TD Wealth

# Wealth Insights

## TD Wealth Private Investment Advice

Winter 2021



# From the Desk of Kevin and Gerson

If we were to summarize the feelings that most clients expressed to us last year it would be that we're all looking forward to the future. It doesn't seem likely that we'll look back fondly on the year that was 2020, or at least at first glance it won't be one that most people will want to go through again.

In planning for the turn of the year, we spent some time going over what the last 12 months were filled with: the unique reality of dealing with a pandemic, a massive shift to staying/working/learning at home, major market declines, a quick shift to technology to deal with our new circumstances, and an election that might have been the most anticipated event in history.

In addition to these common experiences, our team also saw a huge increase in referrals for estate planning services, more discussions about insurance than we've ever had, and a market rally that rewarded those who were willing to embrace change. All of this while balancing families, homes, and kids returning to school (and one leaving for university!). In short, it was possibly the most draining year and the most rewarding year we've been through.

As we enter a new phase of the recovery, we're taking the long view and allocating our portfolio accordingly. We're focusing our investments on technology, healthcare, and financials that are expected to carry our portfolios through the implementation of vaccines across the world, and our particular focus on tax-efficient investing has been more important than ever. Tax-loss selling in the spring and during the year, rather than at the end of year as we traditionally do – would have a meaningful impact to lessen the taxes on gains. It's unusual, but we simply needed to react to what the market was giving us throughout the year.

For 2021, we encourage you to take us up on the offer to review your wealth plan, re-visit your will, powers of attorney, and secondary wills (for corporations), and to review your insurance coverage. As we all evolve to manage our way through the pandemic, being well planned is the most important way we can help our clients to achieve their individual goals.

We look forward to working with you on them!

**The Daley Group Wealth Management**
TD Wealth Private Investment Advice
Gerson D'Souza, Kevin Daley

**To Our Clients:**

*While we face continued challenges this winter with the resurging virus, we can take comfort in the news of promising vaccines to bring optimism for 2021. Continue looking forward and positioning your wealth for better times to come; we're here to provide this support.*

*This is likely a different holiday season for many of us. We hope that you and your loved ones stay safe and healthy, and we wish you every happiness for the holidays and the year ahead.*

**— The Daley Group Wealth Management**

## In This Issue



The Daley Group
Wealth Management

■ Retirement Planning

# Don't Need Excess Funds? RIF Minimum Withdrawal Planning

As you think about retirement, maximizing your retirement income is an important part of this exciting transition. Ultimately, it's your after-tax income that counts: paying the least amount of tax on your income can help you keep more of your hard-earned dollars.

Carefully consider and plan for all sources of income, including pension income, non-registered assets, and Tax-Free Savings Accounts (TFSA). If you have sufficient funds through pension income and non-registered assets to meet your retirement expenses, it may make sense to only withdraw the mandatory minimum amount from your registered Retirement Income Fund (RIF) or locked-in plans such as Locked-in Fund (LIF), Locked-in Retirement Income Fund (LRIF) or Prescribed Retirement Income Fund (PRIF) each year. This allows for continued tax-deferred growth within the plan. Here are some additional strategies to help keep funds invested for longer:

**Basing the withdrawal rate on a younger spouse's age** — If you have a younger spouse, consider basing your withdrawal rate on their age in order to lower the amount of the required annual withdrawal, thereby helping to keep more assets to potentially grow within the plan on a tax-deferred basis.[1]

**Making your first withdrawal at the end of the year in which you turn 72** — You are required to convert your registered Retirement Savings Plan (RSP) or Locked-in Retirement Account (LIRA) into a RIF/LIF/LRIF/PRIF by the end of the year in which you turn age 71, but don't need to make the first withdrawal until the end of the year in which you turn age 72.

**Timing annual withdrawals at the end of each year** — The timing of withdrawals can make a difference over time. If you take your withdrawal at the end of each year, instead of the beginning, you allow for greater time and potential compounding of funds within the plan.

For example, consider a 71-year-old with a marginal tax bracket of 40 percent and an RIF worth $500,000 that has an annual rate of return of five percent. If this individual withdraws the minimum from the RIF at the end of the year in which they turn 72, the after-tax income from age 72 to age 90 will be higher than if payments were made at the start of the year. As well, by the age of 90, $315,970 would be remaining in the RIF, as opposed to $293,177, if payments were made at the start of every year.[2]

**Plan Ahead**

While these strategies involve minimum withdrawals from your RIF, consider that, in some cases, withdrawing more than the minimum amount can improve an overall lifetime tax bill. Every situation is different. As such, please get in touch if you require support as you think ahead.

1. Provincial locked-in plan legislation for LIF/LRIF/PRIF allows for the use of a younger spouse's age, with the exception of New Brunswick; 2. Based on current prescribed RIF withdrawal factors.

**RSP Season Reminder**

*Deadline for 2020 RSP contributions:* **March 1, 2021**.

*RSP contribution limit: 18 percent of the previous year's earned income, to a maximum of $27,230 (for 2020).*

■ Income-Splitting Strategies

# Investment Loans to Spouses Can Make Sense

Consider income-splitting opportunities for the year ahead. With the prescribed rate at its lowest level possible, one strategy may involve splitting income with a spouse by use of a loan.

Making a bona-fide loan to a spouse for investment purposes is one way to put family investments in the hands of a lower-income spouse.

**Why is a spousal loan required for this strategy?** Generally, you achieve no tax advantage if you were to simply give funds to a lower-income spouse to invest. This is because the Canada Revenue Agency (CRA) attributes any investment income earned on these funds back to the higher-income spouse, as if earned by that spouse, and it is taxable at the spouse's higher marginal tax rate. This is known as the "attribution rules."

A spousal loan must be documented and interest must be paid by the borrowing spouse at the CRA prescribed rate. Any interest for the year must be paid no later than January 30 after the year-end. Failure to do so means the attribution rules will apply, and any returns on the investment will be taxable in the hands of the higher-income spouse. Interest paid will be taxable income to the spouse loaning the money and may be deductible from the investment income earned by the lower-income spouse.

The lower the prescribed rate relative to the return on investments, the greater the opportunity to benefit from such a strategy. The current prescribed interest rate is one percent, the lowest possible rate (see CRA website[1]).

**Muddy Waters: The TFSA**

An exception to the attribution rules applies to the Tax-Free Savings Account (TFSA). While the Income Tax Act prohibits anyone other than the TFSA holder from making contributions, it does not prevent an individual from gifting assets to a lower-income spouse who then contributes that gift to his/her own TFSA.

However, the attribution rules may apply when money gifted and then contributed to a TFSA is subsequently withdrawn within a short period of time. The CRA has stated that where a higher-income spouse gifts funds to a lower-income spouse to contribute to a TFSA, and these funds are immediately withdrawn from the TFSA and reinvested, future income or capital gains earned would be taxable to the original high-income spouse.[2]

Please seek the advice of a tax specialist for your particular situation.

1. https://canada.ca/en/revenue-agency/services/tax/prescribed-interest-rates.html; 2. See CRA technical interpretation #2010-0354491E5.

■ Investing Resolutions

# Looking Forward: Lessons from the Pandemic

Amidst the many hardships created by the pandemic, there may be prudent lessons that can assist us in finding greater future financial success. As we look to better times to come, here are some reminders:

### Don't Overlook the Merits of an Emergency Fund

The pandemic has been a stark reminder that unexpected events can affect everyone, regardless of income level. Economic shutdowns have affected the income streams of many, highlighting the benefits of having an emergency fund in place. For some high-net-worth individuals, a common notion has been that having enough assets negates the need to have funds set aside for an emergency. But one of the strongest arguments for having an emergency fund is to avoid the need to liquidate investments on short notice, especially since larger daily expenses may need to be covered. For retirees, while emergency savings may not be needed to replace a missed paycheque, they may help support other unanticipated costs, such as health care.

### Avoid Emotionally-Driven Investment Decisions

The equity market sell-off in March 2020 and the ensuing rebound reminds us that markets can quickly reverse their course, even during the most challenging times. This illustrates the difficulty in attempting to time the market — a testament to the importance of staying the course with your investments. Not everyone is able to keep calm during a crisis, which is understandable. However, this is where our role as advisors comes into play — to help provide objectivity and perspective and offer counsel. While it may be difficult to abandon the worry that comes with fluctuating portfolio values, it is important not to let these worries derail you as you work towards achieving your ultimate goals.

### Reassess Your Current Budget

This is not to admonish anyone about their spending habits, however taking time to sit down and map out the family income and expenses each month can be revealing. More notably, the current pandemic has altered many household spending habits, due to working remotely or lifestyle changes — perhaps you have saved more by not going to the office or gym or traveling for vacation. Reevaluating spending on a periodic basis may uncover opportunities to put more towards retirement savings, which has the potential to pay significant benefits down the road.

### Don't Make Unnecessary Withdrawals

Making early withdrawals from retirement accounts can result in unintended consequences. While the pandemic may have made this temporarily necessary, it is important to have a thoughtful plan for prioritizing sources of potential income during difficult times. Why? Liquidating investments to generate cash flow could potentially result in unanticipated taxes or, in the case of retirees, the loss of income-tested benefits such as OAS (Old Age Security). Equally important, careful thought should be given to how to make up for the potential loss of retirement income down the road.

■ Market Perspectives

# Equity Market Volatility: The Norm

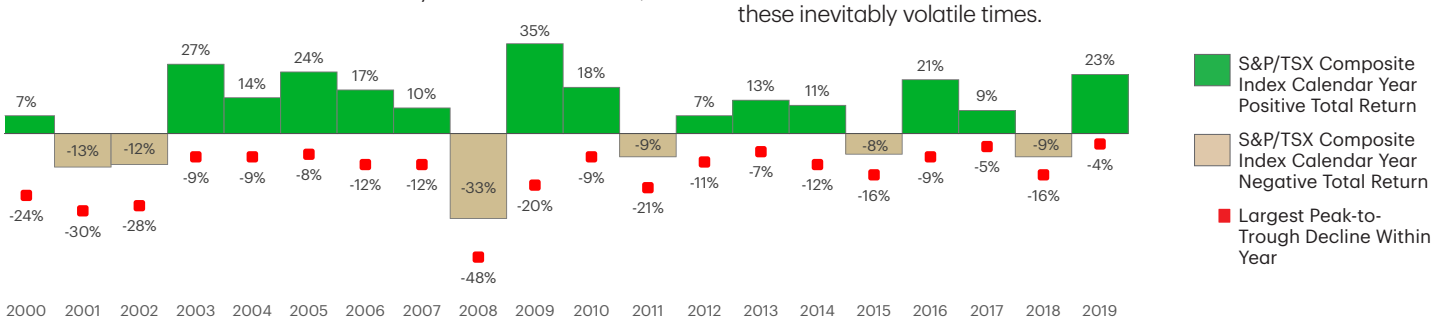
Was 2020 a more volatile year in the equity markets? With heightened noise, it may have felt as though the markets were particularly unsettled.

Yet, a look back over the last 20 years shows that volatility has always been a common feature of the equity markets. The chart below shows the biggest peak-to-trough drawdowns during the year for the S&P/TSX Composite Total Return Index and the resulting annual returns. In 12 of the last 20 years, there has been a double-digit, intra-year correction. Significant volatility is no stranger to the markets.

Today, many factors have helped to drive volatility. Interest rates continue to be at historical lows and many traditional lower-risk, fixed income investments no longer provide meaningful returns, which has pushed many investors into equity markets in search of higher returns. There was no shortage of negative news in 2020, which may also have helped to support volatility. As well, there continues to be significant money sitting on the sidelines, which has driven volatility as investors enter and exit the markets.

However, keep in mind that short-term volatility often has little bearing on what happens over the longer term. In fact, in half of the years where the market experienced a double-digit, intra-year correction, the market ended up finishing in positive territory. Extending the time horizon out across many years may further reduce the effects of volatility.

These perspectives may be good food for thought as we weather these inevitably volatile times.




Source: S&P/TSX Total Return Index, Jan. 1, 2000 to Dec. 31, 2019.

■ Remember Your Investing Time Horizon

# Investing Perspectives: Keep Time on Your Side

If your sense of time has felt warped recently, you're not alone. Some feel as though time is flying; many others say that it has slowed to a crawl. The pandemic has caused stress, trauma, confinement, boredom, and uncertainty for many — *how long will this last?* — conditions which neuroscientists have shown can distort our temporal perception.[1]

These are challenging days, and it may be easy to lose sight of the importance of time in investing. The reasons are many: heightened volatility in the markets, our need for immediacy and the influence of media in the digital age.

However, the merits of maintaining a longer time horizon to take advantage of the impact of compounding over time should not be overlooked. This often involves the difficult task of having to endure inevitable short-term events, such as volatility (a permanent market fixture!), and the even more unpleasant occurrences of a recession or an unexpected pandemic.

**Markets are Cyclical: Nothing Lasts Forever**

In doing so, it may be worthwhile to remember that equity and financial markets are cyclical by nature. History has shown that markets spend more time in positive territory than negative. Consider that since 1956, there have been 13 bull markets and 13 bear markets. The average bull market has lasted 54 months, with an average gain of 131 percent, whereas the average bear market has lasted only 9 months with an average loss of -27 percent.[2] We see similar cyclicality in the economic cycle: the typical business cycle lasts around seven years. Over the same period, the Canadian economy experienced seven recessions, with the average recession lasting 11 months.[3]

The cycle is alive and well today. As advisors, we recognize that cycles go up and down, and we seek to build this into our wealth plans. Periods of uncertainty are not the time to run and hide, waiting for the dust to clear.

**Your Time Horizon May Be Longer Than You Think**

While the pandemic has put pressure on many incomes, which may require some individuals to reexamine retirement options or timing, don't overlook the opportunity to make up for lost time. Just as increasing longevity requires planning, it may also allow greater time for recovery. Consider that an investment with a five percent compounded annual return can double in approximately 14 years. This means that a 70-year-old may still have the potential to see their investments double within their lifetime,[4] and possibly even twice if they become a centenarian.

**Keep Focus**

During these challenging times, we may forget that building wealth takes time. The irony is that young people often think they have so much time, but never enough money. But those who are entering their later years often remark that they now have money, but no longer enough time.

Stay focused on your own investing time horizon. Don't lose sight of the importance of time in supporting you towards achieving your own investment goals and remember to keep time on your side.

1. https://discovermagazine.com/mind/how-the-coronavirus-pandemic-is-warping-our-sense-of-time; 2. S&P/TSX Composite Index, 1/1/56 to 9/30/20; 3. https://thecanadianencyclopedia.ca/en/article/recession; 4. Assuming avg. life expectancy of 83 yrs. old.

## Chart: The Impact of Time in Investing

Time can be one of the investor's greatest allies. The chart below (an example only) shows the potential impact of compounding over time in generating retirement savings. With a longer time horizon, an investor may require a significantly lower monthly investment to yield $1,000,000.

**Monthly Investment Needed to Yield $1,000,000***
*Based on Different Time Horizons and Rates of Return*

| | At Average Annual Rate of Return of... | | |
|---|---|---|---|
| **Years** | **4%** | **5%** | **6%** |
| 20 | $2,726 | $2,433 | $2,164 |
| 30 | $1,441 | $1,202 | $996 |
| 40 | $846 | $655 | $502 |

*Compounded monthly at annual return rates shown. Effect of taxes, fees and inflation ignored.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