

INVESTMENT FOCUS

Personal Newsletter from Watermark Stone Wealth

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Perhaps a result of the time that many of us had during the lockdowns, we have been receiving more questions about life insurance and estate planning. We 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.

It is also the start of the season of giving and in this issue we 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!

– Doug

How Often Are You Checking?

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, father of behavioural finance, suggests that it's not just our biases that can influence poor 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 advisors, we are 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 day-to-day focus on your portfolio to those 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>

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Be Aware: TFSA Overcontributions & Electronic Notifications

A recent article published in the popular press reminds us of the importance of 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.”

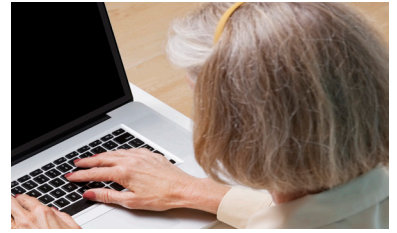
The article discusses a taxpayer who was sent a warning letter electronically to his CRA “My Account” due to excess TFSA contributions. The taxpayer claimed he never saw this letter. Two years later, when his Notice of Assessment (NOA) detailed the penalties and interest owed, he took action to remove 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 upheld the decision not to waive the penalty. The article is a good reminder to not only be aware of your TFSA limit, but to 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,” allowing 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.

It’s prudent to keep good records of your TFSA transactions. When checking *My Account* for contribution room information, be aware that 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



The Season of Giving: “Doing Good” and Benefitting Your Taxes

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. Here are just a handful of options:

Cash Donations — Any donation to a qualifying charity results in a tax receipt that entitles the donor to a tax credit. 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. This credit can be pooled with your spouse to be claimed by whichever spouse can best use it to their advantage. Donations can be carried forward for up to five years. Charitable donations are limited to 75 percent of net income in any year except upon death. Donations of up to 100 percent of net income are allowed for tax purposes in the year of death and the year preceding.

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

In-Kind Gifts — You may consider donating personal property which a charity can then convert to cash. For example, by donating a used car to charity, you may be eligible to receive a tax receipt for its appraised value. Special tax rules may apply to in-kind gifts so check with a professional tax advisor on how to best handle the situation.

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 disadvantage.

Donor-Advised Funds or Community Foundations — These may be cost-efficient alternatives to a private foundation by eliminating certain legal and administrative costs, while still allowing you to direct donations and achieve tax benefits. The benefit of a donor-advised fund is that the contribution will be 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 by the charity until distribution.

We can help provide perspectives on these or other options available and can recommend resources to support many of these endeavours. Please consult a tax advisor as it relates to your situation.

*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.

Business Owners & Family Succession — Changes as a Result of Bill C-208

Keeping a business in the family has become easier and less costly. Over the summer, Bill C-208 was passed. Before this, 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 also enables corporate reorganizations among siblings to take place 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.

What is Generational Wealth Planning?

After a lifetime of building wealth, many of us have a desire to leave a lasting legacy for our families. As such, some are now focusing on generational wealth planning to support this longevity. This goes beyond just designating bequests for (grand)kids through an estate plan. A generational plan considers future generations, including those you may never meet, with the objective of supporting your wealth's longevity in complement to traditional estate planning documents — these legal documents can help to distribute assets, but the generational plan keeps assets working into the future.

Start with a Plan and Document It — A generational plan should set out goals and provisions for how money will be used by future generations, as well as how it will be accessed and replenished. For instance, you may wish for family members to invest in themselves, stipulating that funds should be used for higher education, or a business start-up or expansion. By offering heirs the means to obtain an education or run a business for themselves, they can gain the experience needed to create wealth and grow it. Once you determine your desired goals and provisions, it is important to formally document the plan so that it can be passed along to future generations. You may also consider the use of certain tools (such as a trust) to support your plan.

Communicate Your Plan; Be the Family Resource — It is important to communicate your plan to family members. Often, parents keep their finances and related values secretive, missing the opportunity to pass along their ideals to children. A generational plan puts you in the position of leadership and

guidance by allowing heirs to understand your vision for your wealth after you pass away. While particular financial details need not be shared, the vision can act as a catalyst for meaningful family discussions. The plan can also form the basis of a family constitution, enabling future generations to carry forward the intentions set forth in the plan.



Even if a generational wealth plan isn't your desired path forward, there may be actions that can be taken to help protect and preserve assets for the future:

Consider Protection Tools, Such as a Trust — Certain tools may help to protect future wealth in situations in which beneficiaries may not be financially responsible or where you wish certain goals to be attained. A testamentary trust can provide protection by putting estate assets under the control of a responsible trustee. The terms of the trust can specify the timing and amount of distributions to be made to heirs. Other tools may be considered, such as life insurance, to help protect and grow assets.

Create a Professional Support System — Having a support system of trusted professionals may be a valuable part of ensuring a successful generational wealth transfer, especially when heirs may not have the skillset to independently manage funds.

Creating a generational legacy can be one of the greatest gifts you leave behind. For support as you plan ahead, please get in touch.

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? Statistics Canada has released a personal inflation

Changes in the Prices of Select Items: 1987¹ & 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, Report on Business Magazine, Apr. 2012, pg. 13; 2. StatCan 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, accessed 03/21; 9. At close on 6/7.

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.

Life Insurance as a Planning Tool: It's Never Too Late!

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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