



The **Mosaic** Financial Group LLC
Your Wealth Management Partner

How Portfolio Theory Worked In Real-World 2017

For investors, 2017 was a mirror image of 2016. The top performing types of American companies in 2016 were the biggest laggards in 2017. Meanwhile, the worst performing types of U.S. stocks in 2016 were the biggest winners in 2017.

The orderly rotation of the leaders and laggards vividly illustrates how Modern Portfolio Theory worked in the real world last year. Modern Portfolio Theory is a large body of knowledge

solution spawned of the research by several generations of the world’s best minds for increasing the likelihood of investment success, and it is the framework for investing that this firm believes in.

Applying portfolio theory at the end of 2016 meant lightening up proportionately on the most-appreciated types of assets — small-cap value stocks — and buying more of the types of assets that lagged, the S&P 500

Spotlight On... Derrick Allen & Tim DeBruyne

This article has traditionally been used each quarter to “Spotlight” an employee at Mosaic, in order to provide you with an opportunity to become familiar with some of the names and faces that



Derrick Allen

comprise our firm. This issue is special in that we are announcing the addition of two new partners to the firm, Derrick Allen and Tim DeBruyne. Derrick and Tim have been an integral part of Mosaic’s success and growth over the last 15 years.

Both Tim and Derrick joined Mosaic shortly after the company was founded in 2000. We would like to acknowledge their dedication and commitment

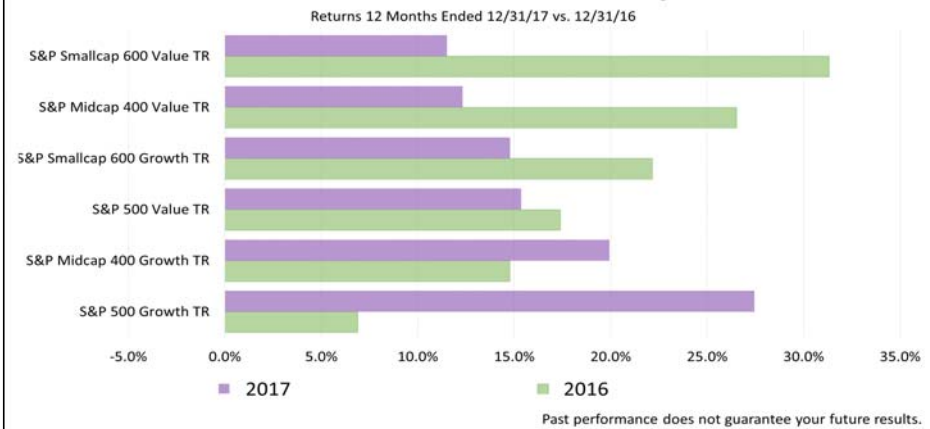
to our firm, clients, employees, and values. We congratulate Derrick and Tim on their appointment, and look forward to their continued contributions and leadership in the years ahead.



Tim DeBruyne

Congrats to Derrick and Tim!

A Vivid Illustration Of How Portfolio Theory Worked In 2017



based on 70 years of research by investment academics. It’s a framework for how investing is now taught in the world’s best business schools and long embraced by institutional investors. Basically, classifying investments based on their statistical characteristics imposes a discipline for managing assets based on history and fundamental facts about the economy.

Of course, human judgment based on a good sense of history is critical in applying the theory to people in the real world. And all this doesn’t guarantee success. It’s a theory. But it is the best

large-cap growth stocks. The exact amount of each type of asset is set based on your personal preferences and appetite for risk.

Usually, when you look at the returns of asset classes from one calendar year to the next, the performance seems random - there is no order to what occurred. The orderly reversal of leaders and laggards from 2016 to 2017 vividly illustrates a key concept in managing wealth prudently. In real-world 2017, then, the theory

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Ask About Personal Residence Trusts

By using a qualified personal residence trust (QPRT), you might be able to sidestep potential estate tax pitfalls while transferring a home to family members. You can continue to live in the home for a term of years, after which ownership passes from the trust to the designated beneficiaries. Your gift of the home to the trust is taxable, but rather than being based on the home's value when it goes into the trust, that value is reduced by the amount of your "retained interest," which is calculated according to a complicated formula based on interest rates, the term of the trust, and other factors.

But this unique estate planning technique is often misunderstood. Here are answers to several common questions about QPRTs.

Q. What are the estate and gift tax consequences?

A. When your home goes into a QPRT, it comes out of your taxable estate. Although the transfer of the remainder interest—the home's value minus your retained interest—is subject to federal gift tax, the resulting tax from this future gift tends to be low, especially while interest rates remain depressed. The IRS relies on the Section 7520 rate, which is updated

monthly, to calculate the tax.

Q. What happens if I die before the end of the trust term?

A. Then the home goes back into your taxable estate. This defeats the purpose of the trust, but your family is no worse off than before the trust was created.

Q. Do I have to transfer my principal residence?

A. That's normally the home used in a QPRT, but it can also be set up for a second home. In fact, you can have multiple personal residence trusts.



Q. How long should the trust term last?

A. There's no set period of time. Note that the longer the term, the smaller the value of the remainder interest that's subject to taxes. But a

longer term also increases the chance that you'll die before it ends and the home will be returned to your estate.

Q. Can I sell the home during the trust term?

A. You can, but you'll have to reinvest the proceeds in another home that will be owned by the QPRT and subject to the same trust provisions.

Q. Who pays for the upkeep of the home?

A. As long as you still live there, you do, for instance, you might pay the costs of monthly maintenance and repair, insurance, and property taxes to the trustee. But you get to deduct qualified expenses on your tax return.

Q. Can I back out of the deal?

A. No, the trust is irrevocable. However, if you want to stay in the home after the trust term, you can set up a rental agreement with the beneficiaries. They will have to pay income tax on the rent they receive.

Q. Are there any other drawbacks?

A. There are costs associated with a QPRT, including attorneys' fees, appraisal fees, and titling expenses. And you can't take out a mortgage on a home that has been transferred to a QPRT. (An existing mortgage is permitted but it complicates matters.) ●

Here's What You Can't Do In An IRA

If you have an IRA, you know how easy it is to move assets from one investment to another. You're able to choose from a wide array of investment options, and to take out money whenever you want, although you'll have to pay tax when you do. But there are some things you can't do with an IRA. There are strict rules against certain "prohibited transactions," which are spelled out in the tax laws. And there could be adverse consequences if you don't comply with the requirements.

The IRS defines a prohibited transaction as any improper use of an IRA by the owner, his or her beneficiary, or any "disqualified" person. That last

includes IRA fiduciaries and members of the owner's family. An IRA fiduciary is someone who (1) exercises any discretionary authority or control in managing the IRA or exercises authority or control in managing or disposing of its assets; (2) provides investment advice to the IRA for a fee, or has any authority or responsibility for doing so; or (3) has discretionary authority or responsibility for administering the IRA.

What can't you do with your IRA? You're prohibited from:

- Borrowing money from it;
- Selling property to it;
- Using it as security for a loan;
- Buying property for personal use

with IRA funds.

You can, however, effectively take a short-term loan from your IRA by withdrawing funds from it and then depositing the same amount back into the same or a different IRA within 60 days. That is technically a "rollover" and is not treated as a prohibited transaction.

If a prohibited transaction occurs, your account stops being an IRA as of the first day of the year of the violation. The net effect is that you're treated as having received a distribution of all of the IRA assets equal to their fair market value (FMV) on January 1 of that year. Assuming the total FMV exceeds your basis in the assets, you owe tax on the

Seven Security Steps After Major Data Breach

On September 7, 2017, one of the “big three” credit reporting agencies in the country dropped a bombshell. Equifax had been hacked, and almost 150 million Americans may have had their credit histories exposed. It was one of the largest cyber-breaches in history, and while it’s difficult to get a handle on exact numbers, suffice to say that it’s quite likely your information was compromised.

And it isn’t just U.S. citizens who are at risk. The hackers also grabbed confidential data on residents of Canada and the United Kingdom. The other two major credit reporting agencies—Experian and TransUnion—weren’t affected.

It took some time for Equifax to get the word out. According to media sources, unauthorized access to data occurred during a three-month stretch between May and July of 2017. The breach was reportedly discovered on July 29, 2017.

What were the hackers after? Again, details are spotty and Equifax has promised to follow up with additional information, but at the very least it’s likely that names, addresses, dates of birth, Social Security numbers and in some cases, drivers’ license numbers were exposed.

Equifax has claimed that there was no evidence of unauthorized activity on

its core consumer or commercial credit reporting databases. But do you feel comfortable knowing that your personal information is in the hands of people who could do you considerable financial harm?

What’s more, it’s easy to be lulled into a false sense of security as time passes and you don’t experience any problems related to the hack. But it could be many months or even years before criminals try to use your information, and it pays not to assume that you’re immune.

Whether you believe your information was exposed or not, there are several steps you can take in the aftermath of the breach to protect your financial affairs. The Federal Trade Commission (FTC) has recommended the following actions:

1. Visit a special Equifax link at www.equifaxsecurity2017.com that the company set up to help consumers. (This link isn’t monitored or controlled by the FTC.) To find out whether your information has been compromised, click on the “Potential Impact” tab and enter your last name and the last six digits of your Social Security number. Your Social Security number is sensitive information, so make sure you’re on a secure computer

and an encrypted network connection before you enter it. The site will tell you whether you’re a victim of the breach.

2. Regardless of whether your information has been exposed or not, if you’re a U.S. citizen you can get one year of free credit monitoring and other services. When you’re ready to enroll, return to the site and click

“Enroll.” Currently, you have until January 31, 2018, to take advantage of this offer, but the deadline may be extended.

3. Check your credit reports from the big three credit reporting agencies by visiting annualcreditreport.com. Accounts or activity that you don’t recognize may indicate identity theft. Another link provided at IdentityTheft.gov tells you what to do if you think there’s a problem.

4. Consider a “freeze” on your credit files. With a freeze, it’s hard for a criminal to open a new account in your name. However, a credit freeze won’t prevent someone from making charges to your existing accounts.

5. Continue to monitor credit card and bank accounts closely for charges you don’t recognize. Remember that it may take a while for such activity to occur.

6. If you decide against a credit freeze, you might instead place a “fraud alert” on your files. A fraud alert essentially warns creditors that you may be an identity theft victim and that they should verify that anyone seeking credit in your name really is you.

7. File your tax return early. If you’re at risk, it helps to get your return into the IRS before a scammer has a chance to. Tax ID theft occurs when someone uses your Social Security number to seek a tax refund or a job. Also, be sure to respond immediately to any letters from the IRS.

Finally, visit Identitytheft.gov/data breach to learn more about protecting yourself after a data breach. In addition, your trusted financial advisors can provide you with more guidance. ●



difference, just like you would on any other withdrawal. Plus, you’re generally required to pay a 10% penalty if you’re younger than 59½.

Other rules restrict the types of investments you can make in an IRA. For instance, you can’t invest in life insurance

or collectibles such as works of art, stamps, precious stones, or jewelry. With a few limited exceptions, IRA funds also can’t be invested in gold or silver coins. And the IRA can’t hold any property that you personally use, such as your primary residence or a vacation home.

Holding certain other types of real estate, however, such as undeveloped land, may be permitted.

The tax law gives you plenty of leeway with regard to IRAs, but there are limits to that freedom. Make sure not to step over the line. ●

Trap

IRAs – Prohibited Transactions

- Any direct or indirect sale or exchange, or leasing, of any property between a plan and a disqualified person; commonly:
 - Residence or cottage
 - Business interest
 - Investment real estate
- Qualified Plan Penalties
 - 15 percent tax on the amount involved with a prohibited transaction
 - 100 percent tax if the prohibited transaction is not corrected
- IRA
 - Entire account is immediately disqualified & deemed distributed
 - Entire account is subject to income taxation

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Bitcoin, Chasing Your Tail, And Investing

Thinking about Bitcoin? Could be a good time to hop on, right?

Wrong! Usually, by the time the average investor jumps on a gaudy, freewheeling bandwagon, it's too late. The price spike has already occurred. If the investment is a fad, a sickening plummet may well await you.

Bitcoin blasted to a record high at rocket speed, hitting \$19,783 on December 17, 2017, before plunging over 50% by the beginning of February, 2018. The crypt-currency may yet be destined for greatness over the long-term, but its supersonic ascent and subsequent nosedive look much like other notorious investment fads.

In 1637, Dutch investors lost their bloomers on tulip bulbs. During tulip-mania, prices for bulbs reportedly rose from November 1636 to February 1637 by 2000%, according to academic research.

These objects of desire were flowers. It made no sense. The crash of the bulbs shattered lives and has ever since served as a beacon in financial history, warning

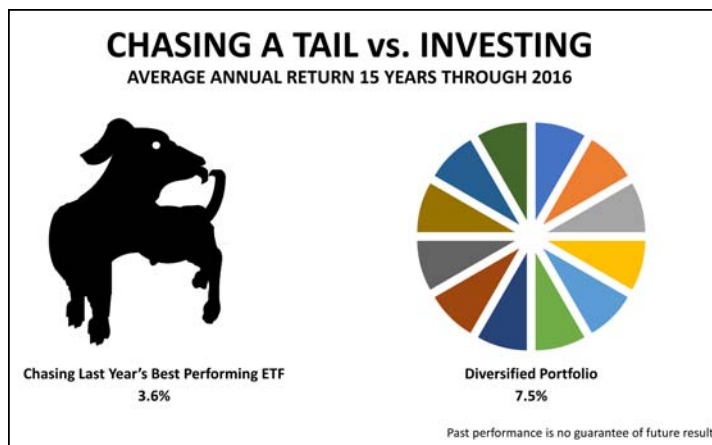
investors of the risk in chasing performance.

Investing in Bitcoin makes little sense considering that it is one of many crypto-currencies being mined on the Internet. The value of a crypto currency is set by supply and demand and supply is set by a software program that's not tied to a sovereign state. Transactions are easily hidden from tax authorities. Ultimately, crypto-currencies compete with sovereign nations, which is why some governments are starting to move to regulate them. In the time this was written, not only had the price of Bitcoin plunged 25%, but South Korea became

the first nation to ban all anonymous cryptocurrencies and regulate the rest.

Bitcoin's ascent was easy to spot as a mania, but the modern-day danger inherent in chasing hot performing investments is often far less apparent. For example, say you bought the No. 1 performing Exchange Traded Fund annually for 15 years through 2016. Sound like it could be a strategy for success? Think again, according to Dr. Craig Israelsen, Ph.D., who teaches portfolio design techniques to financial professionals. Your average annual return was 3.6% — less than half the annual return of a broadly diversified portfolio invested across 12 different types of assets equally and rebalanced systematically every year over the same 15-year period through 2016.

Human nature makes people susceptible to investment manias, shiny bright objects like Bitcoin, and chasing last-year's winners. It's why people will always need investment professionals to stay focused on economic fundamentals, quantitative analysis, controlling fear and greed. ●



How Portfolio Theory Worked

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worked exactly the way it's supposed to — it was uncanny.

Global stock market returns in 2017 versus 2016 reflected a similar mirror image. Although the seven types of U.S. and foreign stocks did not prove the theory quite as perfectly, the biggest winners of 2016, small-cap U.S. stocks, were the biggest laggards of 2017, and the biggest laggards of 2016 were the biggest leaders of 2017.

The real world of investing in 2018 is filled with uncertainty. Tax reform could accelerate economic growth and prompt the Federal Reserve to make a policy mistake by squelching growth or allowing the economy to overheat and inflation to surge.

The political scandal in Washington could devolve into a constitutional crisis or the nuclear standoff with North Korea could erupt with terrifying consequences. A 10% or 15% drop could occur at any time on bad news and the chance of a bear market decline of 20% or more increases as the eight-and-a-half-year bull market grows older.

On the other hand, the bull market could continue in 2018 and beyond, and prices could head much higher. The economy shows no sign of slipping into a recession; leading indicators signal a strong start to 2018; the world economy is growing in synchronicity with the U.S. - the first time that's happened in



many years; and the new tax law is expected to boost earnings sharply and that's what drives stock prices.

You can't be sure what the future holds, but seeing how well portfolio theory worked in the real world in 2017 may give you comfort and boost your confidence to stay committed to a program of long-term wealth management and financial planning. ●