ADVISER FUND UPDATE

Market Summary and Commentary for Individual Investors from Adviser Investments

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Is Your Portfolio Ready for 2013?
With just a few days left in the year, time is running out for those who are considering potential year-end tax saving moves. While it may be difficult to focus on these things during the hectic holiday season, the seven steps outlined below could pay dividends in 2013 and beyond.

1. Consider Rebalancing
At the start of each year, you'll hear a lot about rebalancing from the press and mutual fund providers--specifically, it is pushed as something to do as you make your New Year's resolutions. We have a different take, however.

For those who need a refresher, rebalancing involves selling shares of those stocks, bonds or funds in your portfolio that have had gains and reinvesting the proceeds in assets that are currently underweighted in your portfolio. For example, consider a hypothetical investor who invested in a portfolio comprised of three mutual funds on a year ago, with one third in a large-cap domestic fund, one third in an international stock fund and one third in a U.S. Treasury bond fund.

Due to variations in the performance of these funds over the past year, the investor's asset allocation today would be noticeably different, as Treasury bonds have underperformed stocks over this period, while U.S. stocks have outperformed international stocks. The industry-accepted approach for this investor would be to rebalance back to the original asset allocation. For someone focused on a specific risk profile or keeping a strict asset mix, rebalancing could be a valid practice.

At Adviser Investments, we contend that unless a portfolio has seriously diverged from the original allocation, rebalancing is often unnecessary or of little benefit. In looking at the effects of portfolio rebalancing at various regular intervals versus the effects of rarely or never doing so, we've found that there is little to no performance advantage to automatically resetting a portfolio's allocation every year. Plus, those who regularly rebalance may be burdening themselves with taxes on

gains and any fees generated by the necessary transactions.

That said, if you are planning to rebalance, make sure you speak with a trusted tax professional when formulating your strategy, as there are some additional wrinkles to consider this year, with capital gains taxes likely set to increase in 2013.

2. Know Your Funds' Distribution Dates to Avoid Taxable Income
We mentioned this in the November 23 issue of the *Adviser Fund Update*, but a review of year-end investing wouldn't be complete without it: If you are planning to make any additional purchases in 2012, it's important to know when your funds will be making their December distributions. Why? Taxes. If you buy shares of a fund prior to its "ex-dividend" date (the date on which the fund's price is reduced by the amount of the expected dividend or capital gain), you will have to pay taxes on additional distributions on those shares, even though you didn't own the shares when that income was "earned." Buying shares just prior to the ex-dividend date is often referred to as "buying the dividend," and it's something we avoid whenever possible for our clients.

To help you skip this mistake when investing in Fidelity or Vanguard Funds, we published full distribution calendars for both firms in the aforementioned *Adviser Fund Update* on November 23.

3. Should You Take a Loss?
If you have a loss in a fund you own in a taxable account, it may make sense to sell your shares to avoid a distribution, rather than have the distribution add to your tax bill. However, you'll need to consider the size of the distribution, the size of your loss and any fees that may be incurred in the sale before doing so. If you own the fund in a tax-deferred account, distributions will not affect your taxes. This is another strategy where we'd recommend speaking with a tax professional about your plans before taking action, since it may make more sense for some investors to save their losses until tax year 2013 to offset higher capital gains taxes.

4. Consider Opting Out of Automatic Reinvestment
We recommend that our clients have their income and capital gains distributions deposited into a money market fund, rather than automatically reinvesting the proceeds in the fund that generated them. This provides the flexibility of reinvesting in the fund at a later date or, as part of a rebalancing strategy, using the cash to add to other funds that may have underperformed recently.

5. Maximize Opportunities for Tax-Deferred Growth
It's a well-known fact that 401(k)s, IRAs and other retirement accounts are a great way to keep assets

growing tax-deferred. Therefore, consider contributing the maximum amounts allowable to each account every year. Depending on your employer's plan, you may be able to defer up to $17,000 in earnings to a 401(k) or 403(b) plan in 2012 (that amount increases to $17,500 in 2013). If you will turn 50 before December 31, 2012 and your plan allows it, you can contribute an additional $5,500. For IRAs, the maximum contribution in 2012 is $5,000 and $5,500 in 2013, plus a $1,000 "catch-up contribution" for those who turn 50 before during either calendar year. You have until April 15, 2013 to make your 2012 contributions, but if you do it now, your money can enjoy the benefits of tax-deferral sooner rather than later.

6. Don't Forget Your Required Minimum Distributions (RMDs)
If you have tax-deferred accounts, you will be required to withdraw a minimum percentage each year after reaching a certain age. The RMD rule exists to make sure that savings in retirement accounts are actually used for retirement and not just passed on to heirs.

You generally have until April 1 of the year following the calendar year in which you turn 70-1/2 to take your first RMD. These rules apply to any retirement account in which you contributed tax-deferred assets or had tax-deferred earnings, such as Traditional IRAs, Rollover IRAs, SEP-IRAs, 401(k) and 403(b) plans (Roth IRAs are not subject to RMD rules).

The RMD is calculated (in most cases) by dividing the adjusted market value of your tax-deferred retirement account as of December 31 of the prior year by an applicable factor taken from the IRS life expectancy tables. If you fail to take your RMD from your retirement account, you will be assessed a penalty equal to 50% of the amount you should have withdrawn, in addition to normal income taxes. These are heavy penalties, so clearly it's in your best interests to take these RMDs, something we help our clients with each year.

7. Focus and Finish
While taxes are one of the last things you may want to think about during the holiday season, taking the time to fine tune your portfolio now may help prevent bigger headaches and tax bills come April. That said, restructuring a portfolio and moving assets in an attempt to avoid distributions can be tricky, which is why we recommend you consult with a professional tax adviser before doing so.

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management, Adviser Investments is one of the nation's largest mutual fund research and money management firms. Our investment professionals focus on helping individual investors, trusts, foundations, and institutions meet their investment goals. Our minimum account size is $350,000.

For more information, please visit www.adviserinvestments.com or call 800-492-6868.

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