIELD BOND FUNDS MAY OFFER OPPORTUNITIES

As central banks have positioned themselves to raise interest rates, investors with a higher risk profile may look to fixed-income investment vehicles such as high-yield bond funds for inclusion within their portfolios. A high-yield bond, or "junk bond," is a bond that is issued by a corporation with a non-investment grade credit rating (below BBB as rated by Standard and Poor's or Baa by Moody's).

Corporations with weaker balance sheets — such as those with high amounts of debt or uncertain future prospects — or emerging companies, are assigned lower credit ratings given that the probability of default in repaying debt is higher than with those corporations with stronger balance sheets, or more established operations.

As a result of increased risk, high-yield bonds typically have higher yields than investment grade corporate bonds. High-yield bond yields are typically not correlated with government yields. In early recovery cycles, as government yields rise, high-yield bond prices have been shown to increase as an improving economy generally signals a decreased risk of credit defaults, while government bond prices have declined. A high-yield bond fund, a portfolio of high-yield bonds, may be a suitable addition as you look to another asset class to diversify your portfolio.

Here are the advantages associated with high-yield bond funds:

- **Lower volatility** — Relatively shorter maturities and lower sensitivity to changes in interest rates tend to lower volatility. High-yield bonds are typically issued with terms of 10 years or less and are callable after four or five years versus higher-rated borrowers like investment-grade corporations that may issue securities with longer maturities.
- **Diversification** — Within a portfolio, high-yield bonds typically have low correlation to other fixed income classes that may enhance portfolio diversification. A high-yield bond fund also offers diversification as the potential default and associated losses of any one bond may be offset by the remainder of the high-yield bonds within the fund.
- **Priority ranking** — High-yield bond holders usually rank second to senior lenders, such as banks, but ahead of all equity holders in the event that the issuer is liquidated.
- **Access to high-yield bonds** — Many funds have greater access to the market for high-yield bonds, which are often issued through private placements and may be initially unavailable to the retail market.

One of the greatest disadvantages of investing in high-yield bonds is the risk of default. It may be difficult to assess the default rates for high yield bond funds because the fund manager may have the opportunity to dump bonds before they actually default and replace them with new bonds. However, the fund's average credit quality may be used as an indicator, with a lower average credit rating potentially representing a higher risk of default.

There is also the risk of a high-yield bond reducing in value if a company's financial position deteriorates and its credit rating is downgraded. Investors interested in this asset class need to consider both the benefits and risks when deciding to include high-yield bond funds within an investment portfolio. Please don't hesitate to contact us if you would like to discuss whether a high-yield bond fund may make sense to add to your portfolio.

This material is provided for general information and is not to be construed as an offer or solicitation for the sale or purchase of securities mentioned herein. Every effort has been made to compile this material from reliable sources however no warranty can be made as to its accuracy or completeness. The comments contained herein are general in nature and are not intended to be, nor should be construed to be, legal or tax advice to any particular individual. Accordingly, individuals should consult their own tax advisors for advice with respect to the tax consequences to them, having regard to their own particular circumstances. Before acting on any of the above, please seek individual financial advice based on your personal circumstances. Commissions, trailing commissions, management fees/expenses may be associated with mutual fund investments. Read the prospectus before investing. Mutual funds are not covered by the Canada Deposit Insurance Corporation or any other government insurer, are not guaranteed and their values will fluctuate. There is no assurance a fund will maintain its net asset value or that the amount invested will be returned to you. Past performance may not be repeated. However, neither the author or Macquarie Private Wealth Inc. (MPW) makes any representation or warranty, expressed or implied, in respect thereof, or takes any responsibility for any errors or omissions which may be contained herein or accepts any liability whatsoever for any loss arising from any use or reliance on this report or its contents.

No entity within the Macquarie Group of Companies is registered as a bank or an authorized foreign bank in Canada under the Bank Act, S.C. 1991, c. 46 and no entity within the Macquarie Group of Companies is regulated in Canada as a financial institution, bank holding company or an insurance holding company. Macquarie Bank Limited ABN 46 008 583 542 (MBL) is a company incorporated in Australia and authorized under the Banking Act 1959 (Australia) to conduct banking business in Australia. MBL is not authorized to conduct business in Canada. No entity within the Macquarie Group of Companies other than MBL is an authorized deposit-taking institution for the purposes of the Banking Act 1959 (Australia), and their obligations do not represent deposits or other liabilities of MBL. MBL does not guarantee or otherwise provide assurance in respect of the obligations of any other Macquarie Group company. Macquarie Private Wealth Inc. is a member of the Canadian Investor Protection Fund and IIROC.