

“A New System, New Opportunities, and Expanded Service”

The Challenge of Rebalancing Accounts

Over the years we have improved our quality and our efficiency by constantly looking for ways to upgrade and streamline our investment review and trading processes. A major challenge has been the fact that the review process itself is incredibly labor intensive. This means that we always have some room for human error even when everything is reviewed by up to three people. The other challenges in the investment area come from the actual rebalancing and trading activities. These challenges include making sure all our basic rules are followed, such as:

- Not selling an investment that hasn't been held for 12 months to create a long-term vs. short-term capital gain, when the tax consequences are important.
- Not selling a mutual fund before the redemption fee no longer applies, which is up to 180 days for some funds.
- Making sure there is enough (but not too much) cash in each account to keep your money working for you.

Another challenge is the rebalancing of individual accounts while taking into consideration the investments in all other family accounts including both retirement and taxable accounts. Here again we have designed ways to make the process more efficient, but we still require a large amount of individual effort for review at this level

which means there is still room for human error.

Finding an Answer with iRebal

We have explored many possible solutions over the last few years, including several software systems. We found the answer with a relatively new system called iRebal. This system was developed for large firms that are very similar to ours, and we are the 16th firm to implement it. It is a revolutionary expert, rule-based software application that allows us to avoid many of the human errors that we have described. It will assist us in reviewing for rebalancing more frequently, improve our cash management system, automate the process of harvesting tax losses when needed, provide a means to continually improve the efficiency of our investment operations, and provide a method for improving our client service.

“So What? How Does it Affect Me?”

iRebal allows us to incorporate our rules in the software to make sure that we manage portfolios consistently. We establish models for each client as we do today, but the implementation of the model or investment plan will be more consistent. It will enable us to review accounts for rebalancing on a much more frequent basis since the system does not have the same physical limitations that we, as individuals, have. Once we run a portfolio review for rebalancing, the process is the same. We still have several professionals who review the account, but now the review can be

focused at a higher level. So instead of reviewing to make sure we have held an investment long enough for the gain to be long-term, now we can spend more time determining if the trades make sense based on the overall target and the current environment.

Of the many key functions that iRebal will improve, the most important is our ability to increase the frequency of account reviews. A close second will be a much more efficient method for across-accounts family-level rebalancing. This means that we can be much more proactive in choosing where we sell investments to rebalance such as selling in the IRA vs. selling in a brokerage account. The cash management system will allow us to be more effective at managing cash to make sure the right amount is available when needed, but it remains invested and keeps working for you as long as possible.

Some of the latest studies on rebalancing show that significant value is added by reviewing for rebalancing on a more frequent basis. This doesn't necessarily mean you trade more often, but that you take advantage of opportunities where there is significant volatility or shifts in the financial markets. This is especially true of the more volatile asset classes such as emerging markets and commodity index funds. These studies show that more frequent reviews can improve returns up to .4% over a one-year period of time. This increase may seem small, but compounded over time, the improvement in returns can be significant.

“What's Next and What Will Change?”

In order to take full advantage of the new system, we will need to change the timing and types of reports that you receive when we review your accounts. Under the current

system, we review accounts and provide you with a report before trades are placed. This report advises you what buys and sells are going to be done and when these trades will be placed. Typically these trades have been completed from one day up to two weeks after the review was completed and the report issued.

iRebal gives us the ability to review monthly or weekly or even daily which means we can take full advantage of major financial market moves in a much more timely way. It also means that the trades need to be placed very quickly in order to take full advantage of this capability. We will now place trades immediately rather than waiting up to two weeks as we have in the past. We will continue to provide a summary report that shows the account and the changes that were made to give you a current picture of your accounts. However, you will typically receive these reports after the trades are placed.

Any client who wants to receive the reports more quickly may receive them electronically either through our “Virtual Safe” or through email reporting. If you want to see the trades prior to their being placed, you must complete the attached form making that selection. Please complete the attached pink form either way to confirm your choice so that we provide your reports in the manner you want them provided.

We are in a final testing phase this week and will be ready to go live within the next two weeks. We know this is a big change for some clients, but we believe it will be very worthwhile over the long-term. We are really excited about the improvement of service through the use of this system and welcome any comments or questions.