

■ The Personal Financial Advisor

In This Issue

FIND OUT YOUR
CREDIT RATING
..... 1

CRITICAL ILLNESS
INSURANCE
..... 2

MAKE BELIEVE
WEALTH
..... 3

FEAR AND YOUR
INVESTMENTS
..... 4

ESTATE PLANNING
OPPORTUNITIES
WITH ALTER EGO
AND JOINT
PARTNER TRUSTS
..... 6

HISTORICALLY
MARKETS GO UP
MORE THAN THEY
GO DOWN
..... 8

■ CREDIT RATING

Chris Snyder, CFP, RFP

Although we often hear talk about a person's credit rating, most people have no idea what theirs is. But having a good rating is important, especially for big-ticket items such as cars, lines of credit and mortgages. If you don't know yours, we suggest you find out.

Your rating is a function of the assets you have accumulated, the amount of debt you have at any one time and your history of paying it off. If you have paid your debts quickly, it is likely good. If you have been historically delinquent paying off your loans, it is probably bad.

If you want to find out what your credit rating is, and the parameters and explanation for it, you can go to either Equifax Canada (www.equifax.com) or Trans Union Canada (www.transunion.ca). Either should have your credit rating. You can obtain your personal rating instantly, in which case you will need to pay. Otherwise you can get it by mail at no charge.

You may find your credit rating is not accurate. If so, call the company and advise them. Historically, many women have been caught without a credit rating because their partners may have been doing the borrowing and buying. Women should obtain their own credit rating, and the easiest way to do this is by obtaining a credit card or taking out a short-term loan. You may need to secure the card or loan with some savings as security. Use the credit card for a year or two, always paying on time, or use the loan, then apply for your rating after it is paid out. Either course will create your credit rating.

It has recently become the practice for some insurance companies to increase insurance rates for single parents without notice because of a poor credit rating brought on by separation or divorce. This can be very harsh and unfair, particularly for people who have just been separated and divorced and whose finances have been devastated. Huge debts are often accumulated because of legal bills and other expenses. Sometimes these are paid off after equalization payments are made, but sometimes it is necessary to pay them off over a period of time.

We suggest it is a good idea you find out your credit rating. Make sure you check the entries to ensure they are correct — they can be wrong. If you do not have a credit rating, take the steps to create one.

CRITICAL ILLNESS INSURANCE

Fabio Ventolini, CFP, CDEFA

Many of us are keenly aware of the importance of insuring our lives. We want to leave our dependents free of onerous debts and with sufficient assets to provide them with an adequate income.

Many people, however, do not think about the costs that can come with a debilitating illness. There can be expenses relating to private nursing, or modifications to your home or vehicle to improve your mobility. There are specific day-to-day needs, such as caring for children. If there is not enough money to cover these situations, the anxiety and stress could exacerbate your medical condition.

Statistics tell us that one in three Canadians will develop life-threatening cancer; 50 per cent of heart attack victims are under 65 years old; and each year 50,000 Canadians suffer a stroke. Not surprisingly, the probability of incurring a critical illness increases as you age, especially after the age of 45.

Age	30	35	40	45	50	55
Probability	10%	10%	10%	20%	30%	60%

Disability insurance may cover some of the costs incurred with a critical illness, however, critical illness insurance is designed specifically to offset these expenses. It will provide a lump-sum benefit to help support you financially if you are diagnosed with, and survive, a specified critical illness. The money can be used in whatever way you wish, for example:

- **Reducing your financial burden:** Pay off or reduce your mortgage, credit cards or other debts or keep your business running.
- **Maintaining your independence:** Modify your home or vehicle to improve your mobility. Hire domestic help during your recovery. Fund a leave of absence for yourself or your spouse.
- **Accessing cutting-edge medical services:** In Canada, pay for medications and treatment not covered by provincial health plans. Outside Canada, pay for treatment that may not be available at home, in addition to your family's travel and lodging expenses.
- **Assisting in your recovery in any way you choose:** Spend more time with your family or use the benefit in other ways that can help you focus on getting well.

Fortunately, survival rates for people who suffer most critical illnesses are increasing. Since 1950, however, there has been a 50% decrease in the rate of recovery from a heart attack or stroke.

I have known people who have lived 10 years or more after suffering a critical illness but have not been able to work as they once did, unable to earn the same amount or save the same amount for retirement. Critical illness insurance in these situations could have made a significant difference to their lives.

Even if you have your own income replacement insurance and CPP coverage, critical illness insurance may be still be appropriate

Critical illness insurance is offered by a number of companies. Most provide a lump-sum benefit for the following conditions:

- Alzheimer disease
- Aortic surgery
- Benign brain tumour
- Blindness
- Cancer
- Coma
- Coronary artery bypass surgery
- Deafness
- Heart attack
- Heart valve replacement
- Kidney failure
- Loss of independent existence (not included with all plans, but can be added as an optional benefit)
- Loss of limbs
- Loss of speech
- Major organ failure while on transplant waiting list
- Major organ transplant
- Motor neuron disease
- Multiple sclerosis
- Occupational HIV infection
- Paralysis
- Parkinson disease
- Severe burns
- Stroke

As with any insurance, ask yourself, "What if one of these things happens to me?" If you do not have assets that will cover these contingencies, you would be wise to review the issue with your financial advisor.

MAKE BELIEVE WEALTH

Chris Snyder, CFP, RFP

Some readers may have seen the recent Forbes Magazine article on the estimated wealth of 15 fictional characters. They range from Scrooge McDuck to the Tooth Fairy to Sir Topham Hatt, who owns the railroad of Thomas the Tank Engine.

According to Forbes' estimate, the most wealthy of the Fictional 15 is Carlisle Cullen Forks, the Vampire Doctor from the Twilight series of books and films. He is 370 years old and, largely because of three centuries of compound interest, his fortune has grown to \$34.1 billion. He is helped by his financial advisor's daughter, who can see into the future. Futhermore, he has no healthcare or food costs.

Carlisle Cullen Forks is followed closely by Scrooge McDuck, whose \$33.5 billion fortune is based on gold and treasure hunting. In fact, Scrooge may now be in first place, since gold has risen in price since the last estimate was carried out.

In Forbes' 2008 edition, Uncle Sam was in first place with an infinite worth. Because of the economic downturn, however, Uncle Sam is now off the charts.

Here is the Forbes Magazine list:

Name	Location	Wealth (bln\$)	Age	Source of wealth
1. Carlisle Cullen Forks	Wash.	\$34.10	370	Compound interest, long-term investments
2. Scrooge McDuck	Duckburg, U.S.	\$33.50	81	Mining, treasure hunting
3. Richie Rich	Richville, U.S.	\$11.50	10	Inheritance, conglomerates
4. Tony Stark	New York, N.Y.	\$8.80	35	Defence
5. Jed Clampett	Beverly Hills, USA	\$7.20	51	Oil, gas, banking
6. Adrian Veidt	New York, N.Y.	\$7.00	47	Marketing
7. John Wayne	Gotham City, U.S.	\$6.50	32	Inheritance
8. Tooth Fairy	N/A	\$3.90	Ageless	Inheritance
9. Thurston Howell III	Private Island	\$2.10	60	Howell Industries, South Pacific
10. Sir Topham Hatt	Island of Sodor, U.K.	\$2.00	55	Railroad, real estate
11. Artemis Fowl II	Dublin, Ireland	\$1.90	15	Inheritance, theft, technology patents
12. C. Montgomery Burns	Springfield, U.S.	\$1.300	104	Energy
13. Chuck Bass	Manhattan, N.Y.	\$1.100	18	Real Estate
14. Jay Gatsby	West Egg, N.Y.	\$1.000	30	Racketeering, investments
15. Lucille Bluth	Newport Beach, California, U.S.	\$0.95	68	Real estate

■ FEAR AND YOUR INVESTMENTS

Chris Snyder, CFP, RFP

Fear — the strongest of all human emotions when it comes to money — has again reared its ugly head as people flee from stocks because of the Greek/EU financial situation. One measure of this fear is the VIX volatility index, which is now at its fourth highest point since 1990. (It reached its highest point after the Lehman Brothers collapse in 2008.)

This current downturn shows the fragility of people's emotions. Many investors have backed out of the market quickly, basing their retreat on the rationale, "I don't want to go through a huge downturn again — I'm getting out, even if I am wrong."

Although fear is one of the major causes of the 12% drop in the markets since early April, it is not the only cause. The underlying precipitator is the Greek debt issue, which many people fear might have a domino effect on the rest of the European Union. The most vulnerable countries are Portugal, Ireland, Italy and Spain. All have large debts that include holding the loans of the other countries in this group.

Another factor for the market drop this spring was the correction from the huge up-tick of the market after it experienced the lows of March 2009. Corrections of 10% are not uncommon and since 1928, we have had 20 corrections of this magnitude — an average of one every 2.8 years. The longest has been 252 days, the shortest three days and the median 54 days. The minimum correction was 12% and the maximum was 19%. We are now at 12%. The following chart, courtesy of Fidelity Investments, tracks these market corrections.

Although fear is largely spread by the media, human nature dictates that most of us have a fear of the unknown. A normal reaction is to escape, and backing out of the market is one way to deal with the fear.

The cause of the Greek debacle comes back again to excesses, particularly government spending more than it takes in. Borrowing by government, business or individuals is certainly an acceptable practice, but one needs to pay the interest on the debt and repay the debt in a reasonable period of time.

It appears there will be volatility in the market for some time, and choosing the right time to get out is certainly difficult and usually unwise. It is not uncommon for some of the biggest increases to come immediately after a big "down" day.

Certainly, this is a critical time for the EU since it has backstopped \$1 trillion Euros of debt. However, this is just a loan guarantee, and the EU does not necessarily have to come forward with cash.

You may remember the EU was started some years ago to lower trade barriers and simplify doing business in Europe. This led to the formation of an economic union, which could act as a trading bloc to benefit all Europeans.

But the EU was also put into place to act as a deterrent to future wars. For hundreds of years, Europe had been torn apart by wars which were fought with high casualties. Those remembering the Second World War are growing fewer in number, but there are plenty of books and movies to remind us that short-term financial hardship is much preferable to war. The Russians alone lost more than 10 million people in that conflict. Canada lost 44,000 and more than that were wounded. To keep things in perspective, approximately 150 Canadians have been killed in Afghanistan.

Our bet is that the EU and member countries are motivated enough that the EU will do what it has to in order to overcome this crisis. While the going may be rough in the markets, astute investors will find a lot of opportunities.

continued on page 5

FEAR AND YOUR INVESTMENTS

Historical Stock Market Corrections (1928-2010)

Start	Length of Correction	Time to 1st Correction After Bear Market Ends (Days)	Gain Before 1st Correction (Years)
23 Apr '10	27	1.2	80%
28 Nov '02	103	0.4	21%
16 Jul '99	91	N/A	N/A
17 Jul '98	45	N/A	N/A
7 Oct '97	20	7.0	233%
9 Oct '89	113	2.2	61%
10 Oct '83	249	1.8	69%
13 Feb '80	43	N/A	N/A
5 Oct '79	33	N/A	N/A
12 Sep '78	63	0.7	23%
28 Apr '71	209	1.5	51%
25 Sep '67	162	1.4	57%
3 Aug '59	218	2.4	56%
23 Sep '55	18	N/A	N/A
5 Jan '53	252	N/A	N/A
12 Jun '50	35	1.1	43%
5 Feb '46	21	N/A	N/A
14 Jul '43	138	1.6	69%
6 Apr '36	23	N/A	N/A
12 Jun '33	3	0.3	97%
14 May '28	36	N/A	N/A

Total # of Bull Market Years Since 1928 (out of 82)

57

Total # of Corrections

20

Frequency of Corrections

One every 2.8 years

Bull markets can have multiple corrections; **shaded areas** represent first corrections in a bull market; **non-shaded areas** (N/A) represent corrections that took place after the initial correction in a bull market. "Gain Before 1st Correction" defined as S&P 500 index price return from end of prior bear market to the peak established at the start of the correction. Number of bull years is total years from 1928 to 2010, excluding bear market periods. All references to the stock market represented by the S&P 500 Index. All returns are calculated using closing price return date from 1/3/1928 – 5/20/2010. Source: Bloomberg, FMRCo (MARE) as of 5/20/2010.

ESTATE PLANNING OPPORTUNITIES WITH ALTER EGO AND JOINT PARTNER TRUSTS

Vicki Lungu CFP

An increasing number of Canadians planning their estates are searching for alternatives that will allow them to transfer and pass along the assets they have acquired during their lifetime. Wills are the preferred method, but they have limitations. You must pay probate fees on all assets that pass through your estate and they can be as high as 1.5% of the assets. In addition, the terms of your will can be contested. A child or spouse unhappy with their share can ask the courts to change the terms of the will. Also, for a fee, anyone can obtain a copy of the probate application, which lists all your assets.

Alter Ego Trusts

In 2000, a change in legislation allowed Canadians over the age of 65 to transfer certain assets to a special type of trust called an Alter Ego Trust, which can be individual, or joint with your partner. Because these trusts do not form part of your estate, the assets in the trusts can avoid probate. Furthermore, assets transferred to these trusts do not immediately trigger tax provided:

- You are 65 or older and a Canadian resident;
- The trust is created after 1999;
- You (and your spouse when this is a Joint Spousal Trust) are the only beneficiaries of the income and capital from the trust during your lifetimes.

Here is how it works:

- You set up the trust under the trusteeship either of yourself alone or with your spouse. This allows you to maintain control over your assets.
- You name an alternate trustee who could take over in the event you become incapacitated or die.
- You select which of your assets to transfer: stocks, mutual funds, bonds, GICs, your home or cottage, rental or other real estate properties. (RRSPs and RRIFs are not eligible.)
- You receive all of the income and have access to the capital. You also decide who will be the beneficiary of any remaining assets.

Joint Partner Trusts work the same way as an Alter Ego Trust. One or both of the spouses will be the trustee, making all of the investment and operational decisions. Upon your death, the alter ego trust performs the same function as a will, in that it defines how trust assets should be distributed.

Taxation

Income and/or capital gains generated by the trust must be distributed to you. Any income left in the trust is taxed at the highest marginal tax rate on all income left in the trust (currently 46.43% in Ontario).

At the time of death, you are deemed to have disposed of all of the property at the fair market value of the assets on that date. (In a Joint Partner Trust, it will be upon the second death). As a result of this deemed disposition, any gains or losses in the trust are taxable to the trust, not to the individual's estate, and will be taxed at the highest marginal rate at that time. Gains deferred from the date of transfer will be taxable to the individual.

Capital losses cannot be transferred from the trust to the individual's estate to offset any gains and no personal credits are available.

By comparison, testamentary trusts can claim personal tax credits, such as the age credit. As a result, you may have better opportunities to save taxes with a testamentary trust than with an alter ego trust. Spousal attribution tax rules also apply with a testamentary trust — the income generated by your assets is taxed in the hands of the contributor of that asset to the trust.

Why consider these trusts?

There are some estate planning situations in which trusts can be very beneficial.

- **Eliminate probate fees and ensure estate liquidity**

Since trust assets are not part of your estate and are distributed according to the trust document, you could save probate fees, the amount depending on

continued on page 7

ESTATE PLANNING OPPORTUNITIES WITH ALTER EGO AND JOINT PARTNER TRUSTS

where you live and the value of the estate. You could save up to 1.5% of the value of your estate by avoiding probate and the trustee could distribute the assets immediately, avoiding the hassle and delays caused by the probate process.

- **Protect against estate litigation**

Currently provincial family laws do not apply to trusts. This could be an important if you are in a second or third marriage.

- **Preserve privacy and confidentiality**

Once probated, a will becomes part of the public domain. For a nominal fee, any member of the public can obtain a copy of your probated will, which would contain a list and total value of your assets at death. Any privacy that your family previously had regarding their assets could be lost. Trust documents specifying how the trust's assets should be distributed remain private.

- **Provide an alternative to a power of attorney**

If you have no power of attorney, these trusts can also be useful if you become incapacitated. The provincial law may decide who controls your personal affairs if you become incapacitated but with an alter ego trust in place, your alternate trustee takes over the administration according to your instructions in the trust deed. You will still, however, require a power of attorney to deal with property or assets not held in the trust.

- **Leave your options open**

A fundamental advantage of this type of trust is its flexibility. You can amend your choice of trustees, the number of beneficiaries, or the structure of the inheritances whenever you feel like it. You may change your mind completely, take all of your assets out of the trust and spend every last penny if it suits you.

Expenses will include set-up fees, professional fees for legal and accounting advice, possible trustee fees, maintaining accounting records for the trust and filing annual tax returns. Other potential problems to watch out for and possible solutions for them include:

- If you transfer private company shares or qualified farm property to the trust, the \$750,000 capital gains exemption is not available when these assets are sold. If you do move the asset, the transfer of the property should be done at the fair market value. This way, you take advantage of the \$750,000 capital gains exemption before the transfer.
- For individuals wanting to set up a trust in their wills for their beneficiaries (testamentary trusts), an alter ego/joint spousal trust may not be the best option.
- The property in an alter ego or joint partner trust cannot be transferred to a testamentary trust and will be subject to the highest marginal tax rates for as long as the trust is in existence.
- If you intend to name a charity as beneficiary of the trust, you should be aware of the tax implications. The trust is limited to a maximum credit of 75% of income earned in the year of settlor's death for transfer to (*is something missing here?*) No carry-back is allowed. If the donation is made through your will, a tax credit up to 100% of your net income is available for donations from your estate. Any amount over this limit may be carried back and used as credit against your net income from the previous year.

Despite the potentially negative tax consequences discussed above, there are advantages to the creation of an alter ego or joint partner trust and it can be an additional tool to consider when developing an effective estate plan. As with any tax-planning technique, it is important to assess your personal needs and objectives in consultation with a professional advisor.

Other considerations

When you're considering the advantages of a trust as a substitute for a will or power of attorney, keep in mind the cost associated with establishing and maintaining the trust.

