# Weekly Updates Issue # 582



## 1. Weekly Markets Changes

**[September 16, 2016]**

| S&P TSX | S&P 500 | Dow Jones | NASDAQ | CAD/USD | Gold | WTI Crude |
|---|---|---|---|---|---|---|
| 14,450.69<br>-89.31 -0.61% | 2,139.16<br>+11.35 +0.53% | 18,123.80<br>+38.35 +0.21% | 5,244.57<br>+118.7 +2.31% | $0.7570<br>-0.92¢ -1.20% | $1,313.20<br>-18.60 -1.40% | $43.19<br>-2.52 -5.51% |

## 2. Hot real estate market lifts B.C. budget into billions

**[September 16, 2016]** British Columbia's hot real estate market has boosted the province's bottom line, freeing cash for a housing program and allowing the government to cancel a planned hike in medical services premiums.

Finance Minister Mike de Jong said Thursday that he's now forecasting a budget surplus of $1.9 billion, more than $1.6 billion over the original estimate in February.

He released a financial update that included improved revenue forecasts of about $2.5 billion, propelled largely by higher property transfer tax revenues and increased corporate and personal income taxes.

"Suffice it to say, it's been a pretty good year so far," said de Jong. "We were forecasting a surplus of $264 million. There's now a surplus forecast of $1.94 billion. We're in this position — the envy of the country really — because we've taken a balanced approach and haven't gone on spending sprees," de Jong said.

The greatly improved financial forecast comes just months before a provincial election in which B.C.'s Liberals are seeking a fifth consecutive mandate.

"This is a product of a strong economy," he said. "There are more people in B.C. There are more people coming to B.C. There are more people working in B.C. They are earning more money and therefore paying more taxes."

Property transfer tax revenues are now projected to be $965 million above the original forecast. The budget has been revised to forecast $2.2 billion in property transfer tax revenue, which includes the foreign buyers tax the government introduced in July.

De Jong didn't say how much had been generated so far by the foreign buyers tax, but added that figure would be released next week.

The government has been under pressure much of the past year to take measures to address Vancouver's overheated real estate market, prompting the Liberals to introduce a 15% foreign buyers tax in July.

"There's no question the market in the Lower Mainland, in Metro Vancouver, in other parts of B.C. has been growing at a pace that ultimately the government thought was unsustainable and warranted intervention," de Jong said. "And we did."

The financial update forecasts 40,000 annual housing sales, with foreign buyers making up five per cent of that number.

De Jong said the government will use $500 million from the property-tax windfall to fund a housing affordability initiative to be announced next week.

He said last spring the province began examining housing and retail developments that have grown near major Vancouver area transit exchanges.

The minister said higher revenues will also allow the government to cancel the planned four per cent medical services plan premium increase originally scheduled for next year.

New Democrat finance critic Carole James said it appears de Jong and the Liberals don't understand that many British Columbians are struggling to make ends meet after facing increased rents and housing costs and higher services fees and utility rates.

"The government really wants you to believe everything is fine in B.C. but for many, many families they are struggling," she said.

James said it's ironic that the government's increased property transfer tax revenues are largely a result of its failure to tackle the issue of out-of-control housing prices years ago.

## 3. How to fix TFSA overcontributions

**[September 16, 2016]** Fall is often a time when Canadians make excess contributions to registered plans. Sometimes, the excess is the result of pre-arranged periodic payments. Other times, the cause is windfall payments (e.g., bonuses) directed to registered plans. Regardless, excess contributions to RRSPs and TFSAs can lead to penalty taxes. For this article, we'll focus on excess contributions to TFSAs and discuss options for dealing with excess TFSA amounts.

## TFSA refresher

TFSA contribution room, available to Canadian residents age 18 and older, is calculated as follows:

TFSA dollar limit for the year ($5,500 for 2016)

+

Unused TFSA contribution room from the previous year

+

Withdrawals from the TFSA in the previous year

From 2009 to 2012, the TFSA dollar limit was $5,000 per year. The limit increased to $5,500 for 2013 and 2014, and $10,000 in 2015. With the election of a new government last year, the TFSA limit returned to $5,500 for 2016 and is subject to indexation for future years.

Unused contribution room carries forward to a future year, but does not accrue for any year that an individual is a non-resident of Canada. Contribution room is available, however, without proration for the years an individual turns age 18, emigrates from or immigrates to Canada, or dies. People can confirm their TFSA contribution room by accessing the CRA's My Account, MyCRA app or Tax Information Phone Services. Or, the client can contact the CRA directly to request a TFSA Room Statement or Transaction Summary.

## Allowable withdrawals

One of the great benefits of the TFSA is its flexibility. When an individual withdraws from a TFSA, unlike RRSPs, contribution room is not lost. The amount withdrawn is added to the individual's TFSA contribution room the following calendar year. Consider this example:

Tina regularly contributes to her TFSA. In January 2016, she began the year with TFSA contribution room of $11,000. On February 10, she contributed $10,000 to her TFSA. Later in the year, on March 15, she withdrew $2,000 for home renovations.

Given that Tina had not yet maximized her TFSA for the year, she can contribute another $1,000 in the current year, 2016. In addition, her $2,000 withdrawal will be added to her TFSA contribution room beginning in 2017, allowing her to re-contribute the amount withdrawn.

## Penalized amounts

When an individual exceeds his TFSA contribution limit for the year, the excess, referred to as a "TFSA excess amount," is subject to a penalty tax of 1% per month. The tax is calculated based on the highest excess amount for the month and, unlike RRSPs, there is no $2,000 grace amount.

If you owe TFSA penalty taxes, you must file a special TFSA return (Form RC243) to calculate and report the taxes. The return must be filed by June 30 of the following year, and any taxes owed must be paid by that date. If the return is filed late, additional penalties and interest may apply.

When an individual has overcontributed, he'll owe penalty taxes for the period that he's over his limit. But he can correct his situation and avoid additional taxes by:

- immediately withdrawing the excess amount, or,
- waiting for new contribution room to become available the following year.

With the latter option, the 1% tax would apply to excess amounts for each month up to the end of the current year. Thereafter, new contribution room would absorb the excess and, depending on the amount of new room, the tax would cease. Where excess amounts are immediately withdrawn, the timing of withdrawals is important. Consider the following example:

Tina regularly contributes to her TFSA. In January 2016, she began the year with TFSA contribution room of $11,000. In error, Tina over-contributed to her TFSA for the year. Her 2016 contributions and withdrawals were as follows:

| Date | Transaction |
|---|---|
| February 10 | $10,000 contribution |
| March 15 | $2,000 withdrawal |
| April 10 | $2,000 contribution |
| July 13 | $3,500 contribution |

In speaking with her financial advisor, Tina had the following questions:

1. How much was my excess contribution for the year?
2. How would the CRA calculate my penalty tax?
3. How can I correct my excess contribution situation?
4. How much can I contribute beginning in 2017?

### How much was Tina's excess contribution for the year?

Tina contributed a total of $15,500, which is more than her $11,000 contribution limit for the year. But is her penalty tax based on an excess amount of $4,500, or, after considering her $2,000 withdrawal on March 15, $2,500?

Although Tina withdrew $2,000 on March 15, the withdrawal occurred before she created an excess amount. As a result, she does not receive credit for the withdrawal for 2016 tax purposes. If the withdrawal occurred after her excess amount was created (i.e., after the April 10 contribution), the withdrawal would have been considered a "qualifying portion of a withdrawal" and would have reduced her excess amount and associated taxes. Since the withdrawal occurred before Tina's excess contribution, it does not factor into her penalty tax calculation for the year. Therefore, her excess contribution for the year was $1,000 as of April 10 and $4,500 ($1,000 + $3,500) as of July 13.

**How would the CRA calculate Tina's penalty tax?**

There is no issue with the February 10 contribution as it does not exceed Tina's contribution limit for the year. The excess contribution arises on April 10, and Tina's penalty tax is calculated from that point forward. For 2016, the tax would be $300:

$1,000 x 3 months (Apr – Jun) x 1%, plus

$4,500 x 6 months (Jul – Dec) x 1%.

**How can Tina correct her excess contribution situation?**

The above calculation assumes Tina remains in an excess contribution situation for the remainder of the year. If this is the case, for penalty tax purposes, new contribution room of $7,500 ($5,500 limit + $2,000 withdrawal from 2016) would become available on January 1, 2017 and excess contribution taxes would cease. However, the monthly tax would remain payable for the remainder of 2016. Alternatively, once the excess amount is created, Tina can immediately withdraw the excess. If she did that, the tax would be payable for the month(s) in which there is an excess, but future taxes would cease.

**How much can Tina contribute beginning in 2017?**

If Tina withdraws her excess contribution before the end of 2016, she can contribute $7,500 beginning January 1, 2017 [($5,500 + (-$4,500) + $6,500]. If Tina does not withdraw the excess before the end of 2016, new contribution room will absorb the excess, allowing Tina to contribute $3,000 for 2017 [$5,500 + (-$4,500) + $2,000]*.

For most Canadians, dealing with excess TFSA amounts is a hassle. When faced with such a situation, however, knowing the rules will help to minimize taxes payable.

*2017 TFSA dollar limit + unused room at end of 2016 + 2016 withdrawals; Unused room at the end of 2016 is calculated as: (unused room at the end of 2015 + 2015 withdrawals + 2016 TFSA dollar limit – 2016 TFSA contributions)

## 4. 85% of funds underperformed S&P 500 this year

**[September 16, 2016]** Eighty-five percent of actively managed, large-cap funds underperformed the S&P 500 in the past year, new data from S&P Global shows.

The firm's Spiva statistics, released Thursday in a mid-year report, are updated to June 30, and show over the past five years, an even higher rate, 92%, of large-cap U.S. funds underperformed the American benchmark.

"The figures are equally unfavorable when viewed over longer-term investment horizons," the S&P report says. "The headline international equity and emerging market equity indices rebounded sharply during the first half of 2016. The gains, however, were not sufficient to erase the losses sustained in 2015."

S&P Global notes that active funds with foreign exposure performed worse, and fund size also made a difference. "Generally, larger funds perform better than smaller funds," it says.

The data uses fund returns net of fees, with S&P Global noting: "Fees have an important impact on fund performance."

The report adds: "The hunt for yield has become increasingly challenging for fixed income managers. During the one-year period studied, the majority of managers investing in government and corporate credit bond categories underperformed their benchmarks, with the exception of those managing intermediate-term corporate credit funds."

## 5. Ontario workplace insurance board cuts rates

**[September 15, 2016]** Small businesses welcomed the Ontario Workplace Safety and Insurance Board's decision to cut rates by an average of 5 per cent across all sectors.

It's the first rate reduction since 2001. The Canadian Federation of Independent Business says the cut was important as small business owners deal with rising hydro and payroll costs.

"With the cost of doing business rising in the province, cutting WSIB rates offers not only much-needed stability to Ontario's job creators, but financial flexibility to reinvest in their businesses and the Ontario economy. We look forward to the sector-by-sector breakdown to see how all of our members will be affected," the CFIB's Julie Kwiecinski says in a statement.

Since 2011, the WSIB has reduced its unfunded liability from $14.2 billion to $5.6 billion and is on track to eliminate it by 2021, the CFIB says. It has also made improvements in customer service, and reduced the length of its claim reporting forms by 60%.

## 6. Household debt reaches record high, again

**[September 15, 2016]** Canadian household debt reached a record in Q2, surpassing the previous quarter's record, Statistics Canada data showed on Thursday.

The ratio of household debt to disposable income rose to 167.6% in Q2, up from 165.2% in Q1. The figures indicate Canadians had $167.60 of debt for every $100 of disposable income.

Household debt, which includes consumer credit, mortgages and other loans, climbed 2% in the quarter, rising faster than the 0.5% gain for disposable income.

Economists have warned about rising debt levels amid low interest rates and skyrocketing housing prices in Vancouver and Toronto. The BoC also says it's watching household debt levels as a financial system vulnerability.

Credit Counselling Society of B.C. president Scott Hannah says the household debt numbers are one cent higher than the average debt that was held by U.S. consumers when the severe recession hit in 2008.

Hannah says much of the U.S. economic collapse was linked to mortgages and notes the Canadian market is more robust, but he points to the recent slowdown in Vancouver's home sales as proof that conditions can change rapidly.

The Credit Counselling Society is also flagging Stats Canada figures showing an 8.2% increase in non-mortgage debt among those over 65 years of age.

## 7. Adapt to lower growth and returns, says BoC's Wilkins

**[September 14, 2016]** As the growth potential of the global economy falls and as central banks struggle to provide stimulus, the private sector and policymakers will have to take steps to mitigate risks, said Bank of Canada senior deputy governor Carolyn Wilkins in a speech today to the Official Monetary and Financial Institutions Forum in the U.K.

Heading off risks won't be easy, she suggests, noting that investors and market participants will have to adapt to lower neutral rates. Further, countries must continue to work to meet their G20 commitments as well as take fiscal and structural measures to improve long-term growth and productivity, says Wilkins.

The current environment is tough to deal with, she says, because "we typically link financial stability risks to unsustainably high growth, [but] slower growth and lower returns can also add to vulnerabilities in the financial system."

And, economies around the world face the prospect of sluggish growth because the two components driving potential output—labour supply and productivity—are rising more slowly than in the past, she adds–the Bank of Canada estimates that global potential GDP growth declined from a peak of about 5% in 2005 to just over 3% this year.

Wilkins notes, "Natural by-products of slower potential growth are not only weaker corporate profits and dividends, but also a lower average rate of return on investments."

To gauge this effect, economists estimate the neutral rate (which is the interest rate needed to balance savings and investment when the economy is operating at potential), and that's fallen in Canada to 1.25% today, from 3% in the early 2000s.

Further, with the Bank's policy rate currently at 50 basis points, she notes that monetary policy in Canada remains quite stimulative–although less so than it would have been a decade ago when the neutral rate was higher.

Wilkins says slower growth and a lower neutral rate heighten financial vulnerabilities through several channels. For starters, households could experience longer and more frequent periods of shrinking incomes, making their debts more burdensome.

As well, a lower neutral rate could encourage investors to take on more risks in their search for higher returns. And, lower rates put pressure on bank business models. "We have to adapt to the new reality of lower potential growth," Wilkins says. "The faster we do this, the safer the financial system will be."

## 8. Fintrac finds deficiencies at nearly 500 real estate firms

**[September 14, 2016]** Canada's anti-money laundering agency conducted on-site examinations of more than 800 real estate companies over nearly five years, and it found "significant" or "very significant" deficiencies during 60% of those visits, according to new Fintrac data.

A document obtained by The Canadian Press through an Access to Information request shows Fintrac conducted 823 examinations of companies in the real estate sector between 2012 and mid-June of this year. And, the federal anti-money laundering watchdog found "significant" deficiencies with the anti-money laundering and anti-terrorist financing controls at 468 of those companies, while 28 companies had "very significant" deficiencies.

Meanwhile, 324 companies had only "limited" deficiencies. None of the companies were named in the document.

When asked what constitutes a "limited deficiency," Fintrac said it includes instances where the deficiencies are minor or the regulations are only partially being followed. According to the watchdog, an example of a significant deficiency is when there is a “excessive number” of minor deficiencies found, or a number of more severe issues.

Meanwhile, very significant deficiencies include instances where there is an “unacceptable” number of minor and serious issues, or infractions that are “very serious” in nature.

Federal anti-money laundering and anti-terrorist financing laws require companies in certain sectors–types of companies include banks, casinos and real estate firms–to identify their clients, keep records and report large cash deals and other suspicious transactions to Fintrac (there are roughly 20,000 companies in the real estate sector that fall under the regulations).

If violations are found during an on-site examination, that can lead to fines of up to $100,000 per violation for individuals, and up to $500,000 per violation for companies, depending on severity.

However, the federal watchdog issued monetary penalties only nine times during the almost five-year time span, the document shows.

When asked why more penalties weren’t issued, Fintrac told The Canadian Press it considers several factors when deciding whether or not to fine a company. Those factors include the business’s compliance history, the seriousness of the violation and the extent to which the company has taken steps to correct the problem.

And there are a number of avenues the watchdog can pursue besides a fine, the agency said, such as establishing an action plan or conduction a follow-up exam. “In the nine cases identified, it was determined that the most appropriate course of action was to issue an administrative monetary penalty,” Fintrac spokeswoman Renee Bercier said in an email to The Canadian Press. “For the remainder, other enforcement actions were undertaken.”

According to the federal agency’s website, Pickering, Ont.-based Countrywide Generations Realty was fined $11,440 in July 2015 for six violations including incomplete record keeping and failing to identify clients in some instances. In another case, Mississauga, Ont.-based ReMax Active Realty was fined $6,770 back in 2013 for four violations, including failing to develop and apply policies and procedures to detect money laundering.

In total, Fintrac has issued 12 monetary penalties in the real estate sector since Dec. 30, 2008, though in the vast majority of instances the companies were not publicly identified.

Jack Bensimon, the anti-money laundering adviser at Toronto-based Securefact, told The Canadian Press he wasn’t surprised to hear about the results of the examinations, given the lack of knowledge about best practices amongst real estate professionals.

“There are very, very few real estate brokerage firms that I’ve come across that actually have dedicated compliance staff,” Bensimon said. Also, the low levels of compliance in the sector are problematic because real estate is highly vulnerable to money laundering, according to Bensimon.

“Canada is known to be a safe haven for parking investment capital,” he said to The Canadian Press, adding that it’s fairly easy for criminals to disguise the initial source of the cash by transferring several times, a process referred to as the “layering approach.”

The Canadian Real Estate Association told The Canadian Press it has provided training for its members with regard to preventing money laundering.

Pierre Leduc, a spokesman for CREA, said the organization has asked Fintrac for information about the results of examinations, but the federal watchdog has not provided it. “Since we aren’t getting audit information from Fintrac we don’t know specifics of compliance challenges, which makes it incredibly difficult for us help our members address any shortcomings,” Leduc said in an email to The Canadian Press.

## 9. Get ready for tougher mortgage rules

**[September 12, 2016]** Homebuyers should expect tougher mortgage rules to fully kick in by January 1, 2017.

That’s because the Office of the Superintendent of Financial Institutions (OSFI) has released for public consultation revisions to its Capital Adequacy Requirements Guideline (CAR).

OSFI says, “[This] guideline provides a framework for assessing the capital adequacy of federally regulated deposit-taking institutions, and [it’s] updated periodically to ensure that capital requirements continue to reflect underlying risks and developments in the financial industry,” which includes the Canadian mortgage market.

Along with other revisions, says OSFI, “the draft CAR Guideline has also been updated to include planned revisions to the treatment of insured residential mortgages […] These changes aim to reinforce the need for banks to exercise prudent underwriting and proper due diligence when originating insured mortgages.”

As MoneySense reports, this means “the nation’s financial regulator, banks and lenders that offer mortgage financing will face stricter regulations and this will translate into tougher lending rules for homebuyers.”

In a letter to the industry from December 2015, OSFI highlights that risks in Canada’s mortgage market continue to evolve, with household debt growing faster than income and real estate prices heating up. At that time, it announced plans to propose changes to help protect Canadians and financial institutions.

## 10. Prospects get worse for Energy East pipeline

**[September 12, 2016]** A bank analyst says that the likelihood of the Energy East pipeline project being built has fallen to 25%, from 33%, after members of a regulatory panel were forced to resign last week.

CIBC analyst Robert Hope says in a note to clients that poor prospects have gotten worse for the controversial $15.7-billion pipeline, which would bring about 1.1 million barrels of oil per day from Alberta and Saskatchewan to Eastern Canada refineries and a marine terminal in New Brunswick.

On Friday, the National Energy Board announced that its three Energy East panellists had recused themselves following complaints that two of them met with former Quebec premier Jean Charest, a consultant for developer TransCanada at the time, last year to discuss the pipeline.

The Calgary-based regulator also said board chairman Peter Watson and vice-chairwoman Lyne Mercier will not be involved in choosing a new panel to resume hearings at a later date to avoid "an apprehension of bias."

NEB spokeswoman Sarah Kiley says a new panel will be chosen by a temporary NEB chair from a roster of board members slated to grow with new temporary appointments made by the federal government. She says the new board members are necessary to ensure enough panellists are available to serve who are bilingual.

She adds the regulator still hopes to finish its review process by its current deadline of March 18, 2018, but that the timeline may be extended if necessary to ensure a thorough review.

Analyst Dirk Lever of AltaCorp Capital in Calgary says the pipeline regulatory process has become so "murky" and "messy" due to political pressure that it's difficult to say that any pipeline approval can be assured.

# Have a nice and fruitful week!