

The McCartney Report

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The Last Word

"If you don't know where you're going, you're going to need a map to get there. I'll provide you with a road map to financial peace of mind."

- Jeff McCartney

Welcome to The McCartney Report

The goal of the report will be to provide you, the reader, with useful, pertinent, and timely information on issues that are of interest to you, your investments, and your short, medium, and long term financial goals.

My Core Purpose is to help my clients to enhance their standard of living, while preserving their capital, and minimizing their risk, through the use of disciplined and comprehensive financial strategies.

My Business Beliefs are as follows:

- I believe most people experience various levels of anxiety about their money.
- I believe providing clients with disciplined & comprehensive strategies that preserve capital & minimize risk serves to alleviate their anxiety about money.
- I believe that to add true value to my clients & to become their primary advisor, I must go beyond investment management in my efforts for them.
- I believe in utilizing a Team of Experts to ensure my client's goals are satisfied.
- I believe that circumstances can change suddenly or over time. For this reason, I believe my client's needs and goals must be reviewed regularly

to ensure they are reflected in the investment and financial strategies we've developed.

- I believe in a process that is consultative rather than transactional.

I'm always happy to discuss my beliefs, philosophy, or any of the items contained in these pages over the phone, or over a cup of coffee, so if the thought strikes you, don't hesitate to give me a call.

Update on Income Trusts

Well, what a way to start November. The following excerpts are taken from a ScotiaMcLeod Portfolio Advisory Group piece entitled "Federal Government to Implement New Tax Fairness Plan."

On October 31, 2006, Federal Finance Minister Jim Flaherty announced a new Tax Fairness Plan, designed to restore balance and fairness to the federal tax system by creating a level playing field between Income Trusts and Corporations. In brief, the federal government has announced changes to the tax system that proposes to tax income trusts in the same manner as corporations. Trusts will be taxed at corporate tax rates before distributions; distributions will subsequently be treated as dividends. These changes take effect in the 2011 tax year for trusts that are currently publicly

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traded. It is expected therefore that the existing trust market will likely shrink considerably by 2011. New trusts that begin trading after October 2006 are impacted immediately, and as such there will likely be no further conversions, including BCE and TELUS. Real Estate Investment Trusts (REITS) appear to be mostly exempt, and will not be impacted.

According to the announcement from the Minister of Finance, despite these previous changes to the tax regime, a tax on distributions is being implemented due to the following:

- A significant increase in the number and size of businesses and corporations converting to an Income Trust structure. In the federal government's view, this is a result of the tax advantages still enjoyed by non-resident and tax-exempt investors.
- The ongoing depletion of provincial tax revenues (due to the inability of the provinces to tax distributions to non-residents).
- The shift in tax revenues between provinces (which in turn has caused concerns over lost revenue for the provincial governments).
- Similar actions have taken previously by both the U.S. and Australian governments to address corporate tax avoidance.

Therefore, the federal government is now implementing what they consider to be a more appropriate tax regime for Income Trusts (referred to as Flow Through Entities (FTEs)). Essentially, this tax treatment will be similar to that of corporations. Further, unit holders will now be treated essentially like shareholders.

What are the implications for the Income Trust Market?

- There is no immediate impact on taxable investors from an after-tax distribution standpoint, all

else held equal. Distributions to investors will eventually be lowered due to the introduction of tax at the FTE level, but these distributions will then be treated more advantageously as dividends, resulting in no net after-tax impact. In fact, the planned further reduction in corporate taxes beginning in 2011 is a net benefit to taxable investors.

- The implementation of a tax on distributions will effectively reduce the attractiveness to non-resident and tax-exempt accounts.
- These measures will be effective in rebalancing the income tax treatment of corporations and FTEs, and as a result, the legal form a business takes will going forward depend less on tax legislation.
- These measures will likely result in little to no new issues or conversions going forward, outside of the REIT sector.
- There remains a four-year grandfathering period-FTEs currently publicly traded are not subject to these changes until the 2011 tax year. Therefore, no change in current structures is expected in the near term, as FTEs will remain an attractive tax structure over that period. Beginning in 2011, however, we expect many FTEs will re-visit their structure, to determine what will be in the best interest of unit-holders.
- Beginning in 2011, it will become disadvantageous to hold FTEs in non-taxable accounts (i.e. RRSPs), due to the inability to realize the beneficial tax treatment of dividend income. In 2011, it will be much more advantageous to hold FTEs in taxable accounts, similar to high yielding common equity and preferred shares.

So there you have it. Like it or not, this new change proposed by the government appears here to stay. Time will tell, but it is worth remembering a couple of points:

- Income Trusts currently comprise less than 10% of the market capitalization of the S&P/TSX Composite Index.
- Income Trusts are in general more properly classified as high yield, mid-to-small capitalization equity.

With that in mind, this should be a reminder of the importance of having a well-diversified portfolio, across different asset classes, sectors and styles.

If you are uncomfortable with your current asset allocation/investment structure, perhaps now is the time to re-visit it and ensure that it is representative of your tolerance for risk and volatility. In addition, it will enable you to ensure your portfolio is aligned with your goals.

If you have any questions or comments, don't hesitate to give me a shout.

Jeff

CONCLUSION