# WELL-ADVISED

SUMMER 2024

## CONSIDER THE TIMING OF LEAVING AN INHERITANCE

Naming a beneficiary in a will may be seen as the most common way to leave an inheritance to a loved one.

However, in certain situations, many people choose to give an advance on an inheritance during their lifetime or have the funds distributed in the years following their passing.

### GIVING WHILE LIVING

Our increasing longevity can have a significant effect on the decision to leave an inheritance through a will. When the beneficiary is a child, they may already be well established and financially secure—even retired—when they receive the funds. Giving an earlier inheritance during your lifetime could make a greater difference to a loved one's quality of life. Just one example is gifting the funds for a child or grandchild to make the down payment on a home.

### DELAYING AN INHERITANCE

Some individuals want to control how an inheritance is received, typically by establishing a trust. One person might choose a future year for the inheritance to be received if they're concerned that a large inheritance going to a young beneficiary will weaken their child's work ethic. Another individual may arrange for the inheritance to be paid out in instalments over a specified period if they're concerned about the beneficiary's ability to manage a large sum.

### MAKING YOUR DECISION

Although the reasons to give an inheritance earlier or later may be valid, it's still a decision that should be weighed carefully. If you plan to delay an inheritance, think about the consequences. For example, consider whether a child who receives their inheritance in instalments will feel resentful, especially if their sibling receives their total inheritance upon your passing. If you're thinking about giving an early inheritance, talk to us. We can determine whether it will or will not jeopardize the funding of your retirement, including any unexpected costs. ■

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Many investors wonder about changing the way they invest when markets are on a considerable upswing, and stock markets in Canada and the U.S. reached record highs in the past couple of months. Some investors witness others investing even more in equities and want to jump on the bandwagon. Others fear an eventual collapse and think about selling while prices are high. These reactions are called herd behaviour and loss aversion, and we cover investment biases like these on Page 3 of this issue. If market conditions ever tempt you to change your regular investing habits, contact us and we'll talk it over.

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# DETERMINING WHICH DONATION METHOD SUITS YOU BEST

When choosing how to make a large charitable gift, the number of available options can seem overwhelming—especially when each brings its own financial benefits.

To simplify matters, here are personal situations you may relate to, along with donation methods for each.

**You want to experience the reward of giving now.** You may want the satisfaction of helping out during your lifetime and staying informed of the charity's work. Methods of giving while living include donations made in cash, in investments or through donor-advised funds.

**You aim to maximize your donation's value.** You may be ready to make a large donation, but want a way to make your charitable dollars go further. One method is to donate securities, including stocks, bonds and mutual funds, that have appreciated in value, as the tax normally paid on capital gains will not be payable. Another way is to donate a life insurance policy, since the insurance amount the charity receives may be greater than the amount you spent on premiums.

**You aim to safeguard your standard of living.** You may worry about giving a large gift during your lifetime only to face unexpected situations that make you wish you could have those donated funds back. If you want to give a significant gift without jeopardizing your standard of living, you can leave a bequest upon your passing. Suitable methods include donating through a will, donating life insurance or donating assets in registered plans.

**You're retired and want additional tax-advantaged income.** With a charitable gift annuity, retirees give funds that are split into two portions. The charity provides a donation tax receipt for the gift portion and purchases an annuity for the donor. This annuity gives the donor a guaranteed stream of tax-advantaged income for life.

**You want to make the most of the tax break.** Situations may arise when a donation tax credit helps the most during your lifetime. For example, an individual may sell a vacation property and incur a large capital gain with a burdensome tax liability. By making a charitable donation now, they can use the resulting tax receipt to reduce their tax payable on this year's return. For tax relief now, you can use cash donations, investment donations, donor-advised funds, life insurance or a charitable gift annuity.

In many cases, individuals recognize that estate assets will trigger a large tax bill, so they arrange for a donation to be made upon their passing. To benefit your estate, you can use your will, registered plans or life insurance.

Retirees with a significant Registered Retirement Savings Plan (RRSP) or Registered Retirement Income Fund (RRIF) balance have a unique opportunity. These assets are taxed as income and could potentially be the estate's largest tax liability. However, if you name a charity as the beneficiary of the RRSP or RRIF, the donation tax credit received by the estate can offset the tax payable on the plan's assets. In many cases, the tax liability is *completely* offset. ■

## YOUR DONATION OPTIONS

Here are the most common methods to make a substantial charitable gift.

**Cash donations.** Tax receipts for donations that total over $200 provide a combined federal and provincial tax credit of at least 40% of the donation amount (varies by province).

**Investments.** When donating securities, including stocks, bonds and mutual funds, the donor receives a tax receipt for the investment's fair market value. Neither the donor nor the charity pays tax on capital gains.

**Donor-advised funds.** Designed as a long-term program, donations are invested and grow on a tax-deferred basis. The donor periodically gives grants to charities of their choice.

**Bequests in a will.** It's possible to state the donation as a specified amount, a percentage of the estate or the remaining assets after providing for other beneficiaries.

**Registered plans.** When a charity is the beneficiary of an RRSP or RRIF, the donation tax credit can offset the tax payable by the estate on the RRSP's or RRIF's assets. If a charity is named as the beneficiary of a Tax-Free Savings Account (TFSA), the tax credit can help offset taxes payable by the estate.

**Life insurance.** Donating the proceeds of a new or existing life insurance policy can provide tax relief either to the donor during their lifetime or to their estate.

**Charitable gift annuities.** One portion of the donor's amount is a donation for which the donor receives a tax receipt, while another portion provides the donor with a tax-advantaged income stream for life. ■

# PROFIT BY OVERCOMING INVESTMENT BIASES

Financial behaviourists have identified well over 20 investment biases that can tempt or lead individuals to invest in a particular way. Generally speaking, none of the biases is good news for investors.

Fortunately, investors who have an advisor aren't vulnerable to making poor decisions out of fear, hope or any number of irrational reasons. However, understanding investment biases is still valuable. You'll gain insight into portfolio decisions and better appreciate why not all investments hyped as winners are good opportunities. Also, certain biases, such as loss aversion and mental accounting, may affect any individual's decision-making.

Here are several investment biases that a great many investors encounter.

## HERD BEHAVIOUR

Following the crowd may seem especially comforting and reassuring when our money is at stake. The thought is, "If so many people are choosing this investment, it must be a winner." However, the herding instinct can lead to problems in various ways.

Jumping on the bandwagon may mean that you stray from following an investment plan. When you choose an investment on impulse, it may not be aligned with your risk profile, time horizon or financial objectives.

When herding arises out of the fear of missing out, individuals might chase a popular investment that's hot and on an upswing—

whether it's a stock, fund or something new such as cryptocurrency. The trouble is, you're now buying when the investment is more expensive. In addition, there's always the chance that this year's outperformer will be next year's underperformer.

## MENTAL ACCOUNTING

With mental accounting, an individual values money differently depending on its source, and this may lead to unsound investment behaviour and decisions. Say that someone knows they should be paying their credit card debt or building their Tax-Free Savings Account (TFSA), and they receive their tax refund. Ideally, they should view the refund as rightfully earned money they can apply to their debt or TFSA—not as free money to spend on a luxury item.

## HOME COUNTRY BIAS

A person negatively affected by home country bias holds so much of their equity portfolio in domestic companies that they sacrifice the full benefits of diversifying in foreign equities. It's a global phenomenon, and Canada is a prime example of a country where home bias can deprive individuals of investment opportunities. First, Canadian stocks account for only about 3.4% of the global equity market.[1] Second, the domestic market doesn't offer optimal exposure to all sectors. The Canadian equity market is overweight relative to the global market in the energy and financial sectors, but underweight in the healthcare, information technology, consumer staples and consumer discretionary sectors.

## LOSS AVERSION

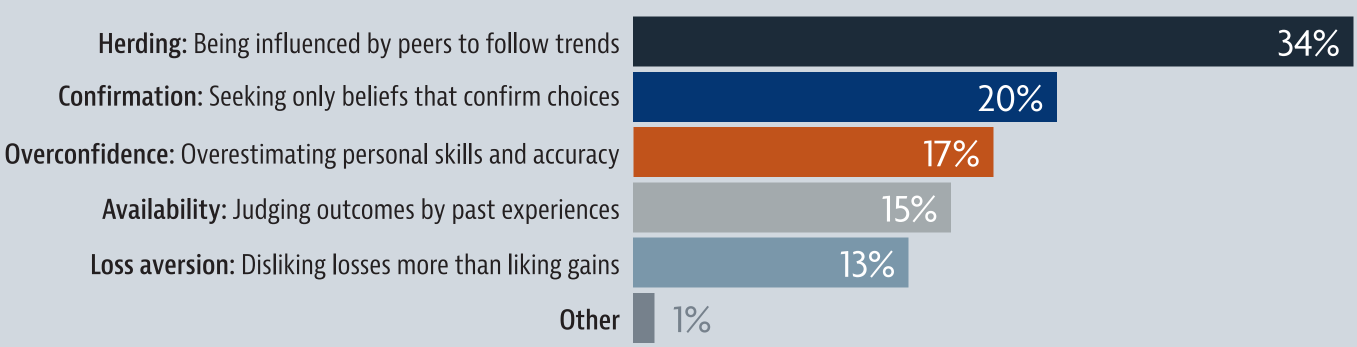
According to financial behaviourists, the degree of pain most people experience from a financial loss is much greater than the degree of joy felt from a financial gain. This aversion to loss can lead some individuals to make questionable investment decisions. For example, think of investors who sold investments or stopped making contributions when COVID-19 first hit and markets plummeted. They would have missed one of the fastest market recoveries in history.

It's only human nature to be affected by investment biases at one time or another. If you ever feel you should react to changing market conditions or new investment opportunities, talk to us and we'll assess the situation together. ■

[1] Vanguard, "A Case for Global Equity Diversification," 2023.

## BIASES MOST AFFECTING INVESTMENT DECISIONS

Poll results of 724 chartered financial analysts from around the world naming the most common bias among investors.




Source: CFA Institute survey, "Which of the following behavioral biases affects investment decision making the most?," 2015.

# HOW TO AVOID OR MINIMIZE THE OAS CLAWBACK

Whether the amount is small or large, whether it applies to a couple of years or many, Canadians don't like their Old Age Security (OAS) pension clawed back.

The clawback is officially known as the OAS pension recovery tax. A taxpayer repays 15% of the amount by which their taxable income exceeds the threshold amount, which is $90,997 for 2024. Here are some common ways to manage the clawback.

**Splitting pension income.** When one spouse has taxable income exceeding the clawback threshold, they may be able to reduce or eliminate the clawback if their spouse has a lower marginal tax rate. Through pension income splitting, they can allocate up to 50% of their eligible pension income to their lower-income spouse. Eligible pension income includes registered pension plan payments and, if you're 65 or over, Registered Retirement Income Fund (RRIF) withdrawals.

**Using a TFSA.** Building a large Tax-Free Savings Account (TFSA) in your income-earning years can be instrumental in helping to prevent an OAS clawback when you're retired. Funds withdrawn from a TFSA are not included as retirement income subject to the clawback.

**Managing your minimum RRIF withdrawal.** The minimum required annual withdrawal from a RRIF can be a key contributor to exceeding the clawback threshold. When possible, you can reduce the annual amount by basing RRIF withdrawals on the younger spouse's age. In addition, if an individual has lower income in the years before turning 65, they may consider withdrawing from a Registered Retirement Savings Plan (RRSP) during this period. Their lower marginal tax rate will make tax on withdrawals less burdensome, and they'll reduce their minimum RRIF withdrawal amount.

**Investing strategically.** In a non-registered account, limiting your taxable income can help reduce or avoid a clawback. Equity investments that generate capital gains are better for this purpose than dividend-paying investments. That's because only 50% of capital gains are included as taxable income, whereas eligible Canadian dividends are grossed up by 38%, so 138% of the actual dividend amount is considered taxable when

determining income for the OAS threshold. Also helpful are mutual funds that provide return of capital distributions, as return of capital is not taxable income. However, note that investments must suit your overall objectives and income strategy, and not be chosen only to avoid an OAS clawback.

Depending on your situation, other strategies may be available, such as making RRSP contributions up to age 71 and selling assets before you start receiving OAS benefits if those assets will trigger large capital gains. Talk to us if there's a possibility your retirement income may exceed the OAS threshold amount, and keep in mind that some strategies may be implemented before you retire. ■

# DO YOU AND YOUR SPOUSE SEE INVESTING THE SAME WAY?

Interestingly, spouses with very different—even opposite—investment personalities may quite easily develop an investment program that's just right for the couple. Yet, in some cases, partners who view investing the same way may need to proceed with caution.

## APPROACHES FOR DIFFERING VIEWS

Take the case of a conservative investor and an aggressive investor who share a non-registered account to save for retirement. With their advisor's guidance, they allocate equities and fixed-income investments to strike a compromise between each spouse's risk tolerance. The conservative investor benefits from potential market opportunities and the more aggressive investor is restrained from placing retirement savings at undue risk.

If one or both spouses aren't comfortable with compromising, it can still work out—simply by investing independently. Say that one spouse invests conservatively in their Registered Retirement Savings Plan (RRSP) and the other focuses on more aggressive RRSP investments. As a couple, their approaches can balance out, combining wealth preservation with long-term growth potential.

## WHEN THE SAME VIEW CALLS FOR CAUTION

An ideal situation is when spouses have a similar investment approach, with risk tolerances that are not extreme. However, if both spouses are highly aggressive investors, they should recognize they may need to temper their approach in light of the couple's investment objectives and time horizon. If both spouses are ultra-conservative investors, the couple must understand they likely have to save and invest more to meet their financial goals.

Talk to us if risk tolerance ever becomes an issue between you and your spouse, and we'll develop a resolution that suits you both. ■