Mark Noble
Welcome to the latest episode of Generation ETFs, and today we are in studio with the Loonie Doctor, who is one of the most widely followed personal financial bloggers in Canada. Who focuses on personal finance for high-income earners, in particular, specialty on doctors. The Loonie Doctor is an actual Ontario-based physician. He'll remain anonymous here. We want him to use his moniker, and his name is derived from our currency. So we're not here to talk about alternative forms of healthcare and medicine. We're actually here to have some very sound advice on financial planning for high-income earners.

Mark Noble
So I'm just going to refer to you as doctor. Doctor, thank you for being here today with us. We're really excited to have a conversation here about personal finance.

Loonie Doctor
Great. My pleasure and thanks for having me.

Mark Noble
I hope you can tell us a little bit about yourself, and how it is you became to be managing your own financial affairs? Because, typically, we see a lot of high-income-earning professionals using advisors. They choose to go advice, which is great. We rarely see them taking control of their own financial affairs. And I think what's really interesting when I read your blog is that you are someone who is in control of your own financial affairs while also being extraordinarily busy as a physician. So I'm wondering if we get a sense of how this came out to be and how it is that you sort of took control of your own financial destiny.

Loonie Doctor
Sure. So I mean, I've ended up here after a road of trying a bunch of different things and as you mentioned, most of us do use advisors and there are good value for some advisors for some things that they do for us. But, over time, I've found that for me the value proposition is better if I just take control myself. And I think even those that do use advisors, it's important that they understand some basics of what they're doing. Just as if we had a patient, we want an educated patient that makes a much better patient than an uneducated patient.

Loonie Doctor
So we should really educate ourselves about our finances to help manage that aspect of our practice. And that's really important because if we have our financial houses in order, I think it actually makes us better doctors. And it makes us better doctors because we are able to have more freedom to move around within what we do within medicine and practice good medicine with the finances actually ironically enough being a secondary consideration and not really getting in the way, but actually enabling you to do things. So, I think it's actually very important for us as practitioners to have that in order. And in terms of how I became interested in it well, I mean, I didn't grow up in a very wealthy family. We were an average family, but my parents worked hard and spent much less than they made and saved and invested over the years. And they taught me to do that as well.

Loonie Doctor
And when I came into medicine that was always part of what I needed to do and I started making money was to plan for my retirement. And to look after myself, my family throughout life. So finances was always important. So I did get a good basic financial education from my family, and then over the years I developed that for others as I needed to. So I started off with advisors like most people do. And then I thought, okay, well this common thing that physicians can fall into. And just like any high-income professional, when I say physicians, I'm really talking about all high-income professionals because we actually share a lot of things in common, whether it's medicine or running a small business or any of these different things that people can do.

Mark Noble
A lot of your advice would apply to lawyers, accountants, dentists, or even entrepreneurs. Someone who's got a high degree of cashflow from an income perspective.

Loonie Doctor
Yeah, that's right. That's where my focus is. I mean, I still do a lot of writing about basic personal finance because even though physicians and other high-income earners earn more money, we still face mostly the same issues that everybody else does. There are some things that we face that are a little bit different that we need to pay attention to as well though. So my medical practice, I've practiced medicine and part of my practice has always been teaching and over the years I've done a lot of teaching. And then I've been in practice about 15 years and a lot of the things that I've been teaching about have kind of matured,a lot of the other projects I was working on and building the practice had matured. So I decided to switch my focus to trying to teach about finance to physicians because I found that to be a big void that needed to be filled.

Mark Noble
And what sparked your interest to write The Loonie Doctor blog? And if you don't follow this, I highly recommend even if you're not a high-income earner, it's a really fun blog. Lots of cartoons and really interesting diagrams. You have a mechanical engineering kind of approach to investment management which I find fascinating. So it's thelooniedoctor.ca that you can go onto and I highly recommend you bookmark this if you're a personal finance interest or personal finance nerd like myself. But what sparked your interest to take it to that next level? Where you actually put your name out there and start writing about this for other people?

Loonie Doctor
Well, I was on a vacation sitting outside my motor home thinking about what to do next. And the reason why I was thinking that because, as I kind of alluded to, I spent the first part of my career trying to build up our department, which became a department and trying to build up my practice and build up some different course type material. But that had already come into fruition and at a point where it's matured. There's other people that could probably take it to the next level and I needed to try to find something else to kind of occupy my time.

Loonie Doctor
So medical practices is one part of what I do. But one of the great things about medicine and one of the things that are important are actually to do a variety of things so you can maintain your interest that can change over time. So this is just really an area I felt that I needed to do something different with. And this was an area where I thought, no one's really writing about it in Canada and it's something that I think is actually very important. And I was sitting there on this vacation thinking I was fortunate to be able to do this. And the reason why I can do this is because I've actually managed my finances and put myself into a good position where I can do these things. And I have the choice to sit here and think about what do I want to do next in my career.

Loonie Doctor
Where there's a lot of people I think feel trapped because they haven't managed their finances well. And by the time they realize that's a problem, well it's because they're actually looking for a way out or looking to do something else so the problem is staring them in the face. So I was fortunate to be in a position that I was in. I thought that, well if I can do something, try and help others be in that position, then that would actually probably help my colleagues as a whole improve the way the we do things.

Mark Noble
One of the things that impresses me about your blogging approach, though, is you get really technical and really granular. Which I deal with professional money managers all day, I deal with advisors, and they don't ask me the kind of questions that you may ask or get into some of the details you may get into on some of the personal finance aspects. How do you come up with this information? This is, generally speaking a lot of the stuff you're doing is something I'd be more expecting someone with a CA or a CFA to be putting out there. I'm curious where you get your information flow to look at some of these investment structures at the depth you do.

Loonie Doctor
Yeah, and well, that's another reason why I started to write this blog. There's a lot of blogs out there and internet material that is very basic. It superficially goes over what the big issues are. And for the average person that's probably actually the best approach to take. The jump between the savings that you make from doing the nice passive index approach that is very cost-effective, between doing that and paying a manager to manage your money or using mutual funds with high fees, that's the big jump. So if you can get people to take that big jump, that's probably the most important thing. And that comes down to simplicity. So I think for most people, that simple approach is actually probably the best one.

Loonie Doctor
I think one of the things that doctors face differently is that we have a tighter timeframe in which to do our investing at higher levels, because we start our careers rather late compared to the average person. So we need to make up for lost time. And the way that our tax system works... taxes actually start to become an important factor. If you make the same income over your lifespan, but you condense it and have high-income years and low income years, you're going to pay much more tax than someone who does it gradually over a period of time. So for us actually taxes becomes actually quite important.

Loonie Doctor
And understanding how things work and all of these details becomes important. And the thing about... if you look at that superficially, well it doesn't really work because there's actually a lot of moving parts there and it is individual as to how to approach this. And I couldn't really find anything written anywhere about how to do that. And one of the things that we do have is those that do use advisors, which like I say I have used advisors, is that your advisors they manage your investment piece. Your accountant takes all the stuff you give them and makes the best of it. But to mesh those two together is actually something that's different. And there's very few people that mesh it together.

Mark Noble
Right.

Loonie Doctor
The finance people will look at the finance piece, the tax people look at the tax piece. But you need to be able to actually put them together to make them work together effectively. And that requires some understanding of some of the details of how things work. And I couldn't find that, so I figured I should learn about it. And in learning about it, I always write things down and make pictures. So I figured I might as well put this as part of what I'm writing about.

Mark Noble
That's excellent. And what are some of the challenges that a high-income earners, it could be particular to doctors, but I think it's good as a catch-all, all high-income earners. What do some of them face? In fact, maybe I'll rephrase. If I could talk to you 10 years ago, what would you tell yourself in terms of things that you didn't anticipate in areas of focus that high-income professionals should be looking at?

Loonie Doctor
Well, I think we get set up to have a number of problems and some of that, most of the problems that we face are the same problems that everybody else faces. Some of the issues are that our spending and our income. So when we do start to earn a higher income, it's very easy to see that. And think, okay well, I can spend on all these things that I've delayed gratification to get here for. So there's that pressure. I mean, you go through a long training period before you start to make larger amounts of money.

Loonie Doctor
So there's some pent up demand that's there. So it's easy.... And feeding some of that pent-up demand is important, but also not overdoing it and feeding it with things that are going to give you ongoing large costs. So people can kind of shoot themselves in the foot if they're not prepared to handle the increase in the income. So that's one of the things that we can slip into. The other things that we slip into is, with that it's easy to mask our problems 'til it's later on. And we have a lot of other things that take up our time. So we spend our time doing all of those other things and don't really pay attention to it until it becomes an issue later. And it's quite easy to have that happen. And that piece about time, actually, becomes very important for us because as we start later, we have a more condensed period of time in which we need to save for our futures.

Loonie Doctor
So the beauty of compounding returns over time is the time part of it. And if we start later, then we have less time to do that. And so we have to make sure that we do that more effectively. So, we have to be careful to save more than we would think otherwise because we have that shorter time window to build things up over time.

Mark Noble
Although as a doctor, you do probably have a little bit more forgiveness in terms of the length of your career, right?

Loonie Doctor
Yeah. I mean, you do. Hopefully. I mean, but the thing is you don't know what's going to happen, right? So you may plan to work to 'til you're 72 but you may have health issues in your 50s or 60s or your family member may…all of these things can crop up. And that's part of what's hit home to me because I look after critically ill people who are very sick. And as I start to look after more and more people my own age. And these are people, they did nothing wrong. Just bad luck, and bad stuff happens to them. So you, you don't know what that future holds for you. And you just got to make sure that everything's covered for it.

Loonie Doctor
So you may plan that work for a long career, but you don't know. And the other thing is that you may plan to do what you're doing now for 20 years, but you may realize after 10 years that you don't like parts of it or some parts of it are getting boring and you want to refocus on your career on different parts of what you're doing. And having that kind of financial freedom from getting your finances in order gives you the ability to actually shift around what you do. I've changed my, the way I practice several times over the last 15 years and I'll continue to change it as some area gets stale or I feel that there's not much more I can contribute to that area, well, there's this other area that I can contribute. And I don't need to worry about the financial aspect of that as much because I'm well established, I can do what I think is the best thing to do and have that be the priority.

Mark Noble
How do you structure your... specifically because we're talking about investment planning. How do you structure your asset allocation, though? How do you come about building your portfolio?

Loonie Doctor
Right. So after I started out with mutual funds, like a lot of people, and then I tried to do, pick stocks for a period of time, which I was terrible at. And I think the only free lunch you get is diversifications. That's why I do use ETFs to do that. It's nice and easy, because for me it's a balance between how much effort I'm going to put in, in terms of time versus the return that I'm going to get. So I want something that's low effort, going to cover all my bases and be simple.

Loonie Doctor
And so, ETFs are probably the way that I would do that because I get multiple companies in one fund and it's easy and it's pretty cost-effective. So that's in terms of what I would use. Then the next question is, okay, well how much do you use? And that's going to get in your asset allocation. So you really kind of have to look at your risk capacity and your risk tolerance. And I separate the two: risk capacity is my ability to absorb losses and not freak out about it from an actual cash flow standpoint.

Loonie Doctor
So if you are well established, and you have good cash flow, and you have good income and you have a long horizon ahead of you that you can continue to earn income, then you have more risk capacity than someone who's basically, income and expenses are very close to each other and they don't have a lot of a wiggle room if something goes wrong. So that'd be the kind of capacity component to it. So you want to keep that in mind. And then also your risk tolerance, which is more your behavioural ability to watch things go up and down and ignore it. So you need to kind of balance those together so that you're not going to exceed either of those because then that's when you start to make behavioural mistakes. And they're related to each other. If you have a little wiggle room and you see things drop a lot, then that's much scarier than if you have a lot of wiggle room. So those are going to be different for everybody.

Loonie Doctor
So the first part would be to assess that for yourself. So for myself, I've got good risk capacity, I've got lots of wiggle room and then my risk tolerance from an emotional standpoint, I've been kind of whiffle-waffling back and forth and trying to figure it out. So I was a hundred percent equity for many, many years. And then as I kind of got over the last couple of years, I was thinking, okay, well, what if I do want to retire a bit earlier, if I want to scale back. Should I be cutting back that a little bit? Or what if I've already won the game, should I keep... why risk money still when I don't need to risk money, I could be safe? And then the [inaudible] is that okay, well, if you're doing well and you're good at playing the game, why don't you make, continue to do that?

Loonie Doctor
And then when you have excess money you can donate it or do other things with it and be a kind of a good steward of the money to grow it to its maximum potential so that you can then do the most with it. So those have been the factors that have been kind of bouncing around in my mind. And I did go to about a 20% bond allocation for a while there. And then there was a market drop, December a couple of years ago. And I found myself just sitting there wanting to sell all the bonds and go back to 100% equity because I really... this is a drop and it didn't bother me that it dropped. I just wanted to actually be more aggressive. So I did move back to being 100% equity at that point. And I've stuck there. And the reason why I stuck there is because, when I think of asset allocation, I think not only of the stocks versus bonds versus all the different ways you can divide it up into a thousand pieces. I think of it as in terms of my total overall human capital.

Loonie Doctor
So, I have a good ability to work and make income. So that's fixed income essentially. And I also have that insured with disability insurance. So I really do have a big fixed income allocation just by virtue of my age and my profession. So I'm able to have more equity in my investment side because I have that as a bit of a safety net. And then I do have a little bit of whole life insurance just for estate planning purposes, which is another basically type of... It's almost like a fixed income type of equivalence. So I've got that. And then I have money that's tied up in my house as equity in my home. So that is another thing that moves differently from the way that stock markets move. So I tried to actually think of all of my different wealth that I've got, including my human capital and, and put that all together. So I'm pretty aggressive with my investment allocation because of that.

Mark Noble
And I think that's something that a lot of professionals you represent don't really think about is that, as a high-income earner you have this certainty of income, but then there's not a big defined benefit pension plan for you at the end.

Loonie Doctor
No.

Mark Noble
So your growth cycle of your portfolio is actually shorter than somebody who actually has a fixed pension at the end. The way you manage your money is very different than how a professor with a pension or a teacher would manage their money based on the certainty of income in retirement.

Loonie Doctor
That's right. Yeah, exactly.

Mark Noble
It's fascinating. And you mentioned you're in favour of using ETFs. Is that just mainly just for the diversification and low cost? Is that what drove you towards this?

Loonie Doctor
Yeah, there's that and then there's that it's easy. So if I'm going to... And again I think a lot of successful investing really comes down to behaviour. So if you can make something simple and easy, you're much more likely to stick to it and follow through on it than if it's complicated and difficult to do. That's why I'm kind of in the middle of... There's people who would use asset allocation ETFs who would think that what I do is very complicated.

Mark Noble
Right.

Loonie Doctor
But for me, if I manage, you know, five or six ETFs, that to me is no different than managing one. It's a few more minutes of my time and a few bucks.

Mark Noble
And these are primarily indexed strategies you're buying into the idea of being in the market.

Loonie Doctor
Yeah, that's right. So I just try to match that.

Mark Noble
And so let's get more into brass tacks here in terms of specifics for I think the advice, everything that you've mentioned is applies to everybody. But in terms of specifics for high-income earners, the one thing we always talk about is incorporating, right? It seems to be that, especially if you're a doctor or a lawyer or accountant, if you go to an advisor and you're not incorporated, I'm willing to bet the first thing they bring up is that you should incorporate. Do you think that's pretty much a necessary move now given the tax advantages of incorporating versus not incorporating as a professional?

Loonie Doctor
Yeah. Well, I think that ties in to actually the next part of investing planning, which is really kind of your asset location. So we talked about what I use, I use ETFs. Why do I use them? Because they're simple and easy. But the other question you have is where do you put them? So for most physicians, actually, I think just like everybody else, the most tax-efficient vehicles that we have are our tax free savings account and our RRSPs. They're very tax efficient. Now the problem that we have as high income earners is that we have to condense our earning to a smaller period of time. And TFSAs and RRSPs have limited space. So they're not going to be able to put as much in there to come close to the income that you're earning during your working years to kind of provide something that's a good enough match when you're retiring.

Loonie Doctor
And the other piece of that is for things like your RRSP and TFSA. The room in there grows over time. The TFSA grows based on your age, which is no problem, but RRSP only grows as you make more income. And since we make more income late in our careers, we don't really start to build a lot of RRSP room until later on in our lives. So the problem we have is we tend to overflow that. And yet, but we still need to actually save more for our retirement and we need somewhere to put it. Well you can put that in a regular taxable account like everybody else does. Or you can put that into a corporate account. And the big advantage of a corporate account is that it gives you some amount of tax deferral. So an RRSP would give you 100% tax deferral.

Loonie Doctor
You get the money from the tax back right away and you're investing 100% with pre-tax dollars. The corporation, if you're eligible for the small business deduction, which most people are, then the tax rate of that range is between kind of 11 and 15% depending where you are in the country. But in Ontario it's 12 and a half percent. So you're investing with, you know, 80 something percent pre-tax dollars. So it gives you more capital to grow over time. Now the other side of that though is it doesn't grow as efficiently as it would in something like an RRSP. So corporations were set up to try to help people with their cash flow. So when I think about a corporation, there's two aspects. There's the active income, which is the stuff you earn from working basically. And there's the passive income, which is what you get from investing.

Loonie Doctor
Active income, it's very useful to smooth your cash flow. So since an employee knows their paycheck is coming, it's pretty regular. If you're a professional, that includes physicians, I mean, there are months where you make a lot of money and there's months where you make no money. There's years where you make a lot of money. There may be a year where you take off parental leave and you have no income. So you want to try to smooth your income between your high-earning years and your lower-earning years because of that fluctuation of costs, you don't have that predictability. So a corporation allows you to do that and take some of the extra money from your higher-income years and preserve that to help pay for your lower income years and smooth that out.

Loonie Doctor
So that's on the active income side and corporations are excellent for that. That's really what they're designed for. The other side part of it is the passive income piece and there's a number of rules, incorporation taxation that actually discouraged passive investing. So when you invest passively, the income is taxed upfront, basically the highest marginal rate and you only get some of that money back usually and you get that back when you flow that money out of the corporation into your personal hands, at which point it gets taxed the remainder of the amount essentially. So corporations work well if you're saving a lot of money in them and you're able to retain money in there, but you're also flowing enough money out that you're able to have the taxes refunded to your corporation. So there's a balance that's there.

Mark Noble
So you try to just have the passive income portfolio and you don't draw down on it. It's basically being taxed at 50%.

Loonie Doctor
Yeah, I mean it would be, just to invest in it as is not that tax-efficient. The advantage is having some more capital, but the drag on the growth over time wouldn't be great. But if you're flowing money out of your corporation, especially Canadian dividends, those are very efficient. Foreign and interest is much less efficient. And there's also the new tax rules that once you start to get a certain amount of passive income, if you are still earning active income on top of that, then it starts to increase the tax rate on the active income as well. So that becomes a pretty big tax bump.

Mark Noble
Right.

Loonie Doctor
Yeah. So that's where, using all of the tools at your disposal, like your RRSP, TFSA, corporation to kind of spread out your risk from a legislative standpoint is useful. And they all have their own pros and cons so you can make them mesh together synergistically.

Mark Noble
So what sort of investment strategies or funds do you use, then, in the corporation? I'm assuming you want to use things that pay the least amount of distributions possible.

Loonie Doctor
Yeah, well, it depends. So I tried to direct my Canadian... I think there's a difference for Canadian dividends, Canadian dividends are very efficient in the corporation. So I tend to use regular... my Canadian holdings that pay rate eligible Canadian dividends, I hold those in my corporation preferentially. And that allows me to save room in my RRSP and my TFSA for some of that stuff that's less tax-efficient. So interest and forward dividends in a corporation are pretty tax inefficient. So for doing that, I'll try to either pick something that pays a low dividend or no dividend to try to keep that down. Although over the years I've honestly built up enough room in my RRSP, TFSA that my corporation mostly has my U.S. investments and my Canadian investments, and my sort of foreign developed markets and other sort of higher distribution type of investments are all my tax-sheltered accounts.

Mark Noble
Got it. That makes a lot of sense. And then you've written extensively about our Total Return Index ETFs. How do you specifically use these ETFs? Do you use them within the corporation then... Because these particular ETFs themselves are not anticipated to pay a distribution. So you can get something like S&P 500 exposure but it doesn't pay out a dividend. And I know you've written extensively on your blog about using some of these in the corporation.

Loonie Doctor
Well, there's two ways that I use it on the corporate side, I would use it, or consider using it if I have something that's a high distribution. So the bond one, HBB, is really good. I haven't had to yet, but if I had to hold bonds on my corporation, that would probably be the way that I would do it because I can delay paying the tax on it. So it's tax deferral and it's tax reduction because it's capital gains instead of interest and interest is very inefficiently taxed. And then foreign developed markets is another area that tends to pay very high dividends and they get taxed very heavily. So if I had to hold it in my corporation then I would. We have used the developed market one, HXDM, in my wife's personal taxable account when she holds things there because she actually, she earns a pretty good income as well. And she has her personal accounts. So we've used that there.

Loonie Doctor
I've also used some of them in my registered accounts. So I think the advantage of the total return structure with the swap contracts is cost-efficient for Canadian type of holdings. So the REITs one has a lower MER than the other Canadian REITs one, just because of the efficiency of the structure. So actually I use that in my TFSA and our RESP because it's just simply, it's a lower cost. And my belief is that you can't control what the market is going to return, but you can try to control the best you can for your fees and your taxes. So if I have a way that I can get the same thing for a lower fee than I'll do that. And if I have the way that I can get exposure to the same investments but pay less tax or at least defer that tax and let it grow more over time, then I'll try to do that.

Mark Noble
Okay. That makes a lot of sense. And you're sort of looking at each, the TFSA and the registered accounts and the corporation, is sort of one holistic portfolio.

Loonie Doctor
Yeah. When I consider it again, just like when I get to think of my asset allocation, I think of my portfolio, I think of it all together as one big piece and it seems complicated. I've actually made online calculators to try to make this easier so you can put in your allocation and how much money you've got and then it'll help to try to make it into an efficient way across a TFSA,RRSP, personal account, corporate account and try to make that a bit more simple from a math standpoint.

Mark Noble
But intuitively it makes sense, right? Because the biggest cost center you're going to have is the taxes and fees. And so you've mitigated that drag on your performance.

Loonie Doctor
I think the one... what I'm talking about as asset location, I think there is some controversy about that, there are people that would say don't bother with asset location. And I don't think that's actually a wrong position to take. I think for the average person paying the average amount of taxes, it's probably not worth it and there are risks that you run with it too, like tax laws can change in the future. We've already seen corporate tax laws change recently and the other risk is if you have a relatively static portfolio where you have to rebalance and you have to sell stuff to rebalance, then you're going to trigger taxes when you do that. Then if you're trying to locate things optimally all the time, you may start to generate that problem.

Loonie Doctor
That's not a problem for most of us during our accumulating years though because we're actually, most of us tend to be putting more money in each year than what we're making on our investments. So rebalancing just means buying whatever's lagging the most, to rebalancce rather than selling things.

Mark Noble
Perfect. Well, this has been a tremendous conversation and I've really enjoyed this kind of advice and it's a little bit different for us because we're usually focusing on more hard investment themes, but I really liked the approach that we've taken today. And the approach that you're taking and really looking at holistic financial planning in the client's side of things. So doctor, thank you very much for joining us today. And again, anyone who's interested in learning more about other work, the Loonie Doctor does, it's thelooniedoctor.ca. Highly recommend you take a visit that site when you get some time. That's it for our latest episode of Generation ETFs. Thanks again, doctor.

Loonie Doctor
Thanks.

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