

Glossary

Here are definitions of some of the more important terms used throughout this guide. For more definitions, please refer to the *Smart tools* CD-ROM.

Balanced fund. These funds are a mix of all types of investments. They can be made up of a combination of equities, bonds, mortgages, and money investments. The mix of these different investments is determined by experts that research and review where the markets are going so that the best investments are purchased.

Bond. A bond is a debt instrument that promises to pay back the principal amount of the bond plus a pre-determined interest rate. Corporations or governments issue bonds to get money they need today, knowing they'll have to pay the money back with interest. In effect, you lend money to the seller by buying a bond. The bond represents an agreement to repay the principal plus interest.

Canada Revenue Agency (CRA). The government branch responsible for promoting and enforcing compliance with Canada's tax, trade and border legislation and regulations. For more information, visit their website at www.cra-arc.gc.ca

Canada/Quebec Pension Plan (CPP/QPP). A government-sponsored plan that provides retirement benefits for working Canadians, whether they're employees or self-employed. The amount of the benefit depends on how long you have been contributing, your income level and when you start to take the benefits. The maximum CPP/QPP will pay is 25 per cent of your pre-retirement income subject to an overall maximum. Special benefits may be available if you're disabled, a surviving spouse or a dependent child.

Contribution limit. This is the total amount you can contribute to a registered plan for which you can receive a tax deduction. For RRSPs, the CRA calculates this amount for you and advises you of your contribution limit with the Notice of Assessment you receive after your tax return is processed each year.

Deferred Profit Sharing Plan (DPSP). These plans are set up by employers as a way to share profits with their employees. Contributions depend upon the profits of the company. Employee contributions aren't allowed. The plan is registered with CRA and contributions are tax deductible within certain limits, as defined by the Income Tax Act.

Defined Benefit Plan. A registered pension plan that provides an employee a specific benefit upon retirement usually based on earnings and years of service. Typically, a member's benefit calculation involves a combination of number of years' membership, salary and actual retirement date. With this kind of plan, members can determine exactly how much income they'll receive during retirement. (See Money Purchase Pension Plan.)

Defined Contribution Plan. (See Money Purchase Pension Plan.)

Diversification. An investment technique intended to minimize risk by placing money in a number of different securities. In a diversified portfolio, a decline in the value of one stock, for example, should not dramatically affect the overall value of the holdings.

Dividend. A per-share payment designated by a company's board of directors to be distributed among shareholders. For preferred shares, it's generally a fixed amount. For common shares, the amount is discretionary.

Dollar cost averaging. Investment of a fixed amount of money at regular intervals, usually each month, to even out market fluctuations.

Employee Profit Sharing Plan (EPSP). A non-registered, non-tax-sheltered plan that's governed by certain provisions of federal tax legislation. The plan may allow for employer-only or employer and employee contributions. Employer contributions are tied to company profits and may be either a fixed percentage of salary or a variable amount. Employee contributions aren't tax deductible, and all earnings within the plan, including company contributions, are taxable to the employee.

Employee Incentive Plans. Many companies choose to reward performance or encourage long-term commitment through share-based compensation. Generally, these types of compensation are based on set criteria and objectives and may have time restrictions. There are a wide range of incentive plans. Stock option plans, restricted share unit plans, long-term incentive plans and employee benefit plans are a few of the types of incentive plans available.

Equities. The common or preferred shares of a corporation, which represent the investor's ownership in the corporation. Also called stocks.

Equity fund. Equity funds are made up of a number of individual securities (mainly stocks). A company raises money by selling part ownership (shares/stocks) of the company. The stock is then listed on a stock exchange to be traded. After the initial public offering (IPO), stocks are traded at prices determined in the market by the interaction of buyers and sellers. The price of a stock isn't guaranteed and can fluctuate from day to day.

Group Retirement Savings Plan (Group RRSP). A collection of individual RRSPs sponsored by an employer or association. Plan members contribute a portion of earned income (up to a maximum limit) and claim the contribution as a tax deduction. Because the contributions are made through payroll deduction, the tax savings can be immediate. Members choose their own investment options from the set of investments offered by the plan, and all the earnings within their RRSP remain tax-deferred while the money's in the plan. The amount of retirement income depends on a number of factors including the final accumulation of money within the plan and the type of retirement income chosen.

Guaranteed interest account (GIA). An investment offered by life insurance companies that guarantees the principal amount and pays a predetermined rate of interest for a specified term, from one to 10 years. Each deposit carries its own deposit date, interest rate and maturity date.

Income fund. An investment fund that invests primarily in fixed income securities such as bonds, mortgages and preferred shares. The objective is to produce income for investors while preserving capital.

Index fund. An investment fund that matches its portfolio to a specific financial market index, such as the S&P,

with the objective of duplicating the general performance of that index.

Interest. The amount of money you earn from a borrower in exchange for a specified amount of money.

Investment fund. An investment entity that pools unitholder funds and invests in various securities. Mutual funds and segregated funds are two types of investment funds.

Investment manager. Also known as money manager or portfolio advisor, the organization responsible for the investment of the fund's portfolio.

Investment style. The manner in which an investment manager selects and manages investments.

Management fee. The money paid to the investment manager for supervising a portfolio and to the insurance company for administering its operations. This fee is a component of the Management Expense Ratio.

Marginal tax rate. The tax rate that you pay on your next dollar of income. (Canada has a progressive or graduated tax system, which applies higher tax rates as income increases.)

Market timing. An attempt to move in and out of the stock market, buying low and selling high based on the investors' predicted move in the market.

Money market fund. A money market fund invests in short-term interest-bearing investments – investments that mature in less than one year. A typical investment in the money market fund would be Government of Canada treasury bills. In order to achieve good returns, the types and terms of the investments chosen for the money market fund are based on market outlook. Investors often choose to “park” their money in a money market fund while they're deciding where they want to invest for the long-term.

Money Purchase Pension Plan (MPPP). A registered pension plan that doesn't promise an employee a specified benefit upon retirement. Benefits depend on the performance of investments made with contributions to the plan. Contributions are credited to an individual account for each member and invested, usually on the direction of the member, in a set of investment options chosen by the plan sponsor. When the member retires, the accumulated funds are used to purchase retirement income (Life Income Fund, Locked-in Retirement Account, annuity). The amount of the income depends on a number of factors, including the amount of money that's finally accumulated in the member's account, so the actual income can only be estimated prior to retirement. (Compare Defined Benefit Pension Plan.)

Mutual fund. A pool of assets that gives individual investors access to a well diversified portfolio of equities, bonds, and other securities. Each unitholder holds units of the fund representing their proportionate share and participates in the gain or loss of the fund. Units can usually be redeemed as needed. The fund's net asset value (NAV) is typically determined each day and published in the newspaper. Each mutual fund portfolio is invested to match the objective stated in the prospectus.

Non-registered savings plan (NRSP). Savings in a non-registered plan aren't tax sheltered and are subject to annual taxation. Although fairly unrestricted by government regulations, there may be employer-imposed limits, or insurance or securities law regulations.

Old Age Security (OAS). A government income benefit that's based on age and how long you have lived in Canada. The program has three parts:

- The OAS pension
- The Guaranteed Income Supplement (GIS)
- The Spouse's Allowance (SA)

To receive the full OAS benefit you must have lived in Canada for 10 years prior to your application. However, in

1989 the government introduced a “clawback,” which means that if your income exceeds a certain limit each year, your OAS pension will be reduced accordingly. The GIS is a monthly benefit paid to people who receive OAS, but have little or no other income. The SA is paid to the spouse of someone receiving OAS who is between ages 60 and 64 and whose family income doesn't exceed certain limits.

Pension adjustment (PA). An amount that reduces the allowable contribution limit to an RRSP based on the benefits earned from the employee's pension plan or deferred profit sharing plan. This amount is calculated by your employer and is on your T4 each year.

Pension plan. A formal arrangement through which the employer, and in most cases the employee, contribute to a fund to provide the employee with an income after retirement. (See Defined Benefit Pension Plan and Registered Pension Plan.)

Registered Pension Plan (RPP). A registered pension plan is an arrangement set up by an employer with the purpose of providing retirement income to employees. The plan's registered with CRA in order to provide tax advantages. Contributions you make to an RPP are tax deductible within certain limits. Investment income isn't taxed until it's paid out of the plan.

Registered Retirement Savings Plan (RRSP). A registered and tax-deferred retirement plan that allows individuals to set aside tax deductible sums of money, within limits, up to the end of the year in which they turn 69 (or such age tax legislation in effect may provide).

Risk. The possibility of loss and the uncertainty of future returns. Specific risks are defined below.

Capital risk – The risk of losing your capital – or the money you've already saved. If you save in a bank account, you can be sure you'll always get back at least the amount of your original capital. With stocks, there's no such guarantee.

Credit risk – This is the risk that a company or individual will be unable to pay the interest or principal on a bond you hold.

Currency risk – If you invest in foreign assets, currency exchange will be a factor when it comes time to buy or sell. That's because currencies, like the Canadian dollar, go up and down.

Geographic risk – The economy of a particular country or region can slow down, adversely affecting the value of stocks trading in that country.

Inflation risk – The risk that the buying power of your money will shrink over time unless the interest you receive keeps pace with (or, ideally, outpaces) inflation.

Income risk – If you invest to receive a fixed income, you may be locked in to a certain interest rate. If interest rates go up, you run the risk of losing out on the income that you would have received from the new, higher rate.

Interest rate risk – There's always a risk that interest rates will rise. Rising interest rates undermine the value of bonds and can also have a negative impact on stocks.

Liquidity risk – Liquidity refers to your ability to convert your investments to cash.

Market risk – The volatility of stock market prices due to company performance and political and economic conditions.

Political risk – Investing in a foreign country can be affected negatively by political instability, which can take the form of a coup or a sudden change in government policies.

Segregated fund. A segregated fund is an investment option available only through an insurance contract. It allows you to combine your money with many other clients. Each individual client is allocated a number of “units” of the segregated fund, which are then used to determine the value of their contract. A professional investment manager then takes the pool of money to the marketplace and invests in a variety of investments consistent with the fund's objective. The unit value of the segregated fund fluctuates with the performance of the underlying investments held by the fund. For

example, if the segregated fund invests in shares of companies and the prices of those shares start to move upward, the unit value of the segregated fund will likely increase.

Spousal Retirement Savings Plan (Spousal RRSP). An RRSP registered in the name of your spouse (as defined by the Income Tax Act). You deduct the annual contribution from earned income (the maximum is your contribution limit minus your personal RRSP contributions) and your spouse receives the eventual income generated. The Income Tax Act's definition of “spouse” includes common-law spouses in certain circumstances.

Stock. The common or preferred shares of a corporation which represent the investor's ownership in the corporation. Also called equities.

Today's dollars. The value of money today. **Future dollars** is the value of money in the future, factoring in the eroding effect of the inflation rate.

Time horizon. The period of time between now and when you will need the investment for other purposes (e.g., to provide a retirement income or to purchase an annuity).