

# Well-Advised

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If you "parked" your contributions this RRSP season, remember that the sooner your savings are allocated to investments best suited to your financial goals, the sooner they'll begin to help you reach those goals. We're here to help you find the options that are most appropriate for your situation.

## Is your portfolio keeping up?

*Your financial health depends on staying current*



**A** sound asset mix strategy and a regular investment plan will provide you with long-term rewards. There's only one problem — life doesn't stand still.

Your goals, financial situation and personal circumstances, as well as market performance, will inevitably change, and your strategy needs to keep pace.

### Major life events

For example, suppose you experience a major life change, such as the birth or adoption of a child, a change in marital status, a change in employment or income, or even a change in health. Any one of these events could affect your financial situation, your needs for the future or your risk tolerance.

As a result, you may need to adjust your level of savings, allocate money toward different goals or seek higher growth from your investments. And your asset mix may need to shift to reflect your change in goals.

### External events

Even if you haven't experienced any major personal changes, it's still important to regularly review your portfolio and make sure your asset allocation is appropriate. Why? Because as different asset classes earn different rates of return, your asset mix could stray from your target allocation.

For example, if your equity investments increase by 10% one year and your fixed-income investments increase by 5%, your portfolio may have more exposure to equities than you are comfortable with. You may need to reallocate or direct ongoing contributions to the underweight areas in order to maintain your target asset mix.

### Regular review

We're here to help with your portfolio review and adjustment process. Meet with us regularly and keep us informed of any key life changes, so we can ensure that your financial plan stays on track. ■

## Make sure you're investing the tax-efficient way

**N**ot all investment income is treated equally from a tax perspective. And one of the best ways to improve investment returns is to earn money in a more tax-efficient manner.

### Different types of income

It helps to understand how different types of income are taxed outside of registered plans. Here's an overview:

**Interest payments.** These are taxed like ordinary employment income. You'll pay tax at your marginal rate in the year you report the income.

Sometimes, you may have to report interest you haven't even received. This is the case, for example, with investments like strip bonds that pay out all the accumulated interest at maturity. The interest that accrues every year is taxable, even though you haven't yet received it.

**Dividend payments.** Those from Canadian corporations are also taxable in the year of receipt, but at a lower rate due to federal and provincial dividend tax credits that you claim when filing your tax return. Recent government proposals would

tax eligible dividend income received after 2005 even more favourably.

**Capital gains.** These arise when you sell or transfer capital assets for more than you paid for them. Only 50% of any capital gain is taxable.

In addition, you aren't taxed on capital gains until you actually sell or transfer the investment. You can defer your gain by continuing to hold the investment and control when any gain is ultimately taxed.

Corporate class mutual funds are another possibility. These fund families are set up as a single corporation rather than a series of mutual fund trusts. Switching from one fund in the corporate family to another in the same family isn't considered a sale and therefore won't trigger a taxable capital gain.

If you own mutual funds that distribute capital gains, however, these will be taxable in the year you receive the distributions.

**Return of capital.** Some capital investments, such as income trusts and high-income investment funds,



also distribute "return of capital."

These payments are received tax-free, but the base cost of your investment for tax purposes will be reduced by the amount of the payment. This increases the capital gain (or reduces the capital loss) generated when you eventually sell or transfer the investment. So while return of capital payments can appear to be tax-free, they are really a form of tax deferral.

## Top tax tips for this year...or anytime

Whether you're looking to squeeze in some extra tax savings when you file your 2005 return or are planning ahead for next year, here are five helpful tips:

**1 Pool medical expenses.** Medical expenses qualify for a tax credit only if they exceed \$1,844 or 3% of net income — whichever is less. Pooling your family's expenses and reporting them on the tax return of the lower-income spouse helps maximize the credit. Also, you can claim expenses for any 12-month period ending in 2005.

**2 Pool charitable contributions.** Donations over \$200 get a higher tax credit. Pooling your contributions with your spouse may maximize the qualifying amount.

**3 Don't pool political contributions.** Tax credits are higher at lower contribution levels: 75% for the first \$400 donated,

50% for donations between \$400 and \$750, and 33.33% for donations between \$750 and \$1,275, to a maximum credit of \$650.

**4 Deduct eligible moving expenses.** If you have moved more than 40 kilometres to be closer to a new place of work, you can deduct eligible moving expenses, including meals, moving costs, legal fees and the cost of selling your old home.

**5 Transfer tax credits.** Unused portions of both the age 65 tax credit and the disability tax credit are transferable to a supporting spouse; the disability tax credit can also be transferred to another supporting relative. ■

### Act strategically

Where you invest both inside and outside your RRSP, you have an opportunity to structure your portfolio to reduce your taxes. Investments that are taxed at a higher rate, such as GICs and bonds, can be held inside your RRSP, where they will be tax-sheltered as long as they stay in the plan. Investments that generate dividends and capital gains can be held in your non-registered portfolio, to take full advantage of the tax benefits.

Also, you'll want to pay investment counsel fees for both your registered and non-registered holdings from your non-registered account. This means that 100% of your RRSP can keep growing tax-deferred.

These are just a few examples of how strategic allocation of your investments can help minimize the taxes you pay. We can work with you to implement these and other strategies that could make your portfolio more tax-efficient. ■

## Getting the most from your family business

**M**any entrepreneurs are so busy building their businesses that they overlook the issue of succession planning. But the potential complexities mean that business owners should take steps well in advance of their retirement to set the stage for a successful business transfer.

Succession planning allows you to determine how you want to transfer the ownership of your business, so you can both maximize your personal financial security and ensure the long-term success of the business. It also allows you to decide who, if anyone, you want to appoint as your successor and determine how you want to make the transition out of actively managing the business.

### Allow time to plan

Developing a good succession plan takes time, particularly if it involves training a successor. You need to plan your exit strategy long before you intend to leave. The amount of time will depend on the nature of the business and who the successor is.

Whether you expect to appoint a successor or sell to a third party, your first step should be valuing the business. You need to determine, objectively, how much it's worth and take any steps you can to maximize its sale price.

You'll also need time and professional help to structure the sale. You'll want to



receive the proceeds of the sale over a time frame that's suitable to you, while ensuring that your successor has the means to finance the purchase.

### Appointing a successor

If you're considering appointing an employee or family member to succeed you, it's important to objectively consider whether your intended successor has both the ability and the desire to run the business.

If you want to keep the business in the family, consider consulting your professional advisors to ensure there's a family member suited to succeed you. You may find that choosing a non-family member who is already involved in managing the business is a better choice to succeed you.

In either case, you will need to ensure

that your succession plan builds in time to groom your successor to take over your role, and allows you to gradually distance yourself from the day-to-day business operations before actually transferring ownership.

### Third-party sale

If you decide to sell the business to a third party, a succession plan allows you to structure the sale in a tax-effective manner. (Keep in mind that the terms of your shareholders' agreement may require you to sell your interest to any co-owners.)

For example, you may be able to divide the ownership of the shares among adult family members in advance of the sale, so that each family member can take advantage of the special \$500,000 capital gains exemption that's available on qualifying small-business shares.

You'll need to decide how best to structure the sale to meet your financial needs. You may decide to sell only a portion of the business, or to receive the purchase price over a period of time, rather than all at once.

If you're involved in a family business, be sure to keep us apprised of its progress and your plans regarding its future. Keep in mind that your business and career plans can have a significant impact on other areas of your overall financial plan as well. ■

## Good reasons to insure good employees

Business owners are well aware of the importance of good staff. Employees who are product experts, who bring in large amounts of new business or who are essential client contacts are among a business's most valuable assets. If a key employee were unable to work for a long period of time, the business could suffer.

To protect your business, you may want to purchase life, disability and critical illness insurance on each of your key employees. Should a key employee become ill, or pass

away, the insurance proceeds could be used to replace lost business income, hire a replacement, pay off company debts or provide additional working capital. The benefits might also be used to provide financial assistance to the key person or his or her family.

Depending on your needs and those of your business, there are a number of ways to structure key person insurance. We can help you explore the best solutions for your particular situation. ■



# Consider these points to solve the downsizing dilemma

If you've been a homeowner for a number of years, you've probably built up substantial equity in your home. You've also probably built up personal equity — a strong emotional connection to your home, neighbourhood and network of friends.

Here's the dilemma. If you don't need the space you once did, or your reason for buying your home (such as its proximity to schools, parks and entertainment) is less of a factor in your life, should you unlock some of your home's value by downsizing?

For most people, it's not an easy decision. Moving to a new location may give you greater financial freedom to pursue a number of goals, from taking early retirement to enjoying extended vacations. But leaving your home of many years may dissolve important social, community and support structures that greatly contribute to your quality of life.

Before you make any decisions, identify all the pros and cons — social, physical and psychological, as well as financial.

**Financial considerations.** Depending on your home's current value and whether you are mortgage-free, selling may generate a sizeable pool of capital that you can invest and draw on throughout retirement. Assuming the home is your principal residence, any capital gain is tax-free, under the principal residence exemption.

If you move to a smaller home, you may also see your monthly expenditures for maintenance, insurance and property taxes go down. Don't assume that this will be the case, however. If you move to a condominium, for example, you'll be required to pay monthly fees to the

property management for the upkeep and maintenance of the common areas.

**Lifestyle.** The effects on your lifestyle will depend largely on where you are moving from and where you're moving to. For example, moving into a condominium, where you don't have to worry about keeping up the yard and building, can give you the freedom to travel or even spend the winter months down south. On the other hand, you'll no longer have as much space for family reunions or visitors.

**Health issues.** Your decision to downsize might be based partly on health concerns. For example, you might need a home with fewer stairs or want to be situated closer to medical facilities in case of emergency. Some new developments even include on-site medical services.

**Psychological effects.** Recognize that there will most likely be an emotional transition along with your physical relocation. Moving of any kind is stressful, but leaving a home you've lived in for many years brings additional complications, including moving away from familiarity, friends and memories.

If this is a concern, you might consider moving to smaller premises in the same neighbourhood so that you can maintain existing friendships and stay in familiar surroundings. Or consider moving to a new location that's close to other family or friends, so that you'll already have the beginnings of a new social circle.

If you are thinking of downsizing, be sure to speak with us. Getting expert advice about the financial implications of your decision may alleviate some of the emotional stress and help you make the decision that's best for you. ■

## How rising rates could affect your mortgage choice

You may be nervous about the prospect of higher rates if you negotiated a variable-rate mortgage when rates were rock bottom. While many variable-rate mortgages allow you to lock in to a fixed term at any time, you should weigh the costs carefully before committing.

### Different interest rates

Variable rates can still be a good choice when interest rates are rising. The choice depends on the difference between variable- and fixed-rate interest charges.

For example, suppose the current interest rate for a five-year fixed-rate mortgage is 6.15%, while the interest rate for a five-year variable-rate mortgage is 4.75% — the difference is 1.4. Unless the prime interest rate increases by more than 1.4 percentage points, you will still come out ahead by choosing the variable-rate mortgage.

### Interest versus principal

Remember, too, that with a variable-rate mortgage, the amount of your monthly payment doesn't change when rates go up. What changes is how each payment is allocated between the interest and the principal. With a higher rate, less of each payment goes toward paying down your principal. However, if rising rates are often on your mind, you might be more comfortable with the security of a fixed-term mortgage.

### Advice is key

It's wise to seek professional advice when making mortgage decisions. And it's important to let us know what those decisions are — we can help you understand how they might, in turn, affect your overall financial plan. ■

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