EDGEPOINT®

CLARIFYING BOOK VALUE

Who would have thought "book value" was so confusing? Clarifying a common issue on your account statements.

When investors view their account statement, a common misconception is to compare the difference between the "book value" (also known as adjusted cost base, or "ACB") of their portfolio vs. the market value, in order to determine how much money was made or lost in their account over a given period. It sounds pretty straightforward, right? At least that's what Accounting 101 taught us. However, comparing these values usually leads to inaccurate conclusions regarding actual account performance.

The book value includes all your contributions to the fund. However, if you elect to receive the fund distributions in units, your book value is adjusted by the automatic reinvestment of distributions. In simple terms, when a fund pays a distribution you get taxed on it, but when the distribution is in fund units, the book value increases at the same time by the amount of the distribution to avoid double taxation. This information is reported on your T3 slip (Relevé 16 for Quebec residents).

Therefore, your book value could increase even if you don't contribute more money to your portfolio, making it a misleading metric to use to evaluate how your portfolio has done. Book value will also be impacted by your withdrawals.

Why can't we just forget about book value?
Book value is actually used for non-registered plans when calculating capital gains and losses for income tax purposes. Any capital gains or losses triggered by a redemption or a switch, are reported on a T5008 tax slip (Relevé 18 for Quebec residents).

How can I tell how much I've made if I can't use book value?
You should look for the "amount invested" in your statements and compare it to the "market value" to calculate how much you've made or lost on a given investment. "Amount invested" excludes any reinvested distributions, but will include all your contributions and withdrawals. You can find this information on most dealer account statements.

I can't believe I'm saying this, but show me the math!
Okay! Here's a hypothetical investor. What was the client's return?

- Client invested $40,000 on July 9, 2015
- She received three years of distributions totalling $11,000
- Book value is (40,000 +11,000) = $51,000
- Current market value = $51,880

Old me (wrong calculation)

Return = (Market value - Book value) /Book value
= (51,880 - 51,000) /51,000
= 1.73% cumulative return

New-and-improved me (right calculation)

Return = (Market value - amount invested) /amount invested
= (51,880 - 40,000) /40,000
= 29.7% cumulative return

The mystery of book value, solved!

Book value is not an appropriate representation of the total amount invested. Rather, it's used to calculate capital gains and losses for income tax purposes. To calculate your true performance, use your market value and amount invested from your statement. While this information may not appear on your monthly statements, most dealers put it on their annual statement with the actual return. If you don't have this information, please contact your advisor for assistance.

See Understanding distributions for more information about distributions and how they work.

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