



**ALSO IN THIS ISSUE:**

- Editorial Comment: It's Not That Complicated .....2
- Northwood Q&A: Issues Facing US Citizens Resident in Canada .....3
- Old Dogs, New Tricks .....4
- Summer Reading List .....4



**Chairman's Message**

Tom McCullough



Welcome to the Summer 2012 edition of the Northwood *Perspective*. This is a special one because it marks the 25th quarterly issue of this newsletter. I am grateful to the nearly 1,000 people who read our thoughts each quarter and I am constantly amazed at how many of you reply with interesting ideas, suggestions, and kind words. I receive comments from about 15-20% of the recipients in response to each issue. It is encouraging that we can help create a healthy dialogue on the issues faced by wealthy families and investors. So thanks for being a part of the Northwood *Perspective* over some or all of the past 25 editions and we hope you will continue to be part of the next 25 issues as well.

This has been a busy period at Northwood. We continue to focus the bulk of our time and effort on our existing clients. We also selectively add new clients and this has been a lively spring for us in that regard. We also continue to be actively involved in leadership and development of the community that serves families of wealth. Here are few examples:

1. Some of you will know that I teach a course in the MBA program at the Rotman School of Management (Univ. of Toronto) each spring. This is an important component in building the capacity of family wealth advisory capabilities for the future and adding to the body of thought leadership in the areas that are important to families. Scott Hayman is also a guest lecturer in the areas of tax and estate planning.
2. We recently co-chaired the inaugural Canadian Family Office and Advisors' Forum. This is a private meeting of an exclusive group of Ultra High Net Worth families, family office professionals and their legal, financial and strategic advisors from across Canada, selected based on their expertise and experience in this area. It was an excellent opportunity to share ideas, build relationships and build proficiency in serving the needs of families of wealth, alongside some of the very best minds in the country.
3. And finally, Northwood is looking forward to hosting the Wigmore Association meeting in Toronto this September. This is a group of six family offices from around the world (Germany, UK, US, Australia and Canada) that meets twice a year to share investment views, asset mix forecasts, and manager selections, and other ideas that will benefit our client families. You can see further details, including a copy of the Wigmore press release, on the Northwood website.

We look forward to continuing to play a leadership role in the family office and family wealth marketplace as it develops over time and once again thank all of our client families and our professional colleagues for their support, trust and confidence.

**The Rush to Safety**

Eric Weir, CFA, CFP



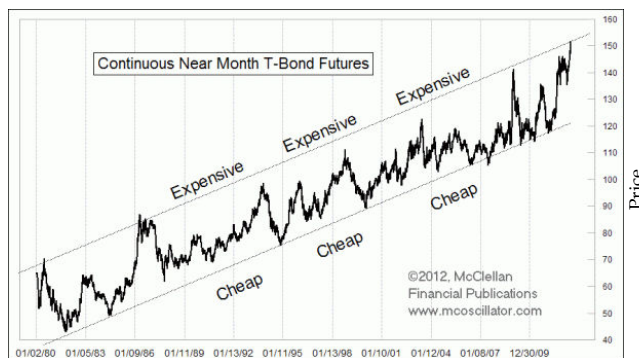
There is a new gold rush happening. But this time the 'gold' is safe assets or sovereign bonds of the highest credit countries in the world. Concerns about deflation, the Eurozone and global financial market stability are pushing nervous investors to the safest assets they can find -- so much so that yields don't seem to matter. The fear and frustration has become so pronounced that investors seem to be willing to do whatever it takes to keep their funds safe.

In the chart below you can see that investors are willing to lend their hard-earned savings to name-brand governments like Switzerland, Japan and Germany for ten years for almost no yield at all -- a paltry 0.5% to 1% per year. Yields in the US and Canada seem robust by comparison at 1.5% to 1.75%. If inflation persists at all, this will be a net money-losing proposition and taxable investors will see an even bigger annual net loss.

The World's Lowest 10-Year Government Yields				
June 1, 2012				
Rank	Country	Yield	1-Month Chg	3-Month Chg
1	Switzerland	0.48%	-0.22%	-0.23%
2	Japan	0.81%	-0.07%	-0.15%
3	Denmark	0.95%	-0.66%	-0.89%
4	Hong Kong	0.96%	-0.18%	-0.33%
5	Germany	1.16%	-0.50%	-0.70%
6	Sweden	1.19%	-0.59%	-0.73%
7	Singapore	1.41%	-0.12%	-0.03%
8	Finland	1.41%	-0.62%	-0.85%
9	United Kingdom	1.50%	-0.58%	-0.69%
10	Netherlands	1.52%	-0.71%	-0.78%
11	United States	1.53%	-0.41%	-0.49%
12	Norway	1.68%	-0.37%	-0.63%
13	Canada	1.74%	-0.39%	-0.37%
14	Austria	2.02%	-0.63%	-0.82%
15	France	2.26%	-0.69%	-0.60%

Source: Barry Ritholtz at The Big Picture

This trend of falling interest rates (and rising bond prices) has continued unabated over the past 20 years (see chart below), making bonds one of the best-performing asset classes over that period, particularly in the last decade as equities have stagnated.



Date

CONTINUED ON PAGE 2...

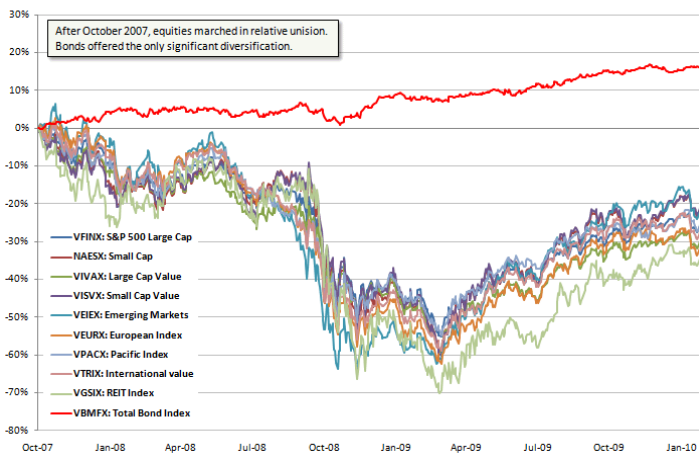
CONTINUED FROM PAGE 1 ... THE RUSH TO SAFETY

But how much lower can bond yields go? Or maybe a better question is how much longer can they stay this low? The range of opinions on this topic is wide. If slow growth continues and deflationary pressures mount as consumers and governments work themselves out from under the significant debt overhang, then rates could stay relatively low for a long time yet. If the world economies begin to grow and resolution is achieved in the Eurozone and other troubled areas and if the developing economies continue their outsized contribution to global growth, then rates should start to increase.

We believe that such predictions are courageous but rarely correct. Our experience suggests that the following approaches will add value:

- Diversification is important and bonds are an important part of a diversified mix of investments. It is one of the key ways investors can protect capital over time. The chart below shows how bonds (the solid red line) protected investor capital in the global financial crisis of 2008-09 when most other asset classes dropped in unison.

Asset Class Examples Using Vanguard Mutual Funds

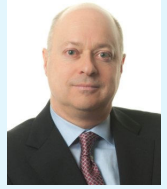


Source: Vanguard

- A shorter term laddered portfolio of high quality government and corporate bonds allows investors exposure to the asset class, protection for drops in yield (because the early part of the ladder has higher yields than today), and the opportunity to take advantage of higher yields when and if they finally come (as the lower-yielding bonds mature making room for higher yielding issues).
- Dividend-paying equities are also an attractive asset for taxable investors with current yields even higher than bonds, the possibility of growth in the dividend and the share price, and a more favourable tax treatment than interest income. It is important to remember that dividend-paying stocks still carry the risk of an equity security, and should not be thought of as a fixed income replacement.
- Corporate balance sheets have been the real stars of the past ten years. As consumers and governments have overextended themselves, corporations have been building cash reserves and improving their productivity. The low interest rates and modest wage inflation have helped them keep costs low. If you believe the financial system will survive and live to fight another day, and if you also believe in mean reversion, equities are due for much better performance after the lost decade of returns in the 2000s and corporations appear to be well positioned for the future. 🌲

## Editorial Comment: It's Not That Complicated!

Tom McCullough, MBA, CIM, CSWP, CFBA



We are currently in the midst of a very complex global realignment. After years of excess and success, driven by low interest rates and massive government and consumer debt, the world has hit the proverbial wall. Like many of you, each week I read dozens of commentators who opine on the complex and fragile mess we are in and the myriad of ways we can work our way out of it. It is an intricate, thorny and delicate problem that will require the best minds and a lot of force of character to resolve.

But at another level, the cause of the problem (and maybe even some part of the solution) is actually simple. When you strip everything away, the issue is this: **You cannot continue to spend more money than you earn.** There *are* consequences of spending today if you don't have the money. This applies to everyone - individuals, families, companies, governments. At some point you have to pay the piper. You can defer the pain for a while by whatever means you have available -- credit cards, second mortgages, or printing money. And you can hope to be skated aside by a change in fortunes.

But at some point, you have to pay the money back to the people you borrowed it from. We saw this in the US housing market where consumers overstretched on their home purchases and have now paid the price in collapsing home equity values. We are seeing this in spades in southern Europe right now, where for years governments have pandered to voters with big spending and mortgaged their future. And closer to home, the same story is playing out in the province of Quebec, Canada, where students have taken to the streets to protest a rise in tuition levels, even though they will still be among the lowest university fees in North America. They too will find out that nothing is ultimately free. What you borrow to spend today, will have to be paid back.

Debt-free living is the epitome of flexibility. Apart from mortgages, student loans and Keynesian government deficits, all of which were intended to be temporary, living beyond your means and taking on debt to fund living expenses is a dangerous path. Debt leaves you at the mercy of economic shocks and personal setbacks. The habit of debt financing can also seep into the psyche and practice of wealthy families and individuals, just as it can in governments and the regular population. In fact, spending levels tend to grow along with wealth. And the patterns are quickly picked up by younger generations who aspire to live at a similarly high level but don't yet have the resources. And so it goes.

The world is full of complex problems. But in some ways, it is not that complicated. 🌲



## Northwood Q&A: Issues Facing US Citizens Resident in Canada

Barrett Lyons, CA, CFP



The number of US citizens renouncing their US citizenship is climbing, and reached 1,485 in 2010, up from 731 in 2009 and 226 in 2008<sup>1</sup>. In 2011, the billionaire co-founder of Facebook, Eduardo Saverin, gave up his US citizenship which raised many eyebrows. The question of whether a wealthy individual living outside the US border should keep their citizenship will depend on a family's goals and circumstances, but there continues to be a significant amount of activity around the topic.

The US continues to seek ways to increase its tax revenues and in 2010 legislated the Foreign Account Tax Compliance Act ("FATCA") rules that will begin taking effect in 2013. These rules are designed to ensure that all US citizens living outside US borders are reporting their worldwide income on US tax returns by having foreign institutions disclose US citizen account holder information. Concurrently, in 2009, the IRS introduced the Offshore Voluntary Disclosure Program ("OVDP") to entice US citizens who are offside on income tax or foreign bank account reporting to come forward. This amnesty program was reintroduced in 2011, and due to its success the IRS announced its third iteration of the program in January 2012. The IRS has reportedly collected more than \$4.4B from the first two OVDPs.

Northwood discussed the topic of US citizenship with Carol Fitzsimmons, a partner with Hodgson Russ LLP. Amongst other areas, Carol's legal practice advises on U.S. tax issues affecting U.S. taxpayers resident abroad, as well as cross-border estate planning.

**Northwood (NW):** *The rules for US citizenship are complex, but generally what qualifies an individual as a US citizen?*

Carol Fitzsimmons (CF): Being born in the US is the most obvious one, but a person born outside the US may also be a US citizen if one or both of his/her parents is a US citizen. Frequently I have clients whose parents were travelling in the US when they gave birth, and in some instances the parents were only in the US for a couple of days when the child was born – but that still makes their child a US citizen.

**NW:** *Does US citizenship ever expire over time if an individual moves out of the US, or is completing the process to formally renounce it the only way to surrender the citizenship?*

CF: For nationality law purposes, a US citizen remains in that status until he/she commits an "expatriating act" with the intent to renounce US citizenship. For US tax purposes, however, the only method for successfully losing one's citizenship, since 2008, is a formal renunciation at a US consulate.

The expatriation rules, both for tax and nationality purposes, have changed numerous times over the years. At one point, voting in a foreign election was an expatriating act, but that has not been the case for decades. Until the early 1970s, it is my understanding that a person becoming a Canadian citizen was advised on application that he/she could not have dual status, so obtaining Canadian citizenship may have constituted an expatriating act with requisite intent, but the burden is on the taxpayer to establish he/she in fact did have such intent.

**NW:** *What significant long-term risks do US citizens resident in Canada need to be aware of?*

CF: Individuals should be aware of US estate tax; the US taxes the value of assets at death, at rates potentially up to 55% beginning in 2013.

Additionally, US beneficiaries of Canadian trusts could face adverse tax rules if income is accumulated in the trust.

There are several inconsistent areas between Canadian and US income tax law. Common issues dual citizens face include:

- no principal residence exemption in the US (only a partial exclusion of gain);
- no lifetime capital gains exemption in the US;
- gifts may produce tax in Canada and gift tax in US without offsetting credits; and,
- personal service companies like professional corporations do not allow deferral of personal taxation in the US.

These differences can lead to a significant US tax liability in addition to any Canadian tax paid.

**NW:** *With the additional annual tax filings, maintaining US citizenship for Canadian residents may seem like a burden to some, but there must also be some significant benefits for maintaining US citizenship?*


CF: Of course. Many people decide to ultimately retire full-time in the US and maintaining citizenship will make the transition process an easy one (compared to the alternatives for non-citizens). Also, US citizenship will provide the opportunity to move back to the US for work at any point, otherwise a work visa would be required which can be difficult or impossible to obtain in some circumstances.

**NW:** *In January 2012, the IRS announced its third OVDP initiative. What is the current state of the voluntary disclosure environment?*

CF: FATCA compliance is approaching so as more time passes, there will be fewer places for US citizens to hide and continue to be non-compliant. Despite the amnesty, the OVDP has not been popular because penalties can be stiff, and are based on bank and investment account balances, not tax liability, so the OVDP is perceived as unfair by many US taxpayers in higher tax rate jurisdictions such as Canada, and the UK. Additionally, there is great uncertainty in dealing with the IRS and what they may impose penalties on (e.g. RRSP balances?). If non-compliant US citizens have not come forward, they should speak with a professional advisor sooner rather than later.

**NW:** *Are there additional issues or risks that Canadian resident US citizens should consider other than income tax? For instance, issues crossing the border?*

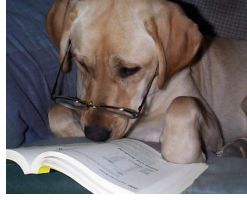
CF: Yes. US citizens are required by regulation to present a US passport when crossing the US border and I have heard of instances where border guards will deny entry because the individual did not have their US passport on hand. This is not always enforced, but likely will be more so in the future. Also, there is now a question on the US passport renewal form that asks if US tax returns have been filed and are current which indicates there is going to be more coordination between Border Services and Homeland Security with the IRS.

In summary, maintaining dual Canadian-US citizenship has its benefits but significant costs as well. When evaluating whether a Canadian resident should keep their US citizenship, they will need to balance their own family's goals vs. the complexities of cross-border tax and legal issues. 

<sup>1</sup> Source: Renunciationguide.com

## Old Dogs, New Tricks

They say that it is hard to teach an old dog new tricks. This hackneyed expression suggests that the older you get, the tougher it is to learn new things. Well, we are here to strike a blow on behalf of all the 'old dogs' out there to prove that we can still learn 'new tricks'. Northwood President Scott Hayman recently



received his Trust and Estate Practitioner (TEP) designation from the Society of Trust and Estate Practitioners. This elite designation complements Scott's other qualifications as a Chartered Accountant (CA) and Chartered Financial Planner (CFP). Northwood Chairman Tom McCullough, not to be outdone, has recently received the Certificate in Family Business Advising (CFBA) designation granted by the Family Firm Institute. These letters will sit alongside the MBA, Chartered Investment Manager (CIM) and Chartered Strategic Wealth Professional (CSWP) designations. Woof! 🌲

## Summer Reading List

Here, once again, is our Annual Summer Reading List, a popular feature in the *Northwood Perspective*. Each year in June, we chair the Canadian Private Family Office Summit in Banff, Alberta. We ask each of the speakers to share their favorite book ideas and then we publish the list in the *Northwood Perspective*, just in time for summer. Enjoy!



### Private wealth issues

- Freedom from Wealth: The Experience and Strategies to Help Protect and Grow Private Wealth, *Charles Lowenhaupt and Don Trone*
- Raising Financially Fit Kids, *Joline Godfrey*
- Wealth in Families, *Charles W. Collier*
- Stewardship in your Family Enterprise: Developing Responsible Family Leadership Across Generations, *Dennis Jaffe*

### Self-Development

- Fierce Conversations: Achieving Success at Work and in Life One Conversation at a Time, *Susan Scott*
- Inner Excellence: Achieve Extraordinary Business Success through Mental Toughness, *Jim Murphy*

### Biography/History

- Life, *Keith Richards and James Fox*
- Team of Rivals: The Political Genius of Abraham Lincoln, *Doris Kearns Goodwin*
- Merchant Kings: When Companies Ruled the World, 1600-1900, *Stephen R. Bown*
- Start-Up Nation: The Story of Israel's Economic Miracle, *Dan Senor and Saul Singer*

- 1491: New Revelations of the Americas Before Columbus, *Charles C. Mann*
- Coming Apart: The State of White America, 1960-2010, *Charles Murray*

### Psychology

- Demand: Creating What People Love Before They Know They Want It, *Adrian Slywotzky and Karl Weber*
- Thinking Fast and Slow, *Daniel Kahneman*

### Economics/Investments

- The Quest: Energy, Security, and the Remaking of the Modern World, *Daniel Yergin*
- The End of Growth, *Jeff Rubin*
- Broke: The New American Dream (DVD), *Michael Covel*
- Moneyball, *Michael Lewis*
- The Big Short: Inside the Doomsday Machine, *Michael Lewis*
- Boomerang: Travels in the New Third World, *Michael Lewis*
- The Alpha Masters: Unlocking the Genius of the World's Top Hedge Funds, *Maneet Ahuja*
- The New Investment Frontier, *Howard Atkinson and Donna Green*

### Other

- Politics and the English Language (Essay), *George Orwell*

### Fiction

- The Passage, *Justin Cronin*
- Gone Girl, *Gillian Flynn*
- Matterhorn: A Novel of the Vietnam War, *Karl Marlantes*
- Imperium: A Novel of Ancient Rome, *Robert Harris* 🌲



For more information or to set up an appointment, please call Tom McCullough or Scott Hayman at

Main: (416) 502-1245

[www.northwoodfamilyoffice.com](http://www.northwoodfamilyoffice.com)

Email: [tmccullough@northwoodfamilyoffice.com](mailto:tmccullough@northwoodfamilyoffice.com)

[shayman@northwoodfamilyoffice.com](mailto:shayman@northwoodfamilyoffice.com)

The Northwood Perspective is published by Northwood Family Office LP and Northwood Private Counsel Inc. Northwood Private Counsel Inc. is registered as a Portfolio Manager and Exempt Market Dealer in the provinces of Ontario and Quebec. The articles and information in this newsletter are prepared as a general source of information and should not be relied upon as personal investment, legal, or tax planning advice, and should not be construed as an offer to buy or sell securities. We have used our best efforts to ensure that all material contained in the newsletter is accurate at the time of publication; however, we cannot guarantee its accuracy or completeness. Any opinions expressed in this document are based on current analysis of market events and circumstances and are subject to change.