

Current Observations

None. Nada. Zip. Zero! By Paul Sutherland, CFP®

There was a recent article in *Bloomberg BusinessWeek* that recently caught my eye. Titled “Rich Pumped for Fees in Private Banking ‘Conflict of Interest’,” the article revealed some of the unsound practices and fee structures implemented by some financial advisers that serve only to benefit themselves rather than their clientele.

The article described how some investment firms have fee structures that incentivize advisers to steer their clients to riskier, more expensive products (e.g., hedge funds, structured products, annuities, etc.), rather than acting in their clients’ best interests. The article also pointed out how one adviser had identified 17 different ways firms earn revenues, which often include fees, commissions and expenses that were neither transparent nor disclosed to their clients. Clients were often not aware of the substantial conflicts of interest that can exist, for example, between brokerage firms, trust companies and private banks. Firms, of course, receive investment management fees, which most often are all that a client will see. The client may not realize, however, that their adviser might also receive transaction commissions, trustee fees, accounting fees, fee-sharing, front-end/back-end commissions or 12b-1 fees from mutual funds, annuities and such. Expenses can be very substantial, and of course it is hard for a consumer to analyze the cost-benefit-value equation in the complex world of investing.

Unlike some of the practices described above, FIM Group does not charge more for “growth” accounts or less for “yield income accounts,” so there is no incentive or benefit to placing a client in a higher-risk investment category. In fact, our fee structure is the same across all four of our main investment strategies. Plus, we not only fully disclose all costs to our clients in a transparent and straightforward way, we are committed to controlling expenses and minimizing the erosive influence that high commissions, hidden fees and expenses can have on a portfolio. FIM Group is a fee-



“Ninety percent of wealth-management clients are not aware of the costs they pay indirectly,” co-founder MyPrivateBanking.com, a Kreuzlingen, Switzerland-based firm that provides research and analysis on the private-banking industry.

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only adviser – which means we cannot receive commissions, fee-sharing payments, or referral fees from trust companies, brokers, banks or any entity or person. None. Nada. Zip. Zero! We only receive the fees that our clients pay, which are fully disclosed and detailed on each monthly and quarterly statement. Through our flexible, global strategy we do invest from time to time in closed-end funds (CEFs) and holding companies that may receive a management fee, but FIM Group is neither incentivized nor compensated when we carefully select investments for our clients. Our job is to seek out the best value and build our portfolios one security at a time, taking into consideration the full investment process.

Doing the Right Thing

We have a huge incentive to control expenses for our clients. Why? Because it's the right thing to do. We believe that there should be no other reason to do something with integrity and virtue than simply because it is the right thing. If Wall Street had done the right thing and operated with virtue rather than greed, they probably could have completely avoided the problems they experienced in the last couple of years. But as the saying goes, "You can't regulate morality."

So is managing a company based on principals and virtue "Pollyanna pie-in-the-sky idealism" or raw and uncooked wisdom? I don't know really – especially when I see Wall Street executives and brokers make hundreds of millions selling junk that they know is junk by misleading or obscuring the reality to unsuspecting or even "sophisticated" investors.

Virtue vs. Greed

I think it is logical to think about the "virtue vs. greed" equation when investing for clients. Should we invest in questionable businesses no matter how profitable the outcome? Should investors hire managers with legacies that show a trail of woe to its

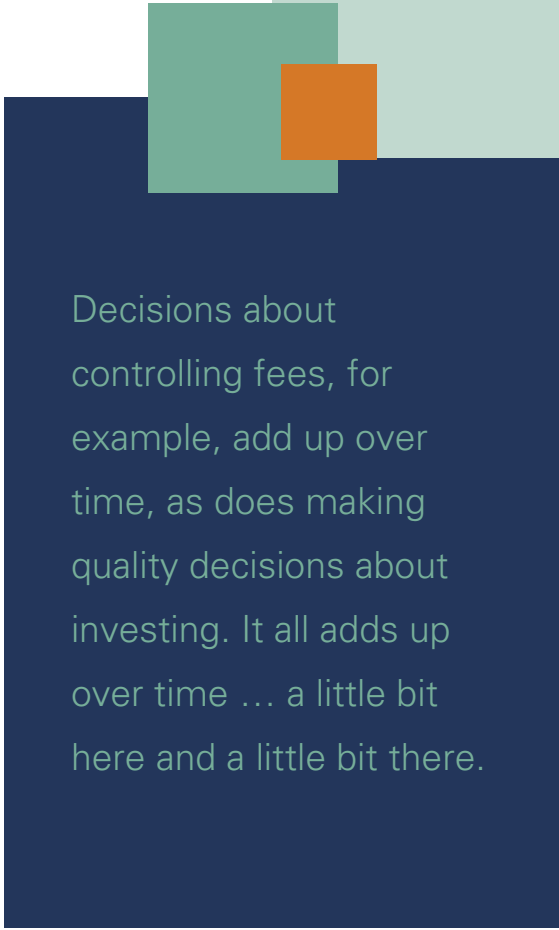
shareholders, clients and rank-and-file employees (while these managers and their kin are often well-rewarded with bonuses made on the short-term speculation)? Should investors be values-neutral in their investing? The tsunami of 2008 and the aftershocks we see today tell us it is a loser's game to invest with those that are values-neutral and that lack an ethical, sustainable, virtuous business philosophy. So I believe defaulting to doing the right thing – the virtuous thing – is the proper course for investors.

Little by Little ...

At its roots you'll find that consistent, positive compounding performance comes from many little "right decisions." Decisions about controlling fees, for example, add up over time, as does making quality decisions about investing. It all adds up over time ... a little bit here and a little bit there. FIM Group is proud of our track record. If you would ever like to compare your FIM Group performance against another manager, index, benchmark mutual fund, entity, inflation, money market or your Mom's investment club's performance, we'd be happy to run the numbers for you. We are committed to integrity, transparency, virtue and performance. If you have any ideas on ways we can improve, no matter how big or small, feel free to let us know by e-mail, phone, snail mail or in person.

Politics and Bailouts

Sadly, taxes, politics and bailouts are part of this value conversation. FIM Group manages all of our taxable portfolios to maximize after-tax returns. Politics will have an effect on tax laws and capital flows because of incentives and bailouts, which seemed to have upset "economic natural order" in the U.S. and overseas. Countries have in some cases allowed risks to be borne by society (bailouts) and rewards to be kept by the taxpayer. Foolish, arbitrary politics creates a moral hazard when risk management and prudent business strategies are trumped by recklessness reinforced by taxpayers' bailouts. When bad decisions by businesses cause



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no pain, then a reinforcement loop happens that continues until something changes. Things are a changing in Washington, but right now for business it seems like we are playing a game where the rules keep changing. Things, however, will stabilize as they always do. The new normal, for awhile at least, will be more bone-headed regulations, harder-to-understand tax laws, new layers of incentives and disincentives, and a Congress and White House ill-equipped to say "no" to anything that has to do with spending. I am not melancholy in this assessment. Democracies are reactive systems, so things will need to get overregulated and Congress will have to say "yes" one too many times before voters say "enough," and the dismantling cycle starts once again. Any student of American history knows this. Any student of world history knows this. And for that we have lots to be grateful for and reason to be optimistic.

An Opportunity Not to Be Missed

By Kevin Russell, CFP®

For the bulk of you timely tax filers, you now possess your 2009 returns. For some of you, there might be a nice planning gem built into your tax returns that you should be aware of. Recently, while reviewing our clients' 2009 returns, we noticed a few situations where a client was at a net operating loss (or negative income) for reasons such as very high itemized deductions from unusually high medical expenses or charitable donations, pass-through losses from rental activities or business pursuits, or investment loss carry forwards from prior years. In these situations our clients had the ability to incur additional income and pay little or no tax. If you expect your taxable income and expenses to be similar in 2010 or future years, this is a prime planning opportunity of executing a Roth IRA conversion roughly equal to your negative taxable income. Not too many people can brag that they legally have taken money out of their IRAs tax-free. Ultimately, when you withdraw from the Roth IRA in retirement, these dollars will come back to you tax-free.

Also, with the significant media coverage of Roth IRAs in 2010, we have received some frequent questions from clients. Below are a few of those questions, along with our responses:

1. Can I contribute to a Roth IRA after I turn 70-1/2?

Yes, as long as you have earned income and adequate cash flow to make the contribution. Your contribution for 2010 would be limited to \$6,000, assuming that you have earned at least that amount. This is in contrast to a Traditional IRA, where you cannot contribute to the IRA once you begin required minimum distributions.

2. What is the income tax impact for my children inheriting the Roth IRA when I die?

One of the great benefits of the Roth IRA is the inheritance value, especially for beneficiaries who are in a much higher tax bracket than you. Assuming that the Roth IRA has been in existence for more than five years, all the distributions taken from the inherited Roth IRA by your beneficiary are tax-free. This is in contrast to an inherited Traditional IRA, which is taxable to your beneficiaries as distributions are taken.

3. Are there required minimum distributions from a Roth IRA?

During your lifetime there are no required minimum distributions from a Roth IRA. However, upon your death, your beneficiaries will be required to take a modest annual minimum distribution from the inherited Roth IRA. This continued compounding of investments stretched over both yours and your beneficiary's lifetime is one of the most powerful benefits of a Roth IRA. In addition, if the beneficiaries so desire, they could use the required minimum distributions from the IRA to fund a Roth IRA of their own. The result would be continued tax-free deferral throughout their lifetime and beyond.

4. Does the adjusted gross income waiver for a Roth conversion in 2010 only apply to this year?

No. Based on current IRS regulations, anyone has the ability



to convert their IRAs in 2010 and in future years. The only unique provision that applies to 2010 alone is the ability to recognize the income from the Roth conversion equally in your 2011 and 2012 income.

5. I have contributed to my Traditional IRA in the past and have not been able to deduct the contributions. How does this basis affect the taxation of the Roth conversion?

Hopefully you have tracked these contributions for the years you did not receive a deduction on your tax return. The first place to check would be Form 8606 on your federal return. If you do indeed have basis in your IRA, a pro rata share of the Roth conversion is not taxable. For instance, if you have an IRA with a value of \$100,000 and \$20,000 of basis, 20% of any Roth conversion would not be taxable. As a note, if you have many IRAs, you need to consider all values in the denominator to determine the percentage that is not taxable.

If you have any questions on Roth IRAs and conversions, please contact one of our advisers at FIM Group. Now would also be a great time, if you have not done so already, to forward a copy of last year's tax return to your local FIM office so we can update your pertinent information.

April 2010 – FAQs

By Barry Hyman, MBA

Q: “Is the sky about to fall in?” – type questions have come up in various forms lately including, “Could the problems in Greece and other European countries reignite the global recession?” or “What about the bubble in China real estate prices?” or “Is commercial real estate going to be the next shoe to fall?”

A: The basic questions that need to be asked are, “Is FIM Group following these developments? If so, how will you protect my portfolio from the potential resulting volatility? Are you positioned to benefit from such events?”

We are indeed keenly aware of all of these issues. Rather than buying and holding a static portfolio of investments and ignoring developments, we are an active global manager, which means we monitor these global developments and manage our portfolios accordingly. It does not mean we are going to bet on the sky falling in. If there is one thing we have learned from the bubbles and busts over the past 26 years, it is that it is impossible to predict the timing of crashes, no matter how inevitable they are. Rather, we are “sticking to our knitting” of assessing risk and making only those investments that we think will compensate us accordingly.

For example, in Europe there are several countries (including Portugal, Ireland, Italy, Greece and Spain – the so-called “PIGS” or “PIIGS” countries) whose governments are facing debt crises. We could bet they were going to fail by “shorting” their national debt, but the risk of bailout is not worth the speculation in our minds. Another approach we have analyzed

is to take advantage of the high yields their sovereign debts are paying as a result of the heightened risk. Some are paying upwards of twice the interest that U.S. Treasuries are paying. And if they are bailed out, we would benefit doubly as their prices would likely rise adding to the high-interest income they pay. But on the other side of the coin, the risk of failure and even the breakup of the Euro, while unlikely, is high enough to discourage us from making such investments.

In China there are indeed signs of a housing market bubble reminiscent of what the U.S. just experienced. But to bet against the housing market continuing to rise would be akin to playing financial Russian roulette. Shorting Chinese housing would be a disaster if timed too early, and the market first doubles from here before the eventual “correction” occurs. So instead, we are avoiding direct China residential real estate exposure as well as exposure to overvalued related investments.

But despite all of these risks, and there are always risks lurking in investing, there are tremendous opportunities. In fact, the more risk and worry that exists, the more room for mispricing of investments, and thus greater opportunity. In Europe we are still able to own companies in defensive and necessary industries like food, energy, health care and infrastructure that are selling for 25% to 40% below their net asset (or breakup) values. In Asia, while we do not own any China-listed securities, we own companies in those same industries as well as in growth industries like aged care facilities or businesses with prohibitive barriers to



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entry such as shipping ports selling at similar discounts.

While we cannot eliminate volatility, we do manage portfolios with an attempt to balance secure and growing long-term retirement income with realistic volatility expectations. Many investments we own pay dividends in excess of those paid by CDs and government bonds, and unlike fixed-income investments, the dividends these companies pay tend to increase over time. In order for investors to secure long-term income, given the low interest rate environment we expect for quite some time, we believe there will be a natural tendency of investors to move out of CDs and bonds as they mature and into these types of investments, accepting their higher volatility as fear subsides over time.

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Q: “I looked at my account on Schwab’s website today. Did Pargesa go down 94% Friday?”

A: Yeah, right. And it went up 1,600% today!

Q: “So how come you didn’t buy a million shares on Friday when it was down?”

A: Okay, I didn’t have this exact conversation, but this represents the kinds of conversations we’ve have with clients who watch their money on a daily basis. No, Pargesa didn’t drop from US\$84 to US\$4 on Friday, and go up from US\$4 to US\$86 on Monday. Friday’s price was a misprint. No matter how many times I give the following two-part explanation, some people just seem intent on watching their money, but I will try again:

1. Do not rely on current day pricing of foreign-listed securities. They are not reliable, because during the trading day, custodians like Schwab and Fidelity utilize the price of the security in the U.S. Over-the-Counter Market (OTC), not the actual price in the foreign market.
2. Watching your FIM portfolio on a daily basis is a misuse of your time and effort.

People don’t monitor the appraised value of their real estate or businesses on a daily basis. Portfolios we manage are no different. The daily movements might be more relevant if we managed

money using a “technical” approach that attempts to capture the daily or weekly movement of prices, markets and behavior, but we don’t. We make long-term investments that we expect to reward us typically within three to five years regardless of what the markets do. We are not going to use “stop-losses” or get out of an investment simply because its price is going down. We don’t try to time behavior of people or markets. Thus, looking at the value of your FIM Group portfolio on a daily basis is truly a waste of time and energy. Access to your accounts is easy and free, unlike getting daily appraisals on real estate or businesses, so I know people are tempted to do so. But your time would be better spent looking at your monthly statements, after all prices have been reconciled. For your daily pleasure, read the websites of the companies we own, and ask us questions about them. Doing so would help you learn something of value and may help make you a better investor. Looking at the prices of your securities daily will do neither.

Q: Indexing questions: These questions come in many forms. “My portfolio has not performed much better than (or even not as well as) the S&P 500 over the (less than market-cycle period of) time I have been with FIM Group. What am I paying you for?” Or, “I read (or heard from my relative or broker or friend) that active investing is inferior to indexing or passive (or buy-and-hold) investing.”

A: For a more thorough answer to these questions, I encourage you to read the

response to the third FAQs question on page 4 of the December 2009, issue of *Current Observations* – www.fimg.net/newsletter/archives.

To add to that answer, given the past decade of its performance, I cannot understand why anyone would want to use the S&P 500, or other common but arbitrary benchmark, as their objective. Over the 10-year period that ended 12/31/09, the compound return of the S&P 500 was a 9 percent negative (with dividends reinvested).* That means a nest egg invested in this index lost 9% of its face value, but when the more than 29% rise in the Consumer Price Index over that period is considered, such a nest egg would have lost nearly 40% of its purchasing power. So again, I reiterate, matching the return of a passive arbitrary index over the long-term may not really be a worthy objective. Your objective should be based on your individual financial situation. In general, on the investment front it should be to attain favorable positive real (inflation-adjusted) gains. More important, your main objective should be to have someone looking over your shoulder and helping you make sure you are on track to achieve your goals as well as someone to give you guidance on financial planning topics, including estate planning issues, insurance, legacy planning, wealth transfer, asset protection, etc.

* Source: Bloomberg

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FIM Group Would Like Your Feedback

Click Here



We realize that you are probably asked to take surveys all the time. Often they are long and daunting, but we have created a very short survey so that we can continue to provide exceptional client service. This survey is posted on our home page www.fimg.net. We would greatly appreciate you taking less than five minutes to provide us with constructive feedback on how we can serve you and other clients better.

Please visit www.fimg.net, and click on the “FIM Group Survey” button.



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