



# TAXMANAGED ALLCAP

Third Quarter 2017

## OBJECTIVE

The TaxManaged AllCap strategy seeks to outperform the Russell 3000® Index on an after-tax basis by combining superior stock selection with rigorous, precise portfolio risk management and active tax management.

**Benchmark:** Russell 3000 Index

**Inception Date:** March 1, 2004

## MANAGEMENT GUIDELINES

**Holdings:** Approximately 65-90 positions

**Position weights:** 0.50% to Russell 3000 weight +2.50%<sup>1</sup>

**Cash position:** Typically 0.5% to 1.5%

**Annual turnover:** Typically 60% to 120%

## INDIVIDUALLY MANAGED AND CUSTOMIZED

An optimal tax-managed strategy not only incorporates active tax management, but also considers the client's actual cost basis, individual tax rate, and requested investment restrictions.

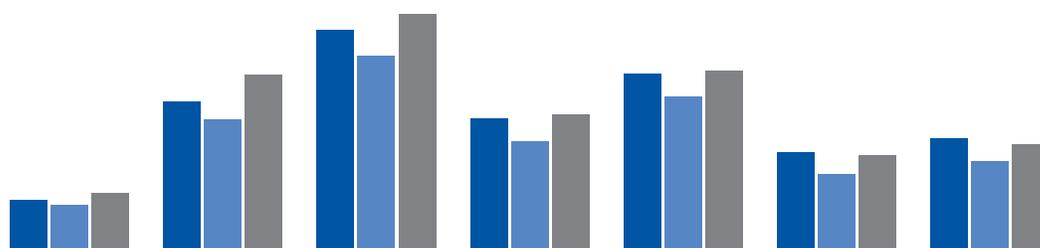
Our tax-managed strategy accommodates client-driven investment restrictions including:

- Stock specific restrictions
- Industry restrictions
- Environmental, Social, and Governance (ESG) preferences

Transition management evaluates client's existing holdings:

- Holdings are not sold off simply because they are not in the model. They are evaluated for return potential, tax consequence, and risk.
- The solution incorporates some portion of the client's holdings with new securities which enhance the expected risk/return profile of the client's portfolio.
- Realized gains are capped at 10% of the portfolio's value at transition or can be adjusted to the client's needs.

## COMPOSITE PERFORMANCE



### AFTER-TAX RETURNS<sup>3</sup>

TM AllCap Gross of Fees <sup>2</sup>	3.84%	11.28%	16.79%	10.11%	13.36%	8.52%	9.16%
Russell 3000 Index Total Return	4.36%	13.20%	17.70%	10.00%	13.62%	7.12%	8.00%

## PROCESS

Optimal management of taxable assets demands a three-dimensional focus on return, risk and costs—especially tax costs.

### RETURN

Using a “bottom up” systematic process, the investment team evaluates a broad universe of stocks using three independent analyses, each of which is designed to provide a unique valuation perspective. Evaluating each stock from these different perspectives is intended to improve the accuracy of the stock evaluation.

- **Broad Universe Analysis:** Evaluates each stock relative to all other stocks in the universe using financial and technical factors.
- **Style-Specific Analysis:** Segregates the universe into four style and market cap groups and evaluates each stock, relative to its peers using a customized model which includes financial and technical factors specific to each style and market cap combination.
- **Sector-Specific Analysis:** Divides the universe into 11 economic sectors and evaluates each stock relative to its sector peers using financial and technical factors.

These three analyses are combined to generate an excess return expectation for each stock. Stocks must rank in the top 20% of the Russell 3000 to be considered for purchase.

### COST

Research shows that over the decades, the tax impact on taxable investors in actively-managed funds has averaged two percent per annum—or 20% of the stock market's long-term gains<sup>4</sup>.

#### Taxable Gains

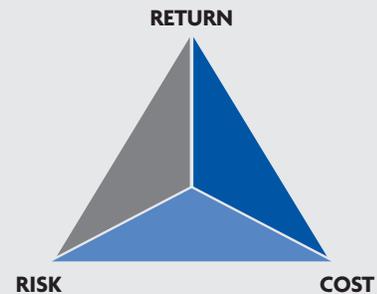
- Losses are harvested during optimization in order to offset realized capital gains.
- We monitor “almost” long-term gains and losses:
  - » Stocks approaching long-term gain status from a short-term gain are given an additional trading penalty
  - » Stocks approaching a long-term loss status from a short-term loss are given an additional trading incentive
- Each client's portfolio is customized to the appropriate tax bracket
- Wash-sale monitoring is fully automated
- Cash for withdrawals is made available by selling high-cost securities

#### Transaction Costs

Transaction costs can amount to 10% of a stock's total return or 40% of a manager's active return.<sup>5</sup> Our optimization process incorporates active monitoring of transactions costs:

- We employ ITG's Agency Cost Estimator® (ACE) to estimate trading costs
- Real-time transaction cost estimates based on actual order flow
- Includes commission, bid/ask spread, and market impact
- We do not engage in soft dollar trading

### A Three-Dimensional Approach



### RISK

Risk management is an essential part of the firm's process. Updated expectations are incorporated into the portfolio using a risk/return optimization process. This process features individual stock selection as the central source of added value while style, market capitalization, and sector departures from the benchmark are constrained:

- **4.5% active risk vs. Russell 3000**
- **Beta of 0.97 - 1.03**
- **Rigorous sector and industry constraints**
- **Rigorous market cap and style constraints**

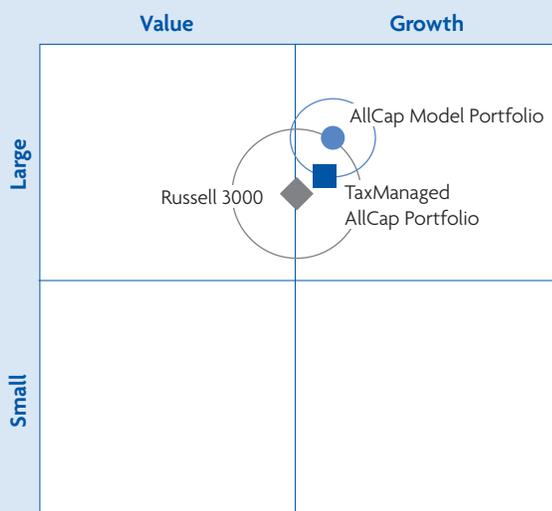
### SELL DISCIPLINE

Successful positions are sold as return expectations are realized and/or valuation perspectives deteriorate into overvalued conditions.

Additional consideration is given to the potential tax impact of each position, and during the rebalancing process, gains and losses may be paired to reduce the tax liability of the transaction while increasing the return expectations for the portfolio.

### DUAL BENCHMARK IMPLEMENTATION

This strategy employs a unique dual benchmark approach. The primary benchmark is the Russell 3000 Index, and our AllCap strategy portfolio serves as a secondary benchmark.



The primary benchmark is used to ensure the TMAC portfolios maintain a true core all cap profile, with a targeted active risk of 4.5% relative to the Russell 3000. We believe this construct is essential in maintaining the client's overall asset allocation.

The TMAC's tracking error target of 1.5% relative to our AllCap strategy portfolio ensures each client's portfolio maintains a similar profile, while providing the flexibility needed to manage the unique tax characteristics of each individual account.

Market cap, style, and sector biases are permitted to vary among individual portfolios and will be permitted to depart from the AllCap Model Portfolio in an optimized trade-off between the tax liabilities and portfolio risks of individual accounts.

Individual portfolios may also hold more positions than the AllCap strategy portfolio to facilitate desired return and risk enhancements at a greater level of tax efficiency.

### MODEL PORTFOLIO COMPOSITION

Top 5 Active Weights vs. Russell 3000	AllCap
Boeing	3.06%
Home Depot	2.65%
BlackRock	2.58%
UnitedHealth Group	2.54%
Tesla	2.53%

Bottom 5 Active Weights vs. Russell 3000	AllCap
Apple	-2.06%
Berkshire Hathaway Cl B	-1.35%
Exxon Mobil	-1.33%
JPMorgan Chase	-1.30%
Alphabet Cl A	-1.11%

Sector Weightings	AllCap	Russell 3000
Consumer Discretionary	8.50%	7.43%
Consumer Staples	10.39%	6.44%
Energy	3.06%	5.54%
Financials	19.42%	20.36%
Health Care	8.21%	12.49%
Industrials	9.57%	8.17%
Materials	7.73%	3.96%
Retail	6.41%	4.67%
Services	2.53%	5.83%
Technology	22.88%	21.90%
Utilities	1.30%	3.21%

Barra Risk Factors <sup>6</sup>	AllCap	Russell 3000	Difference
Currency Sensitivity	-0.01	0.00	-0.01
Earnings Variation	-0.13	0.01	-0.14
Earnings Yield	-0.02	0.00	-0.02
Growth	0.14	-0.02	0.16
Leverage	-0.11	0.00	-0.11
Momentum	0.15	-0.01	0.16
Size	-0.16	-0.06	-0.10
Trading Activity	0.14	0.02	0.12
Value	-0.11	0.00	-0.11
Volatility	-0.04	0.02	-0.06
Yield	-0.14	-0.01	-0.13

1. At the time of purchase

2. Fees, including but not limited to the advisory fee, transaction and custody charges, would reduce the return. For example, if an annualized gross return of 10% was achieved over a 5-year period and total fees (management, custody, transactional and all other fees applicable to a portfolio) of 1% per year was charged and deducted annually, then the resulting cumulative return would be reduced from 61% to 54%.

3. After-tax performance is calculated based on pre-tax rates of return using a pre-liquidated methodology which does not reflect tax impact on unrealized gains or losses and does not reflect deduction of sponsor bundled fees. After-tax returns are reported on a pure gross of fees basis. Information presented on a pure gross of fees basis has not been independently verified. After-tax composite and benchmark returns are based on the maximum Federal individual tax rates in effect for the applicable period and do not reflect state or local taxes. Realized capital gains and losses are recognized on a specific identification basis. The after-tax returns shown are subject to the limitations of the specific calculation methodology applied. Net performance reflects the deduction of investment management fees and bundled fees as applicable.

4. "Pay Less Tax on Your Funds", Kiplinger's Personal Finance, November 2008 (<http://www.kiplinger.com/article/investing/T041-C000-S002-pay-less-tax-on-your-funds.html>)

5. "Why Worry About Transaction Costs?", Advanced Investment Partners

6. MSCI Barra. Barra, Inc.'s analytics and data ([www.barra.com](http://www.barra.com)) were used in the preparation of this report.

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The Disciplined Equity TaxManaged AllCap Composite includes all unrestricted accounts managed for sponsor platforms under the TaxManaged AllCap strategy and is benchmarked to the Russell 3000 Index. Accounts within this composite do not employ leverage. The composite inception date was February 28, 2004. All cash reserves and equivalents are included in returns. Returns are time weighted and include reinvestment of dividends, income and gains. The value of assets and returns is expressed in U.S. dollars. All holdings available upon request. All data is as of September 30, 2017 unless otherwise noted. Performance prior to October 1, 2013 occurred at Advanced Investment Partners prior to being acquired by Great Lakes Advisors. Additionally, market commentary is available on the firm's website at: [www.greatlakesadvisors.com](http://www.greatlakesadvisors.com) or upon request.

The benchmark selected for comparison of returns for the TaxManaged AllCap Composite is the Russell 3000 Index (which contains 3,000 of the largest capitalization stocks of U.S. domiciled companies, representing about 98% of the total U.S. equity market capitalization.); The Russell 3000® Index is a trademark of the Frank Russell Company. Frank Russell Company ("FRC") is the source and owner of the Russell Index data contained or reflected in this material and all trademarks and copyrights related thereto. The presentation may contain confidential information and unauthorized use, disclosure, copying, dissemination, or redistribution is strictly prohibited. This is a GLA presentation of the Russell Index data. FRC is not responsible for the formatting or configuration of this material or for any inaccuracy in GLA's presentation thereof. Index returns are provided to represent the investment environment existing during the time periods shown. All indexes are fully invested, which includes the reinvestment of income. The returns for the index do not include any transaction costs, management fees or other costs. The index is not available for direct investment. Industry sectors are presented to illustrate the diversity of areas in which we may invest, and may not be representative of current or future investments.

Since the client's actual circumstances and tax rates determined after the fact may differ from the anticipated tax rates used in this process, the reported returns may not equal the actual after-tax for specific clients. This information has been prepared for informational and illustrative purposes only and is not intended to serve as legal tax advice. All accounts are customized so performance results will vary.

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