BAKER & EDWARDS FINANCIAL

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NEWSLETTER – JULY 2015

MARKETS

The year is half over, but investment performance is yet to begin. The Canadian market shows zero percent gain in the first 6 months, the S & P 500 has gained less than one percent in US dollars, but almost 9% when converted to Canadian dollars. Globally, Germany and Japan have been strong but the overall world index has only gained 2% in local currencies, but 10% when converted into Canadian dollars.

We have often reminded you that we do not invest in the indices, but rather in funds that pick a few carefully selected businesses in which to invest. This is one of the times when fund performance can differ significantly from market performance. Generally speaking, Canadian balanced funds have negative to slightly positive returns, Canadian equity funds show a wider range, depending on how many energy related businesses are in the portfolio. US and global funds show strong returns, but a good part of this gain has come from the falling Canadian currency.

Recent news headlines have focused on Greece but the real investment story is China. Stock indexes doubled in the first five months of this year, but have fallen by over 30% in the past few weeks and seem to be continuing their plunge. Part of this is due to government interference and part of it is due to excessive borrowing – but a large part appears to be due to a much greater slowing of the Chinese economy than their government wants us to know about. Such a slowdown will have a great impact on the demand for, and the prices paid for commodities such as copper and oil.

These commodities are a significant part of the Canadian economy and are part of the reason that the Canadian economy has been in a technical recession for the past 6 months. Our situation is made worse by the fact that the Bank of Canada is trying to stimulate the economy by cutting interest rates, while the government is cutting spending to balance the budget to meet a political promise – these two bodies are supposed to work together!

PLANNING TIPS

In this section we would like to highlight some of the interesting questions we have encountered recently. Feel free to discuss any of them with us.

1. **Beneficiaries** – should I name a beneficiary on my RRSP/RRIF or should it be my Estate? If you have a spouse, it is usually advantageous to name that person as the beneficiary on the RRSP/RRIF because the money will be transferred without immediate tax. If you are a widow or otherwise single person, naming a beneficiary other than your Estate can cause problems for your Executor. This is because CRA deems that you cashed all your RRSP/RRIFs on the day you died. All of that income on the Final tax return is likely to create a large tax bill – but all the money went to the beneficiary outside of the Estate. When CRA finds that they cannot get paid by the Estate they go after the beneficiary – not a pleasant outcome for anyone.

2. **Common law relationships** – what rights does a common law spouse have on a death or a breakup? Surprisingly, in Ontario, a common law spouse has no automatic inheritance rights. Unless you are specifically named in the Will as a beneficiary (or on a pension, RRSP or RRIF), all of the deceased persons assets go to his blood relatives. There are four sets of laws that affect these relationships so do not rely on CRA's definitions as the complete solution.

3. **Intestacy** – this means dying without a will. It also means leaving all kinds of costly legal headaches and delays for your family. Without a Will no one has the legal authority to deal with your assets and debts, or to provide an immediate income for your family. The provincial guardian will control the estate until someone is able to apply to the courts to be appointed "Estate Trustee without a Will". Your assets can no longer be distributed as you might have wished but will be governed by the Succession Act of your province. **Please** ensure that you have prepared a Will and review it at least every 5 years. Lawyers estimate that at least 95% of do-it-yourself wills contain serious errors that either prevent or impede your wishes – please have your Will prepared by a lawyer.

4. **Executor** – this is the person appointed by your Will to administer your Estate. This used to be considered the honour and duty of a close friend but the complexity and overlapping elements of the laws, especially the 2015 changes to the Ontario Probate Act, make it an onerous chore for anyone who doesn't have the background and experience. **Please** discuss your will with the executor, and with your family to ensure everyone is aware of your wishes and the reasons for them. Also ensure that your Executor knows that they are empowered to call upon your advisors for help, and that the Estate will pay for Executor insurance – a relatively new product that protects the Executor from the many instances of liability that they will encounter. Remember that executors will perform the duties only once or twice in their lifetimes – advisors such as Cory and myself unfortunately encounter it several times every year.

5. **<u>Joint accounts</u>** – many people register accounts jointly with a child in order to avoid Probate fees. Unfortunately they often do not think of the other implications of doing so, especially if there is more than one child – is the intent that the named child gets the entire account, or is it to be treated as part of the Estate and all children are intended to share it? This could easily be resolved by attaching a letter to the Will that clearly states your intentions. Many people also do not understand that adding a child to the account means that it becomes part of the child's assets in the event of a marital dispute. Adding a child's name to your house ownership can be a very costly event. A house sale is normally tax-free because of CRA's Principal Residence Election (PRE). If a child already owns another home she is only entitled to the PRE on one of them so, in effect, half the value of your home is now taxable.

RISK MANAGEMENT

There is one phone call that I am really glad not to have experienced in my almost 30 years in the financial services field. It goes something like this: "Hi Bob, I know we have done well with our retirement planning and investments, but what have we put in place to provide for us now that I have a heart condition (or stroke, or cancer) and need a very expensive treatment in the US?"

The condition of course is defined as a critical illness. In our youth many such illnesses would have been fatal, so life insurance was the priority. Now medical science has advanced to the degree that many people can survive the event or the illness – but such progress comes at a cost, in terms of drugs, continuing care, or an inability to work. Critical illness insurance provides the money to provide for a worry-free recovery period.

We have discussed this need in several previous newsletters but frankly, the lack of questions suggests we have not really connected with you on this topic – so we will keep trying. The odds are not really in your favour in that you are 4 times more likely to have a critical illness before age 65 than you are to die. If you are willing to accept the risk, **please** only do so after a conscious effort to plan how you would be able to live in such a situation.

PS: Cory and I would like to formally welcome Tammy Miller to our team. Tammy has many years of valuable experience in both mutual funds and insurance administration. (Elizabeth retired at the end of January.)

PPS: The enclosed booklet from Invesco will give you very useful information for your estate planning. Call us if you wish to discuss it.