NEWSLETTER OF
EY MANAGEMENT AND
NCIAL PLANNING IDEAS

Planning Ahead

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With the end of year of turbulent market activity almost upon us, thoughts no doubt turn reflective. There's no better time than now for us to get together and have a conversation about the year past, and what lies ahead.

Let's take the opportunity to review where your finances have taken you this year, especially to see whether your portfolio is still in alignment with your goals, as your asset allocation may have shifted. It will give us a chance to review not just your investments, but also all aspects of your financial life.

A new year is a new start. Let's plan today to make the most of it.

FOCUS ON INVESTING

Should you trust economic forecasts?

As 2011 draws to a close, we look back on a year of considerable investment volatility. Can we expect more of the same? Is there any way to know what lies ahead?

Here is a look at economic forecasts, what they mean, and what we should do with them.

Pack an umbrella

While forecasts can provide valuable insight as to where the economy and markets might be headed, it's not particularly wise to use them as a prescription for action. It's important to remember that forecasting is by no means an accurate science and many simply turn out to be wrong.

And when it comes to long-term or even mid-term predictions, they tend to be all over the map. Forecasting is much easier over the short term. We'll consider the "middle ground" when using forecasts to help formulate an investment strategy, weighing the most optimistic and most pessimistic outlooks for a reality that is likely to lie somewhere in the middle.

Stick to your plan

Making sense of those forecasts isn't easy. But there's no need to be confused — or alarmed — by what you read in the media.

The most important thing to remember during times of market and economic turbulence is to stick to your plan; it was created to be in line with your goals, your time horizon, and your risk tolerance. Still, now is an ideal time for us to sit down. We'll sift through what the experts are saying about 2012, and decide whether or not you should make any changes. ■

How you can turn fund losses into tax benefits

With the end of the year approaching, it's an ideal time to review the performance of your investments — in particular, mutual fund holdings that have declined in value.

Because fund performance sometimes results in a loss, depending on the markets in a given year, we need to pay as much attention to our "sell" strategy as we did to the steps that originally led us to make those investments.

The end of the year is a good time to consider selling underperforming mutual funds. We may not be able to revive them, but the right strategy can help minimize taxes and give the holdings one last crack at doing some good for your portfolio returns.

If the proceeds from those funds can be used in more promising investments, this could be the time to sell at a loss to improve your year-end tax position.

A good opportunity to 'sell low'

By redeeming fund units (outside your registered plans such as Registered Retirement Savings Plans) for less than their original cost, you will create a capital loss that can be used to offset capital gains on your income tax return. By reducing your capital gains, you reduce your tax bill. You may even be able to use that loss to reduce taxes in future or past years.

If you own money-losing mutual funds that are likely to make a year-end distribution, you take advantage of the capital loss for tax purposes and avoid a taxable distribution by redeeming before the distribution date (generally mid-December).

We need to carefully consider which of your mutual fund holdings are candidates for tax-loss selling. These should be investments we believe have little opportunity for recovery. We also need to weigh the financial benefits of tax-loss selling in each case.

When we create a capital loss, it must first be used to offset any capital gains earned in the same tax year. Any remaining losses can be carried forward indefinitely to future years or applied to gains from the previous three years.

How it works

Here's an example of how tax-loss selling can work to your benefit.

Let's assume you invested $80,000 in a mutual fund a few years ago (outside a registered plan) and sold that investment this year $100,000, for a profit of $20,000. You also sold a money-losing fund investment this year for a loss of $10,000. (See infographic.)

You would deduct the $10,000 loss from the $20,000 gain, leaving you with a capital gain of $10,000 for the year. Half that amount must be reported as a taxable capital gain on your income tax return, so you will pay tax on $5,000.

You can use a capital loss on any eligible investment to offset a capital gain on any other eligible investment. For example, your mutual fund loss could be used to offset gains from mutual funds, stocks, bonds, exchange-traded funds, or even investment real estate. However, capital losses can normally be used only to reduce or eliminate capital gains, not to offset other income.

There is one important caveat: When you sell a security to claim a capital loss, do not buy that security again for at least 30 days. Otherwise it will be deemed a superficial loss by the Canadian Revenue Agency and you won't be allowed to use it to reduce taxable gains.

Timing is important. Transactions need to be completed before year-end to qualify for your 2011 income tax return. Please refer to your tax professional or accountant for advice. ■

How tax-loss selling works

No tax-loss selling	Using tax-loss selling
$20,000 Amount gained from selling A	**$20,000** Amount gained from selling A **-$10,000** Amount lost from selling B
x 50% Only 50% of the gain is declared for tax purposes	$10,000 Net gain, after applying B against A x 50% Only 50% of the gain is declared for tax purposes
$10,000 Taxable capital gain, not using tax-loss selling	**$5,000** Taxable capital gain, using tax-loss selling

MONEY FILE

Power up your TFSA

A November 2010 survey by BMO Financial Group showed that while more than a third of Canadians have opened a Tax-Free Savings Account (TFSA), they know little about the wide range of investments that they can hold within those plans. As a result, investors may not be taking full advantage of the tax benefits and investment return potential of TFSAs.

The survey showed that 37% had no idea what investments are eligible for their TFSAs. Only 20% knew that mutual funds were eligible and 26% knew that Guaranteed Investment Certificates (GICs) could be included in their plans. The reality is that a TFSA can hold many types of investments. Here's a look:

It's not a simple 'account'

The range of eligible investments is similar to what qualifies for inclusion in a Registered Retirement Savings Plan (RRSP) or Registered Retirement Income Fund (RRIF). That means a wide selection of individual securities, such as eligible stocks and bonds, mutual funds, real estate investment trusts (REITs), annuity contracts, foreign currency, and more.

Diversifying beyond cash or savings-type investments in your TFSA can improve long-term growth potential and returns. Because your investment returns are completely tax-sheltered in the TFSA and tax-free upon withdrawal, the more you earn in your TFSA, the more you benefit from the tax advantages. Compounding of tax-sheltered returns can greatly increase your investment profits and leave you with a much larger pool of wealth than you would have if you invest in a taxable account.

Strategy is key

The investments you hold in your TFSA will depend on your financial goals, your risk tolerance, and other factors. We need to consider your TFSA as part of your overall investment plan, carefully balancing what you hold in your TFSA, RRSP, and non-registered investments. We also need to ensure that your investment decisions aren't driven solely by tax considerations, but that taxes are just one part of deciding how and when to invest.

We can make the most of your TFSA by exploring its full investment and tax-saving potential within your overall investment plan. ■

MONEY TALK

Manage the stress of an emergency

As the Canadian population ages, more of us in our 40s, 50s, and beyond are supporting the care of, or helping to care for, senior parents. There's a good chance that at some point we'll be called upon to deal with emergencies involving our aging relatives. Sometimes those emergencies require us to supply information needed for our parents' care or well-being.

When that time comes, you'll want to access that information as quickly as possible. You or your loved ones don't want to be scrambling to figure out necessary details when time is critical and stress is high.

The best way to make sure you can act quickly and confidently is to prepare in advance. Speak with your parents about their information, compile it and any documents you might need, and make sure they're easily accessible. The more knowledgeable you are, the better you'll be able to look after not just your parents, but yourself as well.

We recommend putting together the following:

Medical information

If a parent is in sudden need of medical care, supplying the right information in a hurry can be a lifesaver. Keep a list of your parents' blood types, medications, details of allergies, a history of past illnesses and surgeries, and contact information for doctors and other caregivers. You'll also want to have details of any medical insurance plans, as well as supplemental coverage such as critical illness insurance or long-term care insurance.

Financial information

You may be called on to manage or help manage your parents' finances in an emergency. This will require access to bank account information, credit card information, details of loans and loan payments, investment information, and any other pertinent financial details and documents.

Legal documents

Quick access to important legal documents is essential for medical and financial matters. If you or another family member has power of attorney to manage your parents' healthcare or finances, copies and originals must be easily accessible. Other information you may need in an emergency includes your parents' wills, their written instructions about the level of medical treatment they want if they can't express their wishes (sometimes known as a "living will"), and insurance policies. Other estate planning information should also be readily available. The documents and information you need will depend on your parents' situation. We can help you plan a strategy for gathering the necessary documentation, speaking with your parents, and deciding where their information should be kept for immediate access. ■

Stress test your portfolio

With so much financial market volatility this year, you might be feeling nervous about the security of the wealth you've accumulated in your investment portfolio. Fallout from economic concerns, government debt crises, global political turmoil, and even natural disasters has contributed to extreme market gyrations.

The timing is right for us to "stress test" your portfolio, to see how well it is positioned to weather current and future developments.

No EKG required

What is a stress test? Is it reason to get stressed? Rest assured you won't need to walk on a treadmill attached to a heart monitor. For your investments, it's simply when we review all your portfolio holdings to identify potential weak spots or problem areas.

We can review your holdings to assess vulnerability to potential shocks and make sure you're not overly exposed to any single country or industrial sector. We can also make sure you avoid overlapping investments in similar securities or funds.

We will look to see if your asset allocation is out of alignment with that of your last review, and we'll make adjustments to put it back in line.

Mitigating risk is key

We can then take action to fortify your investments so they can better cope with today's challenges and the challenges of tomorrow. We want to avoid the hazards of underestimating or ignoring the downside potential of financial markets — whether it's from unexpected developments or events that are currently unfolding.

We will also consider the possible impact of rising inflation and interest rates. Many experts expect rates to increase in 2012 and beyond. While moves are likely to be gradual, they can have an impact on performance and may influence the asset mix in your portfolio.

It's time for fine-tuning

We can also consider risks associated with investments in individual companies and mutual funds. Those risks change with volatility, global developments, and perceptions of the economy. Many companies and funds take steps to prepare for current and future turbulence or crises by managing currency exposure or business exposure to more turbulent global markets.

Of course, this doesn't mean we need to take an overly conservative approach. Trying to play it too safe or sitting out volatility may mean you miss out on major financial market advances or attractive buying opportunities. When markets are rocky, it's always a good test of your true tolerance for risk.

In the long run, our best strategy is a broadly diversified portfolio that provides a buffer against uncertainty, and is in line with your risk tolerance, your time horizon, and your goals. A stress test will help us make sure your portfolio is ready and well-focused. ■

The difference between value and price

BEING UNCLEAR ON the distinction between value and price can negatively affect your portfolio returns. Here's what you need to know:

How they differ

Price is what investors are willing to pay for shares of a company. It can move up or down in a matter of seconds as a result of general investor sentiment, the economic outlook, or short-term events.Value, on the other hand, is a reflection of the company's "intrinsic" worth and its future potential. It is far more constant because the factors that affect value don't usually change quickly.

For many investors, the true value of a company is its ability to generate a satisfactory long-term return. When the price of a stock fluctuates, it is unlikely that the value of the underlying investment has changed.

What this means to you

For future returns potential doesn't depend on how far the price has risen, but rather on how much higher it's likely to go. Investors may be reluctant to invest in a company in the wake of substantial share price increases, thinking that prices are already too high, only to miss out on gains as prices move even higher.

What really counts is price relative to a company's current value and prospects for the future. These are things we can help you determine. ■