Private wealth: allocation, tax and review

Private Wealth

1 A story: the textbook portfolio

- A textbook mix ignores the person in the room
- Start with objectives and constraints
- Count the whole picture, not just the portfolio
- Link every choice to a reason and a trade-off

IN THE LESSON

- Picture a new client walking in, and the adviser reaching for a model portfolio.
- A standard mix of shares and bonds, done.
- Now meet Hana Whitlock.
- She spent most of her career at one company and still holds a big block of its shares, which she has never wanted to sell.
- The textbook says sell them and diversify.
- But those shares cost her very little, selling would trigger tax, and she must pay for her retirement.
- Callum Reyes therefore starts with a question, not a model: what is this money for?
- At Level Three you do not just recommend.
- You propose, and then defend every part of it.

2 Hana's objectives and constraints

Objectives and constraints, in Hana's facts

Item	Hana's facts
Return and horizon	Retire at 65, 7 years
Ability to bear risk	Limited: one essential goal
Willingness	Sold in a past fall
Tax and unique	20% on gains; legacy stock

IN THE LESSON

- Here is how Callum Reyes sorts what he knows about Hana.
- The required return is what the portfolio must earn to reach the goal.
- Hana retires at sixty five, seven years away, and that gives her horizon.
- Next comes risk.
- Ability to bear risk is what her finances can absorb.
- Hers is limited, because one essential goal depends on this money.
- Willingness is how she feels about losses.
- She once sold in a market fall, so her nerve is modest.
- Last, taxes, legal limits and unique circumstances.
- Gains are taxed at twenty per cent, and the legacy stock is her unique circumstance.
- Liquidity and values based wishes would be listed here too.

3 Example 1: the whole picture

Hana, 58: the total picture, in millions

Whole portfolio	everything she has invested	**4.0m**
Legacy stock	one company	**1.2m**
Stock as a share of wealth	1.2m ÷ 4.0m	**30%**
Essential goal, today	retirement spending	**2.0m**

IN THE LESSON

- Now count what Hana owns.
- Her portfolio is four million, and it includes the legacy stock, worth one point two million.
- Divide one point two by four and the stock is thirty per cent of her wealth, one company in a third of a fortune.
- That is too concentrated to keep as it stands.
- Her essential goal, paying for retirement, has a present value of two million.
- A complete adviser also counts pensions, her future pay and any business the client owns, because they change how much risk the portfolio can take.
- Hana has none of those beyond what you see, so the portfolio is the whole picture.

4 Example 2: the tax on selling

Selling all the stock today, tax rate 20%

Stock value	today	**1.2m**
Cost basis	what she paid	**0.2m**
Taxable gain	1.2m − 0.2m	**1.0m**
Tax at 20%	20% × 1.0m	**0.2m**
Tax as share of wealth	0.2m ÷ 4.0m	**5%**

IN THE LESSON

- Why not simply sell the stock?
- Because of its cost basis, which is what she originally paid.
- Hana paid only two hundred thousand, so selling at one point two million produces a gain of one million.
- Tax at twenty per cent on that gain is two hundred thousand.
- Divide that by her four million of wealth and it is five per cent of everything she owns, paid at once.
- After tax she keeps one million to reinvest, not one point two.
- This number is the trap in the outcome.
- A textbook answer that ignores it throws away two hundred thousand that a patient plan could manage better.

5 Two sub-portfolios, one client

Value (millions)

Bonds	**2.0**
Diversified shares	**0.8**
Legacy stock	**1.2**

Essential: bonds. Aspirational: shares and the stock.

IN THE LESSON

- Callum Reyes now splits her money by goal.
- Look at the bars, in millions.
- The first bar is the essential sub-portfolio, two million of bonds.
- It pays for the retirement spending she cannot do without, so it holds assets whose value should be there when she needs it.
- The other two bars are the aspirational sub-portfolio, the money for things she would like but could live without.
- It holds point eight million of diversified shares and the one point two million legacy stock.
- Placing the stock here is the key choice.
- If the company falls, her aspirations suffer, but her retirement does not.

6 From allocation to vehicles

Build the proposal

Pick the vehicles → Active or passive → Place by tax

Defend the proposal

Link it to a goal → Show the trade-off → Name the risk

IN THE LESSON

- Once the split is set, the adviser chooses how to hold it.
- Read the top row.
- First pick the vehicles, such as funds, exchange traded funds or direct holdings.
- Then decide between active and passive management, paying for active only where skill is likely to earn its fee.
- Then place each asset with tax in mind, so tax heavy assets sit in sheltered accounts.
- The bottom row is the defence.
- A strong proposal links every choice to a goal or a limit, shows the trade off it accepts, and names the risk that remains.
- Without those three, a recommendation is only an opinion.

7 Example 3: the price of safety

Essential 2.0m in bonds or in shares (illustrative returns)

Expected bond return	a year	**3.5%**
Expected share return	a year	**6.5%**
Return given up	3.0% × 2.0m	**60,000 a year**
What it buys	goal met if shares fall	**a secure goal**

IN THE LESSON

- Every defence admits a cost.
- Suppose bonds are expected to earn three and a half per cent a year and diversified shares six and a half per cent.
- These are made up for the example.
- If Callum Reyes holds the two million essential sub-portfolio in bonds rather than shares, Hana gives up three per cent of two million, which is sixty thousand of expected return each year.
- What does she buy?
- A retirement that does not depend on the share market.
- Callum states the trade openly: she accepts a lower expected return to protect an essential goal, and she signs knowing the price.

8 Example 4: selling the stock in stages

1.2m stock, 1.0m gain, sold in three equal years

Sold each year	1.2m ÷ 3	**400,000**
Gain in each sale	400k × 1.0 ÷ 1.2	**333,333**
Tax each year	20% × 333,333	**66,667**
Total over three years	3 × 66,667	**200,000**
A 60k loss harvested	20% × 60,000	**saves 12,000**

IN THE LESSON

- Now the legacy stock.
- Selling it all today costs two hundred thousand at once, so Callum proposes a third a year over three years.
- Each year she sells four hundred thousand, and since most of the value is gain, each sale carries a gain of about three hundred and thirty three thousand.
- Tax at twenty per cent is about sixty six thousand seven hundred a year.
- Over three years the total is still two hundred thousand.
- With a flat rate, staging defers the tax rather than removing it.
- What it adds is room to offset gains.
- A sixty thousand loss harvested elsewhere would save twelve thousand of that tax.

9 Defending each choice

Choice and the reason behind it

Choice	Because
2.0m in bonds	Essential goal
Sell stock over 3 years	Tax and concentration
0.8m diversified shares	Growth for aspirations
Low-cost index core	Skill hard to prove

IN THE LESSON

- Here is the defence on one page, each choice with the reason it answers.
- Two million in bonds answers the essential goal, and the trade off is the lower return.
- Selling the stock over three years answers two things at once, the tax bill and the concentration, and the remaining risk is that the stock can still fall while it is being sold.
- Point eight million in diversified shares gives the growth that aspirations need, and it can fall.
- A low cost index core suits the part of the portfolio where skill is hard to prove.
- Notice that no row says only what to buy.
- Each row says why.

10 A story: two identical portfolios

- Same assets, different accounts, different wealth
- Interest is taxed yearly, often at higher rates
- Unsold gains are taxed later, often more lightly
- How the return arrives decides the tax

IN THE LESSON

- Here is a puzzle.
- Two clients hold exactly the same assets, the same bonds and the same shares, with the same total in a taxable account and a sheltered account.
- Years later one is clearly richer.
- The only difference is which asset sat in which account.
- Tax efficiency is about how returns arrive.
- Interest is usually taxed every year, and often at the higher income rate.
- A gain on shares that you never sell is taxed later, if at all, and often more lightly.
- An asset whose return arrives as taxable income leaks every year.
- One that defers its gains keeps compounding.
- Callum Reyes uses this difference on purpose.

11 How tax-efficient are the asset classes?

- High-yield bond interest
- Bond interest
- High-turnover active fund
- Low-turnover index fund
- Shares held for years

IN THE LESSON

- Place the asset classes on one line, from tax inefficient on the left to tax efficient on the right.
- This line assumes, as is typical, that regular income is taxed more heavily than deferred gains.
- Far left is the interest from high yield bonds, taxed as it arrives.
- Next is ordinary bond interest.
- In the middle is a high turnover active fund, because its manager keeps selling and so keeps realising gains, which creates a tax drag.
- Further right is a low turnover index fund, which sells rarely.
- On the far right are shares held for years, where tax waits until a sale.
- Rules differ by jurisdiction, so treat the order as typical, not universal.

12 Four tax-management techniques

What each technique does

Technique	What it does
Asset location	Shelters tax-heavy assets
Deferral	Delays realised gains
Loss harvesting	Offsets gains with losses
Highest-cost lots first	Smaller gain per sale

IN THE LESSON

- Callum Reyes has four tools.
- Asset location means holding the tax inefficient assets in tax advantaged accounts and the efficient ones outside.
- Deferral means postponing realisations, because tax paid later leaves more money compounding in the meantime.
- Loss harvesting means selling a holding that is below its cost to book a loss, then using that loss to offset gains.
- And lot selection means that when you sell part of a holding bought at different prices, you sell the highest cost lots first, so the taxable gain is smaller.
- Whether you may choose the lots depends on the jurisdiction.

13 Example 5: location, worked out

Bonds 5%, taxed 40% yearly; shares 7%, taxed 20% at the end

Plan A: bonds taxable	1.806 + 3.870	**5.676m**
Plan B: shares taxable	3.296 + 2.653	**5.949m**
Gain from the swap	5.949 − 5.676	**0.273m**
Gain as share of plan A	0.273 ÷ 5.676	**4.8%**

Each plan: 1m taxable, 1m sheltered, 20 years

IN THE LESSON

- Let us measure asset location.
- A client has one million in a taxable account and one million in a sheltered account, for twenty years.
- Bonds earn five per cent, all taxed each year at forty per cent, so only the after tax return compounds.
- Shares earn seven per cent, all taxed at twenty per cent when sold at the end.
- Plan A puts bonds in the taxable account.
- They grow to one point eight oh six, and the sheltered shares grow to three point eight seven oh.
- The total is five point six seven six million.
- Plan B swaps them.
- Taxable shares reach three point two nine six, sheltered bonds two point six five three, a total of five point nine four nine.
- The swap adds two hundred and seventy three thousand.
- Where money sits matters as much as what it holds.

14 The arithmetic of a harvested loss

Tax saved now = loss × tax rate
Later gain is bigger by the loss

Loss realised	Cost minus the lower price
Tax rate	Rate on gains and losses
Tax saved now	Loss times the rate
Extra gain later	Taxed when sold later

IN THE LESSON

- When you harvest a loss, the tax saved today is the loss times your tax rate.
- That is the part everyone remembers.
- The part they forget is what you gave up.
- After selling, you reinvest in something similar, but its cost basis is now the lower price you just paid.
- So if it later recovers, the gain you will eventually report is larger by exactly the loss you took.
- At an unchanged tax rate, that later extra tax cancels the saving.
- What remains is deferral, the use of the saved money in between.
- The benefit is real only if future rates differ, or the deferral lasts a long time.

15 Example 6: harvesting fifty thousand

Fund cost 200,000, now 150,000; rate 25%

Loss harvested	200,000 − 150,000	**50,000**
Tax saved now	25% × 50,000	**12,500**
New cost basis	reinvest at 150,000	**150,000**
Sold later at 200,000	25% × 50,000 gain	**12,500 due**
If the later rate is 15%	12,500 − 7,500	**5,000 kept**

IN THE LESSON

- Hana's fund cost two hundred thousand and is now worth one hundred and fifty thousand.
- Callum Reyes sells it, books a fifty thousand loss, and at a twenty five per cent rate saves twelve thousand five hundred of tax today.
- He reinvests the one hundred and fifty thousand in a similar fund, so her risk is unchanged.
- But the new cost basis is one hundred and fifty thousand.
- If the fund later recovers to two hundred thousand and is sold, the gain is fifty thousand and the tax is twelve thousand five hundred again.
- At the same rate, the saving was only a deferral.
- If her rate then is fifteen per cent, the later tax is seven thousand five hundred and she keeps five thousand.
- Timing and tax rates both matter.

16 Example 7: choosing the lots

Sell 100 shares at 60; gains taxed at 20%

Lot costing 20	gain 4,000	**tax 800**
Lot costing 40	gain 2,000	**tax 400**
Lot costing 55	gain 500	**tax 100**
Highest cost first saves	800 − 100	**700 now**

Whether you may pick the lot depends on the jurisdiction

IN THE LESSON

- Now lot selection.
- Hana holds a fund bought in three lots of one hundred shares each, at costs of twenty, forty and fifty five.
- The price is now sixty, and she needs to sell one hundred shares.
- Sell the cheapest lot and the gain is four thousand, so tax at twenty per cent is eight hundred.
- Sell the middle lot and the gain is two thousand, tax four hundred.
- Sell the lot that cost fifty five and the gain is five hundred, tax only one hundred.
- Selling the highest cost lot first saves seven hundred today.
- It also leaves the low cost lots with their large gains for later, so again the saving is partly timing.

17 Example 8: when tax dominates

Keep the 1.2m stock to avoid tax? After-tax value, gain taxed at 20%

Sell now, after tax	1.2m − 0.2m tax	**1.000m**
Keep, price unchanged	0.8 × 1.2m + 0.04m	**1.000m**
Keep, price falls 30%	0.8 × 0.84m + 0.04m	**0.712m**
Keep, price rises 30%	0.8 × 1.56m + 0.04m	**1.288m**

IN THE LESSON

- Here is the trap.
- Hana says she will keep the whole legacy stock, to avoid the two hundred thousand tax.
- Test it.
- Sell now, and she has one million after tax.
- Keep it and the price stays flat, and she still owes the deferred tax, so her stock is worth the same one million after tax.
- Waiting did not remove the tax, it only delayed it.
- Now let the price move.
- If it falls thirty per cent, she is left with seven hundred and twelve thousand.
- If it rises thirty per cent she has one million, two hundred and eighty eight thousand.
- She keeps a large bet with no extra expected return, just to dodge a bill she still owes.

18 Mistakes to avoid so far

- A textbook mix that ignores the tax on selling
- Ignoring liquidity needs and behavioural limits
- Tax-heavy assets left in the taxable account
- Treating a harvested loss as a permanent saving
- Letting tax keep a risky position in place

IN THE LESSON

- Let us collect the common mistakes from the allocation and tax topics.
- One: recommending a textbook mix that ignores the tax on selling what the client already owns.
- Two: ignoring the client's liquidity needs and behavioural limits, such as the nerve she has shown in a fall.
- Three: leaving tax heavy assets in the taxable account when a sheltered one is available.
- Four: treating a harvested loss as a permanent saving, when at the same rate it is mostly a deferral.
- Five: letting tax decide the allocation, so a risky position stays in place just to avoid a bill.

19 A story: pay the tax now or later

- Deferred account: tax comes off at withdrawal
- Exempt account: tax comes off at the start
- Compare the rate today with the rate later
- Imogen, 40: a move abroad can change the later rate

IN THE LESSON

- Hana's daughter Imogen is forty and saving for retirement.
- Her employer offers two kinds of account.
- In the first, she puts in pre tax money, it grows free of tax, and the withdrawals are taxed.
- In the second, she pays tax on the money first, it grows, and the withdrawals are free.
- Both look sensible, and they can give exactly the same result, or very different results.
- The answer depends on one comparison: her tax rate today against her tax rate on the day she withdraws.
- And if she retires in another country, that second rate may be a different one altogether.
- That is the heart of this outcome.

20 Deferred against exempt

Deferred: $(1 + r)^n \times (1 - t_n)$
Exempt: $(1 - t_o) \times (1 + r)^n$

Yearly return	Return earned each year
Years invested	Years until withdrawal
Rate today	Tax rate when contributing
Rate at withdrawal	Tax rate when withdrawing

IN THE LESSON

- Here are the two formulas.
- In a tax deferred account, the contribution is made before tax.
- It grows to one plus the return, to the power of the years, and then the withdrawal is taxed at the rate at withdrawal, so the final value is that growth times one minus the later rate.
- In a tax exempt account, the contribution is taxed first at the rate today, so only one minus that rate goes in, and it grows with no further tax.
- Look at the two together.
- The growth factor is identical, so the only thing that differs is one minus the later rate against one minus the rate today.

21 Example 9: a hundred over twenty years

100 pre-tax, 6% a year, 20 years; rate now 30%, later 20%

Growth factor	1.06^20	**3.207**
Tax-deferred account	100 × 3.207 × (1 − 0.20)	**256.57**
Tax-exempt account	100 × (1 − 0.30) × 3.207	**224.50**
Deferred is ahead by	256.57 − 224.50	**32.07**
They tie when	rate now equals rate later	**30% = 30%**

IN THE LESSON

- Imogen has one hundred of pre tax earnings to save, for twenty years at six per cent.
- The growth factor is one point oh six to the twentieth, which is three point two oh seven.
- Her rate today is thirty per cent and she expects twenty per cent in retirement.
- In the deferred account she keeps one hundred times three point two oh seven times point eight, which is two hundred and fifty six point five seven.
- In the exempt account the tax is paid first, so only what is left goes in, and that grows to two hundred and twenty four point five oh.
- Deferred wins by thirty two point oh seven, because her later rate is lower.
- If the two rates were equal, the accounts would tie.

22 Which account wins depends on the later rate

Chart: Final value of 100 earned vs Tax rate at withdrawal (0 to 50%)

- Tax-deferred
- Tax-exempt: 224.50
- Equal at 30%
- Rate today

IN THE LESSON

- Here is the comparison on one picture.
- Along the bottom is the tax rate Imogen will pay at withdrawal, from nothing to fifty per cent.
- Up the side is the final value of the hundred she earned.
- Follow the exempt line first.
- It is flat, because its tax was paid at the start, so it ends at two hundred and twenty four point five whatever happens later.
- Now the deferred line.
- It starts high, at the full growth, and falls steadily as the later rate rises.
- The red vertical line marks her rate today, thirty per cent.
- The lines cross exactly there.
- Left of the crossing, deferred wins.
- Right of it, exempt wins.

23 Example 10: Imogen retires abroad

10,000 pre-tax, 5%, 25 years; taxed 40% now; 15% abroad

Growth factor	1.05^25	**3.386**
Deferred, retires abroad	10,000 × 3.386 × 0.85	**28,784**
Exempt account	10,000 × 0.60 × 3.386	**20,318**
Deferred, if she stays	10,000 × 3.386 × 0.60	**20,318**

IN THE LESSON

- Now the cross border twist.
- Imogen is taxed at forty per cent today, and can put ten thousand of pre tax earnings into either account for twenty five years at five per cent.
- The growth factor is three point three eight six.
- She is thinking of retiring to a country where, in this illustration, residents pay fifteen per cent on pension withdrawals.
- Deferred, abroad: ten thousand times three point three eight six times point eight five, twenty eight thousand seven hundred and eighty four.
- Exempt: sixty per cent goes in, twenty thousand three hundred and eighteen.
- If she stayed home, the deferred account would also give twenty thousand three hundred and eighteen, a tie.
- So deferred wins if she moves and ties if she stays.

24 Legal planning and residency

Legal and residency checklist

Item	Why it matters
Beneficiary designations	Who inherits the account
Power of attorney	Someone can act if she cannot
Tax residence	Governs tax on withdrawals
Review on a move	Documents may not fit abroad

IN THE LESSON

- Tax is not the whole plan.
- Legal planning also matters, and it too depends on the jurisdiction.
- Beneficiary designations say who receives an account when the owner dies, and they can override the will, so they must be kept up to date.
- A power of attorney names someone who can act if Imogen cannot, which covers incapacity, a risk that is easy to ignore until it happens.
- Tax residence is the country where she is treated as living for tax, and it governs how withdrawals are taxed.
- And when she moves, every document should be reviewed, because a form that worked at home may not be recognised abroad.

25 Example 11: the trap of the wrong rate

Same 10,000, 5%, 25 years; rate now 40%; retires where the rate is 45%

Rate at withdrawal	retires to a 45% country	**45%**
Deferred account	10,000 × 3.386 × 0.55	**18,625**
Exempt account	unchanged	**20,318**
Exempt is ahead by	20,318 − 18,625	**1,693**
Break-even rate	equals the rate today	**40%**

IN THE LESSON

- The trap in this outcome is picking an account without estimating the future rate.
- Suppose Imogen is advised to choose the deferred account because everyone says it wins, and she then retires somewhere that taxes withdrawals at forty five per cent.
- Deferred is now ten thousand times three point three eight six times point five five, which is eighteen thousand six hundred and twenty five.
- The exempt account still gives twenty thousand three hundred and eighteen, because its tax was paid at forty per cent and is behind her.
- Exempt wins by one thousand six hundred and ninety three.
- The break even is simple.
- Deferred is better while the later rate is below today's rate of forty per cent.
- Always estimate the future rate first.

26 A story: the manager beat the index

- Beating an index is not the same as meeting a goal
- Is the report fair to the manager?
- Does it show the client's own experience?
- Is each goal still within reach?

IN THE LESSON

- Hana's retirement pot has just had a review meeting, and the manager is proud.
- The portfolio beat its benchmark.
- Should Hana feel safe?
- Not yet.
- A market index is not her goal.
- Her goal is to pay for retirement, and a portfolio can beat an index while the goal slips away, for instance because she added money before a fall, or because the index was the wrong yardstick.
- Success for a private client means progress on what the money is for.
- So Callum Reyes reads the report asking three things.
- Is it fair to the manager?
- Is it true to the client's own experience?
- And is the goal still reachable?

27 What a good report shows

Report items and why they help

Report item	Why it helps
Net of fees, after tax	What she really keeps
Custom benchmark	A fair yardstick
Risk, attribution, costs	Why the result happened
Progress on each goal	Funded status

IN THE LESSON

- A good report starts with returns net of fees, and ideally after tax, because that is what the client actually keeps.
- It compares them with a suitable benchmark, often a custom one built to match the client's own asset mix, rather than a headline index.
- It shows risk, attribution, which explains where the return came from, and costs, so that drag is visible.
- And it shows progress on each goal, for example each sub-portfolio's funded status, which is its assets divided by the present value of what it must pay for.
- Without that last item, the report cannot say whether the programme is working.

28 Two returns and a funded status

Time-weighted = $(1 + R_1) \times (1 + R_2) - 1$
Funded status = assets ÷ goal's present value

Return, period one	Return, ignoring cash flows
Return, period two	Return, ignoring cash flows
Time-weighted return	Judges the manager
Funded status	Below 100% means a gap

IN THE LESSON

- Three measures matter here.
- The time weighted return links the return of each period, ignoring when money went in or out.
- Add one to each period's return, multiply them, and subtract one.
- It judges the manager, who does not control the client's deposits.
- The money weighted return is different.
- It is the single rate that equates the money put in with the money taken out, so it reflects the client's own timing of contributions and withdrawals.
- And the funded status is the assets of a sub-portfolio divided by the present value of its goal.
- A figure below one hundred per cent means the goal is not yet covered.

29 Example 12: a manager win and a client loss

1m, +20%, add 1m, then −10%; custom benchmark 6.5%

Time-weighted, two years	1.20 × 0.90 − 1	**8.0%**
Custom benchmark	same two years	**6.5%**
Ending value	(1.2m + 1.0m) × 0.90	**1.98m**
Money-weighted, a year	1m + 1m in, 1.98m out	**−0.7%**
Goal funded status	1.98m ÷ 2.10m	**94%**

IN THE LESSON

- Hana's retirement pot was one million and rose twenty per cent in year one.
- She then added another million, and year two returned minus ten per cent.
- The time weighted return is one point two times point nine, minus one, which is eight per cent.
- The custom benchmark returned six and a half per cent over the two years, so the manager beat it.
- But the ending value is two point two million times point nine, one point nine eight million.
- She put in two million and has one point nine eight.
- The money weighted return is about minus point seven per cent a year, because she added money just before the fall.
- Her goal is worth two point one million today, so it is ninety four per cent funded.

30 The goal is still short

Value (millions)

Portfolio now	**1.98**
Goal's present value	**2.10**
Shortfall	**0.12**

Funded status is 94%

IN THE LESSON

- Here is the verdict drawn as bars, in millions.
- The first bar is what the pot is worth now, one point nine eight.
- The second bar is the present value of the retirement goal, two point one.
- The third bar is the gap between them, point one two.
- The manager can truthfully say that the portfolio beat its benchmark.
- The client can truthfully say that she has less than she put in.
- Neither statement is the verdict on the plan.
- The picture is: the goal is ninety four per cent funded, and the shortfall is what a periodic review must now act on.

31 Example 13: what the review decides

Funded status 94%: the options at the review, in millions

Shortfall today	2.10m − 1.98m	**0.12m**
Option: top the pot up	add the shortfall	**0.12m**
Option: trim the goal	0.12m ÷ 2.10m	**5.7%**
Option: revise the policy	more risk, if she can bear it	**Judgement**
Verdict	beat the index, goal slipping	**94% funded**

IN THE LESSON

- So what does Callum Reyes recommend?
- The shortfall is two point one million minus one point nine eight, which is point one two million.
- There are three honest options.
- Top the pot up by point one two million.
- Or trim the goal, which means spending a little less in retirement.
- A cut of point one two over two point one is about five point seven per cent.
- Or revise the investment policy statement, perhaps accepting more risk, though only if Hana's willingness and ability allow it.
- The review may also lead to rebalancing.
- What it must not do is declare success because the manager beat an index while an essential goal has drifted out of reach.

32 How reviews run

Every regular review

Read the report → Check each goal → Hold, rebalance or revise

Extra review after

A life event → A market shock → A change of goal

IN THE LESSON

- Finally, the rhythm of review.
- Look at the top row.
- At every regular review, Callum Reyes reads the report, which should be net of fees and after tax, checks each goal's funded status, and then decides whether to hold, rebalance or revise the policy statement.
- Now the bottom row.
- Some events should not wait for the calendar.
- A life event, a market shock, or a change of goal each triggers an extra review.
- Reviews that happen only at set dates miss the moments when the plan is most likely to need a change.

33 Recap: the lesson in five lines

- Objectives and constraints first; defend each choice
- Shelter tax-heavy assets, but do not let tax lead
- Deferred wins if the later rate is lower
- Time-weighted for the manager, money-weighted for her
- Success means each goal stays funded

IN THE LESSON

- Let us pull the lesson together.
- First, begin from objectives and constraints, count the whole picture, split money by goal, and link every choice to a reason and a trade off.
- Second, tax efficiency depends on how returns arrive, so shelter the tax heavy assets, defer gains, harvest losses sensibly and pick the highest cost lots, but never let tax dominate risk.
- Third, a deferred account wins when the later rate is lower, ties when equal, and loses when higher, and legal planning and residency matter.
- Fourth, judge the manager by time weighted return and the client by money weighted.
- Fifth, judge success by goals.

34 Try three quick questions

1. Loss of 80,000 harvested at 25%. Tax saved now; permanent?
   Answer: 20,000 now; mostly a deferral, as the basis falls.
2. 100 saved, 5%, 10 years; rate 40% now, 25% later. Which wins?
   Answer: Deferred: 122.2 against 97.7.
3. A fund returns +10%, then −10%. Time-weighted return?
   Answer: 1.10 × 0.90 − 1 = −1.0%.

IN THE LESSON

- Now try three quick questions yourself.
- Pause after each one.
- Question one.
- A client harvests an eighty thousand loss at a twenty five per cent rate.
- What is the tax saved today, and is it permanent?
- Twenty five per cent of eighty thousand is twenty thousand now, but the new cost basis is lower, so at an unchanged rate the later gain brings the tax back.
- It is mostly a deferral.
- Question two.
- A hundred is saved for ten years at five per cent.
- The rate is forty per cent now and twenty five later.
- Which account wins?
- Deferred, one hundred and twenty two point two against ninety seven point seven, because the later rate is lower.
- Question three.
- A fund returns plus ten per cent, then minus ten per cent.
- What is the time weighted return?
- Minus one per cent.
- Remember to judge the plan by the goal.