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Personal Newsletter from Nicole Deters, Harbourfront Wealth Management – Gilman Deters Private Wealth

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Lessons From Generational Resilience

“Things will wax and wane; grow and decline. The same is true for economies, markets and companies. There’s little more dangerous than extrapolating today’s events into the future...”

– Howard Marks

One of our modern-day challenges is that technology has ushered in an era of instant communication and connectivity that seems to amplify awareness and sensitivity. There is never a shortage of negative news and today is no exception. Despite economic resilience and growth that has exceeded expectations, we may be distracted by new uncertainties: deleverage, higher rates and slower growth (ironically the goal of the central banks by raising rates!), to name a few.

Yet, we should be reminded that time changes all things. Consider the Millennials (born 1980 to 1994): For many years, they were said to be the first generation worse off financially than those before. As they have started to turn 43, purportedly the age when we ‘stop feeling young,’ they have outpaced previous generations. Millennial household income has surpassed that of prior generations at the same age: \$9,000 more than the median GenX (1965 to 1979) household income and \$10,000 more than the Boomers (1946 to 1964). Despite soaring real estate prices, Millennials are only slightly behind: 48 percent owned a home as 25-to-39-year-olds, compared with 50 percent of Boomers.¹ As they enter their peak earning years, the future looks bright.

The narrative wasn’t much different for the generations prior. Just 30 years ago, there were “dire predictions” about the economic prospects of GenX. They entered the workforce into an economy recovering from a recession described as “the deepest since the Great Depression.” Unemployment soared to 11 percent in the early 1990s after interest rates were aggressively raised to fight inflation. Canada’s future economic prospects looked bleak. An editorial in 1995 referred to “Bankrupt Canada” as “an honorary member of the Third World.”² And yet, to end the 1990s, Canada would end up taming its debt crisis to post strong GDP growth.

Likewise, many Boomers came into the job market in the 1970s, a period plagued by significant inflation, increasing unemployment (hence, stagflation) and low economic growth, as well as a stagnating stock market. Let’s not forget that in 1979, the front page of *BusinessWeek* magazine declared the “Death of Equities.”³ However, the Boomers have lived through one of the most fortuitous periods in investing history. If you were to have invested in the stock market in this seemingly bleak period, the total return today would be over 4,100 percent!⁴

Indeed, economic cycles come full circle and the rebound of the Millennials, and the generations before, serves as a reminder that time changes most things. We have no control over the stock market, the economy and other macroeconomic events; to a certain extent, many prove to be cyclical. Much of long-term investing success relies on the ability to accept this inevitable cyclicity by making the appropriate adjustments along the way, rather than attempting to evade it.

As one market strategist reminds us: “A good bet in economics: the past wasn’t as good as you remember, the present isn’t as bad as you think, and the future will be better than you anticipate.”⁵

1. www.theatlantic.com/magazine/archive/2023/05/millennial-generation-financial-issues-income-homeowners/673485/; 2. www.reuters.com/article/us-crisis-timeline-idUSTRE7AK0FF2011121; 3. <https://www.bloomberg.com/news/articles/2019-08-13/it-s-been-40-years-since-our-cover-story-declared-the-death-of-equities>; 4. S&P/TSX Composite Index Total Returns, 8/31/1979 - 1,911.69; 7/31/2023 - 81,536.38; 5. <https://collabfund.com/blog/everything-is-cyclical/>

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Do You Have Power of Attorney Documents in Place?

According to a recent survey, only 35 percent of Canadians have appointed a power of attorney (POA).¹ How about you? Do you have POA documents in place? While the names and obligations may vary by province, generally there are two types of POA intended to protect an individual should they become incapacitated: i) POA for property, which includes managing finances and other assets on behalf of the incapacitated; and ii) POA for personal care, which includes making healthcare decisions.

Here are some reasons why the POA should be a consideration:

- On average, we will live with good cognitive health to around age 77.² However, our average life expectancy is well beyond this age.
- Those over age 85 have a 1-in-4 likelihood of suffering from some form of dementia.³
- Regardless of age, life is unpredictable: accidents or unexpected health issues can occur at any time.

Even if a POA exists, consider reviewing your documents from time to time as circumstances can change. There may also be situations which may warrant revisiting your POA, including:

Personal wishes or specific instructions have not been discussed.

Engaging in conversations with family members and your “attorney” (the person(s) designated to make decisions under the POA) while you are “capable” can go a long way in maintaining familial harmony and ensuring your wishes are carried out. Recent surveys suggest the vast majority aren’t having these critical discussions. In one unfortunate case that led to litigation, two brothers couldn’t agree on the type of care for their mother — one wanted life-prolonging care while the other wanted hospitalization only for comfort.⁴

Multiple attorneys have been appointed. Many parents feel the need to treat children fairly by jointly naming them as attorneys; however, consider that in some situations the greater the number of attorneys appointed, the greater the opportunity for conflict.

How Well Are We Planning for Our Incapacity?

Here are a few surprising outcomes from recent surveys:

24% Have a plan for financial expenses in the event of dementia.¹

25% Believe there are no consequences to not having a POA.²

34% Have a plan for assets if unable to make financial decisions.¹

1. www.bloomberg.com/press-releases/2023-05-15/ig-wealth-management-estate-planning-study-despite-aging-population-most-canadians-lack-estate-plan; 2. www.rbcwealthmanagement.com/en-ca/insights/estate-planning-report-reveals-many-canadians-are-not-prepared

Attorneys have not been updated. Have your designated attorney’s circumstances changed? Updates may be needed to address the incapacity or death of a named attorney. Or, there may be complications if an appointed attorney moves outside the country, i.e., a non-resident attorney for property may be subject to rules that prohibit a financial advisor from receiving instructions. Often, there is value in naming a contingent attorney who can step in.

Underestimating the cost of care. While the appointed attorney for personal care is not personally responsible for funding the financial obligations of your desired care, if the associated costs are not properly planned for, this can unfairly complicate the attorney’s role. Alternate care may need to be considered, possibly against your wishes. Consider that the cost of care associated with incapacity, such as long-term care (LTC), can be extensive; on average around \$36,000 per year for a private room at a care facility, or in excess of \$130,000 at home.⁵ Planning ahead can help protect family members from an unexpected financial burden. Often when children are appointed as POA attorneys, they feel pressure to contribute.

If you have yet to give your POA the thought it deserves, why not make this a priority? Please consult an estate planning professional.

1. www.niaaging.ca/canadian-perspectives-on-estate-planning; 2. www.washingtonpost.com/national/health-science/research-shows-that-the-prevalence-of-dementia-has-fallen-in-the-united-states/2018/06/15/636d61ac-6fd1-11e8-bf86-a2351b5ece99_story.html; 3. www.chi.ca/en/dementia-in-canada/dementia-in-canada-summary; 4. *White v White*, 2017 ONSC 4550; 5. Based on \$33,349/yr. (2021), grossed up by 4% per year. www.advisor.ca/news/industry-news/most-canadians-arent-planning-for-long-term-care-costs-survey/. At home, based on avg. cost of care of \$30/hr., 12 hrs./day, 365 days/yr.

Billions Remain Unclaimed: Keep Your Assets Working Hard for You

For those of us who manage wealth on a regular basis, it continues to be surprising to see the growing number of assets that are forgotten or just not optimally put to work. Here are two actions we can all consider to help keep assets working hard for the future:

1. Consolidate financial accounts. The latest data suggests at least \$2.5 billion of funds remain unclaimed: the Bank of Canada holds \$11 billion of unclaimed balances¹ and the Canada Revenue Agency (CRA) has 8.9 million uncashed cheques, with a total value of over \$1.4 billion.² This sheer magnitude of funds should remind us of the benefits of consolidating financial accounts to ensure assets do not become orphaned over time. Consolidation can also provide other benefits, including better visibility to optimize asset allocation and tax efficiency, greater simplicity and improved legacy planning, among others.

Do any unclaimed funds belong to you or your loved ones?

To search for unclaimed assets, see: www.unclaimedproperties.bankofcanada.ca/app/claim-search. Check your CRA “My Account” for unclaimed cheques at: www.canada.ca/en/revenue-agency/services/uncashed-cheque.html

2. Consider fully maximizing tax-advantaged accounts.

Investing in tax-advantaged accounts can make a significant difference down the road. As one example, consider an investor who invests \$50,000 today at an annual rate of return of 6 percent. In 25 years, this investor would have almost \$215,000 if invested in a TFSA. Investing the same amount in interest-bearing investments in a non-registered account would yield only \$104,000 after taxes.³



Do you have available RRSP or TFSA contribution room? The latest statistics suggest that there is over \$1 trillion of unused RRSP contribution room available.⁴ And, as noted in last quarter’s newsletter, the vast majority of TFSA holders, at all wealth levels, have not maximized their contribution room.⁵

1. nationalpost.com/news/canada/how-to-know-if-you-own-any-of-the-1-8b-in-unclaimed-bank-accounts-in-canada; 2. www.canada.ca/en/revenue-agency/news/2022/08/approximately-14-billion-in-uncashed-cheques-is-sitting-in-the-canada-revenue-agencys-coffers.html; 3. Assuming a marginal tax rate of 50.25% on interest income; 4. At 2016; Stat Canada T: 111-0040 “RRSP Room”; 5. www.canada.ca/content/dam/cra-arc/prog-policy/stats/tfsa-celi/2020/table1c-en.pdf

RRIF Planning: Sometimes Forgotten — “In-Kind” Withdrawals

As we enter the final months of the year, this is often a time when retirees take their Registered Retirement Income Fund (RRIF) required withdrawals. Don't forget that an “in-kind withdrawal (transfer)” can satisfy part or all of the requirement; securities do not have to be sold.

An in-kind withdrawal involves transferring investments directly to a non-registered account or Tax-Free Savings Account (TFSA). There may be associated benefits: You will maintain ownership of the shares and it may minimize trading costs. An in-kind withdrawal from the RRIF to a TFSA, subject to available TFSA contribution room, could also allow for the future tax-free growth of the securities transferred.

For an in-kind withdrawal from the RRIF, the fair market value (FMV) of the shares at the time of transfer will be added to your taxable income and their cost base will be adjusted. For example, an in-kind withdrawal of 100 shares of XYZ stock trading at \$60 will be valued at \$6,000 (the FMV of the shares). This amount will be added to your taxable income. The adjusted cost base (ACB) of the transferred shares will now become \$6,000, regardless of the price paid when originally acquired. If the transfer is to a non-registered account, the ACB will be used when the shares are eventually sold to calculate the capital gain/loss. Keep in mind that if the transfer value is greater than the RRIF minimum withdrawal requirement, the excess amount will be subject to withholding tax.

Still Have Yet to Open the RRIF? Consider Planning Ahead

If you still have yet to open the RRIF, planning ahead is always recommended. Here are four practices that may require forethought.

1. Opening a small RRIF before the age of 71. The pension income tax credit generally begins at age 65, so this may be one way to take advantage of this non-refundable credit. You may also be able to split pension income with a spouse/partner, which can reduce taxes or improve access to income-tested government benefits.



2. Using a younger spouse's age to determine the RRIF minimum withdrawal rate. A younger spouse's age can minimize withdrawal amounts and maximize flexibility since you can always withdraw more than the required minimum if you need it (subject to withholding tax). However, you must elect to use a spouse's age when first setting up the RRIF, and this cannot be changed at a later time.

3. Making withdrawals closer to year end to allow greater potential tax-deferred compounding. Remember: for those who convert the RRSP to the RRIF at age 71, mandatory withdrawals aren't required until the year after the plan is opened.

4. Varying RRIF withdrawals with your tax bracket. For years in which you will be in a lower income tax bracket, consider the opportunity to make greater withdrawals than the minimum requirement to take advantage of the lower tax rate (subject to withholding tax).

The RESP: Helping Grandchildren Fund the Cost of Education?

A decade ago, an article published in the *Globe & Mail* compared the costs of education and the housing market to the 1980s to answer the question: Do young adults have it harder today? The conclusion: “Back in my day, economically speaking, life was easier.” One could argue that the same can be said in 2023. The chart (right) shows just how these costs have continued to rise over the decades.

It is, therefore, not surprising that many grandparents wish to help younger generations fund the cost of education. When it comes to the Registered Education Savings Plan (RESP), it is possible for grandparents to set up (as “subscriber”) the RESP for the benefit of grandchildren (as “beneficiary”). However, caution should be taken as there may be complications, such as in the following three situations:

1. The child does not pursue post-secondary education. While it may be possible to transfer up to \$50,000 of RESP accumulated income payments to a subscriber's RRSP, grandparents may be beyond the age of holding the RRSP. In this case, there are likely to be tax implications.

2. The grandparent retires outside of Canada. There may be tax implications for the subscriber, depending on the tax rules of the retiree's country. For example, in the U.S., the U.S. Internal Revenue Service doesn't recognize the tax-deferred status of the RESP, so it would be considered a foreign trust. While the RESP would continue to be tax exempt in Canada, annual income earned in the RESP, plus annual grants received, would be taxable to the subscriber on a U.S. tax return.

Education & Housing Costs vs. Family Income, 1984, 2012 and Today

	1984	2012	Today	% Change from 1984
Undergrad Tuition (A)	\$977	\$5,313	\$7,076	+624%
Average Home Cost (B)	\$76,214	\$369,677	\$709,218	+831%
Median Family Income (C)	\$48,500	\$71,700	\$104,350*	+115%
5-Year Fixed Mortgage (D)	14.96%	4.23%	5.51%	-63%
Unemployment Rate (E)	12%	7.2%	5.5%	-54%

A: StatsCan Table: 37-10-0150-01; B: CREA national average selling price in July 2023; C: *2020 data. <https://www.statista.com/statistics/484851/median-family-income-fpl-couple-families-in-canada/>; D: StatsCanada, Average of <https://www.ratehub.ca/best-mortgage-rates/5-year/fixed-at-08/12/23>; E: July 2023. Source: *2012 vs 1984; Yes, Young Adults Do Have It Harder Today; R. Carrick, *Globe & Mail*, 8 May 2012.

3. The RESP subscriber passes away. Many incorrectly assume that, upon death, RESPs are treated similarly to RRSPs and pass outside the estate to the beneficiary; however, this isn't the case. Generally, if there is no surviving joint subscriber or alternative plan in place, RESP assets would become part of the deceased subscriber's estate (i.e., the plan would collapse, with tax implications for income and grants received) and the value will belong to the beneficiaries of the estate. The estate beneficiaries may not be the same as the RESP beneficiary.

Given the potential complications, if a grandparent feels comfortable with the parents' discretion, it may be beneficial to consider gifting funds to parents to contribute to a child's RESP. There may be other options, such as setting up a family plan with multiple beneficiaries (siblings, cousins), so if one or more beneficiaries decide not to pursue a qualifying education, the plan's assets can be used by others. Providing explicit instructions within a will can help to pass along the RESP according to the subscriber's wishes in the event of death.

An Alternative to GICs: The Discount Bond Opportunity

As interest rates are at levels not seen in decades, there has been greater attention to low-risk, fixed-income investments like Guaranteed Investment Certificates (GICs). However, there may be a tax-efficient alternative that is worth consideration: the discount bond.

With the rapid rise in interest rates since the start of 2022, and unprecedented bond market volatility, many quality bonds are trading at discounts to their par values. These bonds can offer a tax-efficient alternative to GICs from a risk perspective, but may provide greater after-tax return potential. This is because when a GIC is held in a non-registered account, any income earned will be fully taxable at the investor's marginal rate — compared to capital gains and dividend income, which generally receive more favourable tax treatment. A discounted bond has a portion of the total return taxed at lower capital gains rates.

What is a Discount Bond?

First, let's look at the differences between a GIC and a bond. GICs pay a guaranteed return, expressed as an interest rate paid on the amount invested, which is taxable as interest income in a non-registered account. Since they aren't tradeable assets, they don't vary in price. At maturity, the original investment, including interest, is returned to the investor. Bonds, on the other hand, generally pay a coupon, or an annual interest rate (sometimes paid semi-annually), which is taxable as interest income. The coupon rate is expressed as a percentage of the bond's "face value" — the amount paid to the bondholder at maturity. Over the life of the bond, a bond's price can vary as interest rates change.

Take, for example, a 2-year, \$1,000 bond issued with a 4 percent annual coupon rate, or a \$40 coupon amount. Let's say that interest rates rise for comparable bonds in the next month to 6 percent, so these bonds now offer a coupon amount of \$60. As such, the bond that pays the coupon of \$40 will need to fall in price so that its coupon and eventual face value paid at maturity (\$1,000) will be equivalent to the new 6 percent yield. So, the bond's price would fall to \$966. When a bond is sold for less than its face value, it is termed a

"discount bond." Conversely, if interest rates fall and become lower than the bond's coupon rate, the bond will be sold at a "premium" (or above par).

What Makes a Discount Bond Attractive?

Bonds generally mature at par, which is \$1,000

in the example above. With the discounted bond, the return achieved from the discounted price paid, or \$966, and its original par value, or \$1,000, would be treated as a capital gain for tax purposes. The coupon amount would still be taxed as interest income. However, since a portion of the total return generated by the discounted bond is taxed at a lower capital gains tax rate, this makes the discounted bond more tax-efficient than a comparable GIC with returns fully taxable as interest income. The chart (above, illustrative) shows this scenario and the difference in after-tax returns.

In some cases, even if the GIC has a higher pre-tax expected return than the discounted bond, the after-tax returns of the discounted bond may be notably higher. In addition to the tax advantage, many quality bonds are more liquid than GICs. As well, in a situation where future interest rates decline, there may be an opportunity to realize gains before the bond reaches maturity. Since many quality bonds currently trade at a discount, investors may be able to find appropriate portfolio additions that meet their risk tolerance, while offering higher after-tax returns than GICs. To learn more, please call the office.

The Impact of Taxes: Discount Bond vs. GIC

	Bond	GIC
Term (Years)	2	2
Yield-to-Maturity	6%	6%
Principal Invested	\$966	\$1,000
Coupon Rate	4%	6%
Sale Price at Maturity	\$1,000	\$1,000
Coupon Payment	\$40	\$60
Price/Roll Yield	\$20	—
Annual Before-Tax Yield	6%	6%
Tax* on Income (50.25%)	\$20.10	\$30.15
Tax* on Capital Gains (25.13%)	\$5.03	—
Total Tax Paid	\$25.13	\$30.15
Annual Net Income After Tax	\$34.87	\$29.85
Annual After-Tax Returns	3.487%	2.985%

*Tax rates are based on the average 2023 combined federal, provincial and territorial marginal tax rates for \$250,000 of ordinary income and will vary by individual income level and province of residence.




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