


# Globe Investor

Gold	\$819.58	+0.5%	SPONSORED BY  BULLION MANAGEMENT GROUP INC.
Silver	\$10.30	-0.6%	
Platinum	\$881.00	+2.1%	
www.bmginc.ca/metals			B M G

## INVESTOR BEHAVIOUR

# I await with trepidation the possible avalanche of tax-loss selling



**NOREEN RASBACH**  
INVESTOR'S DIARY

nrasbach@globeandmail.com

I'm always happy to hear other people's investing stories, although lately those tales always seem to centre on the severity of investment losses. This week, after hearing a few horror stories from friends and colleagues, it occurred to me that it's been months since I've heard a positive anecdote from anyone I know.

It's ugly out there, isn't it? No one even talks about making money any more; it's all about just trying to protect what you have.

Since we're heading into December, the timing is right to look at a possible silver lining

to those investing losses. 'Tis the season for tax-loss selling – when you sell equities that are losing money to claim the tax advantage that comes with capital losses.

Experts are expecting a huge amount of tax-loss selling this year because the conditions are perfect for it. Over all, share prices have plunged (as of yesterday, only 12 of the 241 stocks on the S&P/TSX composite have gained in 2008) and the markets have already seen big selloffs, particularly in September and October.

Losses are also coming after a few good years on the markets, which means that many investors have claimed capital gains over the past three years. According to tax expert and Globe and Mail columnist Tim Cestnick, the issue of capital gains is one of two crucial factors for investors in deciding whether to take advantage of tax-loss selling. (The other: "If you just don't like the investment any more.") If you file

for losses this year but have filed capital gains in the past three years, you can get a refund for some of the taxes you paid.

Here, according to Mr. Cestnick, is how it works: First, losses have to be outside any registered plan, which means that if you're investing through your RRSP or RRIF, you can't take advantage. Also, you have to make sure that you sell your shares before year-end, which means that you have to sell just before Christmas to make sure the trade is settled in time.

If you have losses this year that are higher than the capital gains you have this year, "then you are entitled to carry those losses back – and apply them against capital gains that you may have realized or reported in the last three years – so, 2007, 2006 and 2005."

One other caveat is that an investor has to wait 30 days before repurchasing a stock sold for tax-loss purposes.

Not surprisingly, Mr. Cestnick is seeing a lot of people this year who are considering tax-loss selling, and not just because they have significant losses or the possibility of big tax benefits. "Many people just aren't comfortable with their portfolios right now. Not only are they selling because they want to trigger losses, but more importantly, because they're not comfortable holding what they're holding."

Like many investors, my investments are in my registered retirement savings plans, which means I can't take advantage of tax-loss selling even if I wanted to. But there are still some very big implications for me involving the market itself: If a number of investors choose to sell off to meet that late-December deadline, prices will decline and markets will fall again.

Eric Kirzner, a professor at the Rotman School of Management who holds the John H. Watson chair in value invest-

ing, says it's reasonable to expect substantial tax-loss selling this year "given that we've seen one of the biggest selloffs in recorded history – maybe only matched by 1932."

He also says there's no question that a lot of the selling will be technical, "that is, unrelated to the fundamentals of the company but related to capturing a tax loss." Investors might not be unhappy with their holdings but will sell anyway for the tax advantage.

What nobody really knows, Mr. Kirzner says, is how much of that tax-loss selling has already taken place, and how much will still be done in the month to come.

He generally advises people to make investment decisions independent of tax decisions – "If you want to get out for some reason, you should be getting out" – but admits that this year the tax implications are "very real" to a lot of investors. For the right person, tax-loss selling "will put real cash

in your pocket."

I certainly can understand how irresistible it would be for someone in certain circumstances to want to get out and take what tax money is available. Unfortunately, my losses are like those of everyone else who invests through their RRSP – increasing and not eligible for tax considerations. All I get to look forward to is the potential of another selloff – and more sad stories from my friends.

### TELL ME YOUR STORY

It's been a tough few months for investors, but the year hasn't been all doom and gloom. What are you most proud about with your investments this year? What lessons did you learn from the falling markets, even if you learned it the hard way?

Drop me a line at nrasbach@globeandmail.com to share your story. I'll choose some of the best lessons for a column later in December.

## FINANCIAL FACELIFT

# Tuition costs mean retirement plan needs rethink

BY ANDREW ALLENTUCK

In Toronto, a couple we'll call Boris, who is 54, and Susi, who is 51, have a combined, after-tax income of \$115,200 a year. They have a modest mortgage for their income, just \$56,000, that they expect to pay off in two years, three school-age children, and \$618,000 in financial assets. They worry that turbulent financial markets will make it impossible for them to finance their retirements and to put their kids, ages 12, 10 and 8, through university.

"We would like to know if we have enough savings to have a gross income of \$100,000 a year in retirement and also enough to cover our kids' costs at university in the next 10 years."

### WHAT OUR EXPERT SAYS

Facelift asked Frank Wiginton, a financial planner at Tridelta Financial Partners in Toronto, to work with Boris and Susi to develop a way for them to have a secure retirement income and money for their children's post-secondary education.

"As they begin transitioning from working life to retired life, they need to start transitioning their financial affairs," the planner says.

Boris and Susi are aware that they will have major educational expenses for their children. The eldest, now 12, could begin post-secondary education in as little as five years. But there is only \$26,000 in the family's registered education savings plan (RESP). Nothing has gone into the RESP in recent years because Boris and Susi view investing as throwing money into a hole in which, courtesy of swooning markets, it just disappears.

Mr. Wiginton suggests keeping faith in financial markets.

He suggests putting \$7,500 a year into the RESP. That's \$2,500 per child, a sum that qualifies for the maximum Canada Education Savings Grant that is a maximum of the lesser of 20 per cent of contributions or \$500.

Once the eldest child begins university, they can cut contributions to \$5,000 a year for the next two years and then when the second child begins post-secondary education, to \$2,500 for the last two years. With a 6-per-cent growth rate, this will make the RESP swell to \$100,000 by 2014. Over the following years, each child can take \$12,000 for each year of university, the planner says. Payouts after age 18 are taxable in the hands of the beneficiary, who is presumably in a low tax bracket, the planner notes.

The cost of financing the RESP will begin at \$625 a month. Boris and Susi could extend their mortgage from its present termination in 2010 to 2012. They are currently paying it off at \$2,030 a month. The extension of the mortgage would reduce payments to \$1,269 a month. That would liberate \$761 a month and satisfy the funding requirement for the family RESP, Mr. Wiginton says. When their mortgage is paid off in 2012, they will be able to divert the \$1,269 monthly payments to savings.

Boris and Susi are unduly pessimistic about their retirement incomes, Mr. Wiginton suggests. Each has a defined benefit pension plan. Boris's plan is indexed, though Susi's plan is not.

They already have generated combined annual pension entitlements of \$18,000 for Susi and \$40,000 for Boris, assuming that he retires in 2014 at age 60. By age 65, when he begins to receive Canada Pension Plan benefits, his employment



J.P. MOCZULSKI FOR THE GLOBE AND MAIL

### Client situation

**THE COUPLE**  
Torontonians in their 50s.

**THE PROBLEM**  
Low RESP balances for university education for three kids, worries over retirement plans.

**THE PLAN**  
Extend mortgage amortization slightly to obtain cash for RESPs, add to RRSPs.

**THE PAYOFF**  
Ample funds for postsecondary education and more than enough cash for retirement.

**NET MONTHLY INCOME**  
\$9,600.

**ASSETS**  
House \$600,000, RRSPs \$550,000, Non-registered investments \$40,000, RESP \$26,000, cash \$2,000. Total: \$1,218,000.

**MONTHLY DISBURSEMENTS**  
Mortgage \$2,030, property taxes \$350, food \$1,000, utilities & phone \$370, restaurants \$300, entertainment \$250, clothing \$300, child care \$1,200, RRSP \$300, car gas & repairs \$500, travel \$500, car & home ins. \$190, house cleaning \$400, kids' hobbies \$450, life insurance \$260, charity & gifts \$450, savings \$250, misc. \$500. Total: \$9,600.

**LIABILITIES**  
Mortgage \$56,000.

pension would lose a bridge income and fall to \$37,340. Total for the couple so far at age 65: \$55,340.

Canada Pension Plan benefits start at age 65 of \$10,615 at current rates for each partner – that's another \$21,230 into retirement income. Add another \$6,204 per person for Old Age Security at age 65, a total of \$12,408, and the sum is \$88,978 in 2008 dollars at Susi's age 65.

The \$100,000 pretax retirement income target that Boris and Susi have set should be revised. After the couple have retired, they will not have to make RRSP contributions, fund employment expenses, or pay into their children's RESPs. Their mortgage will have been paid off. That reduces what they need to maintain their present way of life to

\$76,000 a year, Mr. Wiginton estimates. That's less than their projected income from employment and public pensions.

The couple can put surplus cash into their RRSPs in order to get the benefit of income tax deductions. They currently add only \$300 a month.

Though limited by the pension adjustment, which curtails the amounts persons with company pensions can contribute to RRSPs, they could boost their contributions. If they were to increase their RRSP contributions to \$1,500 a month after their mortgage is paid off, then at 6-per-cent annual growth and allowing for inflation running at 3 per cent a year, their RRSP balances, currently \$550,000, would grow to \$622,200 by the time that Boris is 60, his intended date of retirement, the planner estimates.

If this sum were to generate income at 6 per cent a year before any inflation adjustments, it would add \$37,332 a year to their retirement income.

"Boris and Susi have a house and substantial tax-deferred investments. They have already met their retirement income targets," Mr. Wiginton says. "Moreover, if the last partner to die passes away at age 90, there will be an estate for their children, including their house, of \$1.37-million in 2008 dollars. They need not worry unduly about the future."

"This has given us assurance that we can relax about funding our retirement," Boris says.

"Our past financial planners in the past have been salespeople. This report is strategic," Susi adds.

» Special to The Globe and Mail

Contact us

andrewallentuck@mts.net

## MARKETS

# Armchair v. professional investor: These days it's a much fairer fight



**TOM BRADLEY**  
BUY SIDE

Tom Bradley is president of Steadyhand Investment Funds Inc. tbradley@steadyhand.com

I've been getting more "hate" mail lately. The e-mails from readers who disagree with me have become more pointed; I need oven mitts to handle some of them. It could be that I'm missing the mark more often, but I like to think it's more a reflection of the times that are – and the returns that aren't.

In many cases, the comments are a diatribe on the wealth management industry in general: its fees, complexity and lack of added value relative to the expectations that have been set (exotic travel, children at Harvard, your own vineyard). And it's interesting

that, in more than a few instances, the writer's conclusion has been to fire their advisers and managers and go it alone.

Now, while I'm part of this currently unpopular profession, I am no portfolio management snob. I happen to think that some individual investors do a good job managing their own portfolio. But let me be clear. Those "some" make up a tiny portion of the population. There are very few people that have the time, interest, knowledge and psychological makeup to do it themselves. Most need to focus their efforts on being better consumers of investment services, not better stock pickers.

Having said that, I think the armchair investor who does have the time and interest is competing on a more level playing field versus the pros than at any time I can remember. It's a much fairer fight.

Obviously, the professionals have some important advantages. For starters, investing is their day job, so they have the requisite time, training and ex-

perience. With that comes a better flow of research information, including access to company managements and industry experts. They also have the tail wind that results from paying lower trading commissions – just pennies a share.

But the pro's edge is not what it used to be. With changes to company disclosure requirements and online access to conference calls and management presentations, the information gap has narrowed. As for trading, the commission discounts enjoyed by professional managers are often offset by the market impact of their large orders. For example, they have to pay up to buy a block of stock, or take a bigger haircut on a sale. A patient buyer of 5,000 shares through a discount broker will often have a lower cost of acquisition (commission plus market impact) than a buyer of 500,000 shares.

While the professional's edge has narrowed, the individual's advantages are as valuable as

ever. If small investors don't trade too much, they should be able to lower their costs by not paying management fees or absorbing marketing costs. Another big advantage is that smaller investors don't have liquidity constraints, so they can buy any size or type of stock. As a result, they can make a small company a large part of their portfolio, something the mega-managers in a consolidating industry cannot do.

Although it's a sad commentary, the fact is that individuals whose retirement horizon is years away can take a longer view than most portfolio managers. They can take advantage of the market's biggest structural inefficiency, namely "short-termism," because they aren't bound by the quarterly reporting cycle, fund constraints and/or career considerations.

Individuals are not beholden to an index or benchmark as many professionals are. If they feel uncomfortable not knowing what's on a bank's balance

sheet, they don't have to own it. Exposure to energy and resources can amount to 10 to 15 per cent of their portfolio, not 40-50 per cent. And they can collect the income from their corporate bonds, preferred shares and high dividend stocks, and ignore the short-term market gyrations.

In addition to those realities, there are a number of factors that make me think the field has levelled even more in the current environment.

Individuals aren't dependent on their bank or broker for credit, unlike hedge fund and private equity investors. Without a management fee of 2 per cent plus a 20-per-cent performance bonus to pay, they don't need to lever up their investments to make the numbers work.

They don't have redemptions to deal with, so they aren't forced to sell a stock on someone else's schedule. Indeed, individuals can take advantage of the current environment where forced or distressed selling is a regular occurrence.

While others are experiencing margin calls and client losses, an opportunistic buyer can find some real bargains.

Having stated the case for the amateur investor, I don't want to play down the skill factor or imply that success is guaranteed. Far from it. In this market, many individuals have had their head handed to them, as it's been a minefield for the types of stocks they like to own: banks, insurers, income trusts and, for the more adventurous, small-capitalization resource companies.

Still, I think this market will be a wake-up call for many Canadian investors, and that their first move (after sending me or someone else in the industry an angry e-mail) should be a careful assessment of the alternatives, which range from complete delegation to "do it yourself." I would like to see more investors move into the "do it yourself" camp, but I'll settle for just moving into the middle of the curve – being a good consumer of investment services.