WEALTH MANAGEMENT ADVISOR

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BUILD A DIVERSIFIED PORTFOLIO TO REDUCE RISK — AND MENTAL STRESS

INTEGRATED FINANCIAL

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Build a diversified portfolio to reduce risk — and mental stress

Diversification is a key strategy for managing risk in an investment portfolio, based on the philosophy that you shouldn't put all your "eggs in one basket." By spreading investments among asset classes, industries, sectors, geographical areas or other criteria, you're more likely to own securities that perform differently under different market conditions. However, building a diversified and more stable portfolio isn't as easy as it might seem.

Managing risk

Diversification increases the odds that at least some of your investments will perform well at any given time. But simply distributing your money among several mutual funds doesn't necessarily achieve diversification. Putting your eggs in many baskets won't be effective if the baskets are too similar to each other. This concept is generally known as "false diversification." To determine whether your portfolio is truly or falsely diversified, you need to drill down beneath the surface.

But first, it's important to understand that the goal of investing isn't to *eliminate* risk. After all, without some risk, there would be no rewards. If you invest too conservatively (particularly when you're young), your asset growth may not keep pace with inflation and may erode your wealth over time. But if you invest too aggressively (particularly when you're approaching retirement), you may expose your wealth to market volatility, which can quickly turn gains into losses.

Diversification, therefore, is a valuable tool for balancing risk and reward. The idea is to spread investments among assets that are negatively correlated — meaning their prices tend to move in different ways in response to the same conditions. If assets in your portfolio are too highly correlated or their prices move in tandem, your portfolio will be more sensitive to market volatility.

For example, if all of your investments are in large-cap stocks, a downturn in the S&P 500 index (which is made up of large-cap stocks) can have a devastating impact on your portfolio. But if your portfolio is properly diversified, poor performance in one area of the market may be offset by gains or more limited losses in other areas.

DO YOU HAVE TOO MUCH OF A GOOD THING?

As critical as portfolio diversification is, it's possible to overdo it. As you add stocks, bonds, funds and other assets to your portfolio, remember the law of diminishing returns. The more investments you add, the less risk reduction you get in return, until it's minimal. At that point, you may actually harm returns.

There are several reasons for this. One is that the more assets you hold, the greater the commissions, fees and other transaction costs you may pay. Another is that investing in a large number of assets makes it more difficult to track and manage your holdings, which can have a negative impact on quality, tax efficiency and asset mix.

Right mix

Although the right mix of assets for you depends on your particular circumstances, diversification can be achieved in many ways. These include by:

Asset class. Stocks, bonds and cash (generally, very short-term debt) tend to behave differently under similar conditions.

Company size. Large-cap, mid-cap, small-cap and micro-cap stocks often perform differently under similar conditions.

Bond type. You might invest in a mix of government, corporate and municipal bonds, in bonds of different maturities or durations, or in bonds with different credit ratings.

Investment style. For instance, a mutual fund or exchange-traded fund (ETF) might focus on growth investing, value investing or a blend of the two styles.

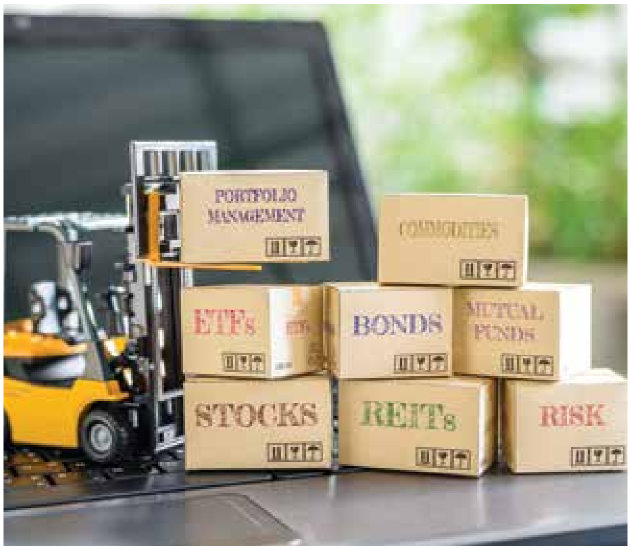
Industry or sector. The same economic or market factors may affect companies in different industries or sectors, such as technology, energy and pharmaceuticals.

Geography. Diversification can be achieved with a mix of domestic and international investments and, within the international arena, a mix from developed and developing countries. Note that securities from developed countries, particularly of large international companies, often perform similarly to U.S. securities.

These are just some of the factors to consider. The key to successful diversification is to analyze when the movements of your holdings are highly correlated.

False diversification

Mutual funds and ETFs can be great diversification tools. Often, they invest in a specific asset class or follow a particular investment style



(although many funds blend several asset classes or styles). But simply investing in several mutual funds or ETFs doesn't necessarily mean your portfolio is diversified. True, each fund may hold dozens or even hundreds of investments. But if these "baskets" are too similar to one another — for example, if they all invest in large-cap, dividend-paying stocks — their underlying securities will tend to correlate.

To avoid false diversification, ensure your funds provide a mix of assets and investment styles that are negatively correlated. And don't let your portfolio's strong performance during good times give you a false sense of security. If all of your investments are up at the same time, that can actually be a red flag for false diversification. Tomorrow, they could potentially all decline together. You also could potentially lose money on one or more investments.

Mix it up

In general, the best way to reduce investment risk is to examine your own personal financial goals, time horizon and tolerance for market volatility, and diversify from there. You may not want to do anything that can potentially reduce your portfolio's upside potential. But remember, diversification also usually lowers downside risk. Talk to your financial advisor about the best way to "mix it up." ■

Paying for college: Scholarships and grants may be taxable

Is your child starting college this fall? If so, you may be knee-deep in the many financial considerations that attend higher education. You're probably grateful if your child received scholarships, grants and other financial aid to help defray the cost — but not so grateful about potential tax exposure. When exactly is financial aid taxable and when is it not? Let's take a look.

When aid is tax-free

Scholarships and grants, including Pell Grants and Fulbright Grants, are generally treated the same from a tax perspective. If scholarship or grant funds are used by a degree-seeking student to pay for qualified education expenses at eligible education institutions, they *aren't* considered taxable income.

A degree-seeking student pursues studies for an associate, bachelor's or higher degree at an eligible education institution. Eligible institutions provide programs with full course credits toward college degrees, or they offer training programs for students seeking gainful employment in recognized occupations. These institutions also must have received a nationally recognized accreditation status.

Qualified education expenses include tuition and fees, as well as course-related expenses (such as books, supplies and equipment) required in a student's course of instruction. They don't include room and board, however. To qualify, expenses must be required of all students taking the particular course. Optional expenses aren't considered qualified.

When proceeds are subject to tax

If scholarship or grant proceeds are used for any external purposes, the money is considered unearned income and *is* subject to taxation. This includes funds left over after all qualified education expenses have been paid. Of course, students can use this money for other purposes, such as to pay for room and board, utilities, groceries or meals eaten out. But they'll have to pay tax on it when they file income tax returns.

It's important to note that qualifying payments received through the Department of Veterans Affairs (including the GI Bill) generally aren't taxable if used to pay for education or training. But if a student receives payment for teaching, research or other services that are required as a condition of receiving the scholarship or grant, this money *is* generally considered taxable income. Exceptions are made for services required by the National Health Service Corps Scholarship Program, the Armed Forces Health Professions Scholarship and certain other programs.

Payments received through the Department of Veterans Affairs generally aren't taxable if used to pay for education or training.

When the "kiddie" tax comes into play

Another potential issue is the "kiddie" tax. This tax originally applied to children under 14 years old with unearned income, but its scope has progressively increased over the years. Now, the kiddie tax applies to some college students — specifically, children who are claimed as dependents and are under 19 years old, or full-time college students between 19 and 23 years old who have at least one living parent and aren't married and filing joint tax returns with their spouses.

College students who meet one of these definitions and have unearned income worth more than twice the standard deduction amount for a dependent must complete IRS Form 8615 to determine how much tax is owed. The 2024 standard deduction for a dependent is $1,300 or the sum of $450 plus the individual's earned income, not to exceed the regular standard deduction.

Don't let it fall through the cracks

Right now you might feel a little overwhelmed by the financial details of sending a child to college. But don't let tax issues fall through the cracks. Consult an experienced financial advisor. ■

The NIIT is ensnaring more people. Are you one of them?

The net investment income tax (NIIT) has been around for more than 10 years, but the number of people subject to it has gradually more than doubled during that time. Why? Because the income thresholds that trigger the tax aren't indexed for inflation. As incomes rise with inflation, an increasing number of taxpayers are exposed to the NIIT. Here's how to minimize the threat.

Assessing your risk

The NIIT is an additional 3.8% federal tax on net investment income (NII) from items such as taxable interest, dividends, capital gains, rents, royalties and passive business interests. Certain types of income are exempt, including wages, income from a business you actively manage (except for trading financial instruments or commodities), tax-exempt interest, taxable distributions from IRAs and qualified retirement plans, and Social Security benefits.

It applies to individuals with modified adjusted gross income (MAGI) over $200,000, married couples filing jointly with MAGI over $250,000 and married people filing separately with MAGI over $125,000. These are the same thresholds that applied when the tax was established in 2013. Although NII includes capital gains, the tax doesn't apply to the tax-exempt portion of your net gain on the sale of a principal residence ($250,000 for single filers, $500,000 for joint filers).

To calculate your exposure, multiply your NII *or* the excess of your MAGI over the applicable threshold (whichever is less) by 3.8%. For example, if you're a joint filer with $100,000 in NII and MAGI of $300,000, your tax is 3.8% x $50,000, or $1,900.

Strategies for reducing NII and MAGI

In general, you can reduce NIIT by reducing your MAGI or by reducing your NII (which also reduces your MAGI). To reduce your MAGI:

- Increase tax-deductible contributions to traditional IRAs, 401(k) plans and other retirement plan accounts — all of which reduce gross income.
- Make qualified charitable distributions (QCDs) from a traditional IRA. If you're over age 70½, you can donate up to $100,000 per year directly from your IRA to a qualified charity. QCDs apply toward the amount of required minimum distributions you'd otherwise have to take, keeping those funds out of your gross income.
- Convert a traditional IRA into a Roth IRA, which can reduce your gross income in future years.

If you want to lower your NII (and also your MAGI):

- "Harvest" capital losses (or sell investments at a loss) to offset capital gains you've realized during the year.
- Reduce taxable interest income by investing in tax-exempt municipal bonds.
- Minimize dividend income by shifting investments into growth stocks that pay low or no dividends.
- Transfer income-producing investments to family members in lower tax brackets (provided the "kiddie tax" doesn't apply to them).

You may also be able to spread sales of highly appreciated investments over several years to minimize the amount of NII in any single tax year.

Small tax, big bite

A 3.8% tax may seem relatively insignificant, especially compared with federal income tax rates. But when you compare tax-equivalent returns on various investment alternatives — such as taxable vs. tax-exempt bonds — consider the NIIT. To ensure you're making the most tax-efficient decisions, discuss strategies with your financial advisor. ■

Your estate plan needs to reflect life changes

Estate planning isn't a "set it and forget it" proposition. You should review your plan regularly and update it to reflect changes in your personal or financial circumstances.

Personal and financial shifts

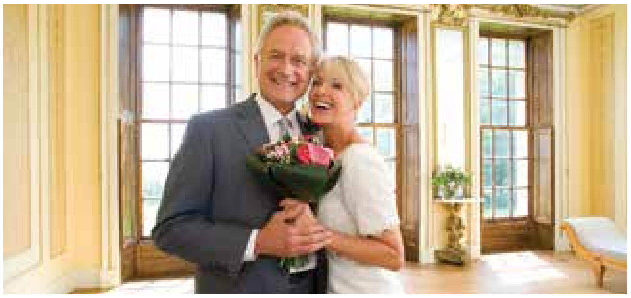
Perhaps your net worth has substantially increased or decreased or you've acquired or disposed of valuable assets. If you got married, you'll probably want to add your spouse to your plan. And if you got divorced, you'll likely want to remove your ex-spouse — as a beneficiary as well as a trustee. Other family changes that may prompt an update include having or adopting a child, becoming a grandparent, the death of a beneficiary, or changes in a beneficiary's financial circumstances.

It's also important to review provisions designating representatives charged with executing your plan. Say, for example, a person you named as executor, trustee, guardian or power of attorney holder has died, or is no longer capable or willing to serve.

Check and revise

Other life changes may make it necessary or desirable to update your plan. Determine whether any of these apply:

- ✔ You started a business venture and want to coordinate business succession planning with your estate plan.
- ✔ You're concerned about exposure of your wealth to creditors' claims or lawsuits and wish to increase asset protection.
- ✔ Your children have reached adulthood and you wish to name one or more of them as executor or give them powers of attorney.



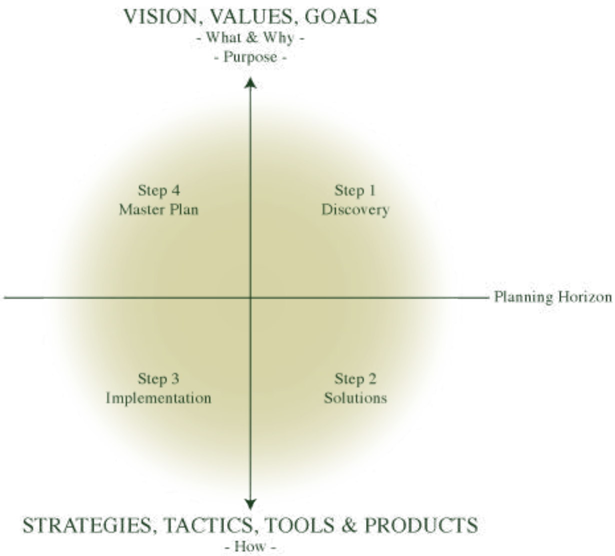
- ✔ A child, grandchild or other family member is or has become disabled and you wish to set up a special needs trust.
- ✔ Your child or grandchild divorced and you want to protect your wealth from ex-spouses.
- ✔ You moved to a new state with substantially different income or estate taxes.
- ✔ Your relationship with a beneficiary has soured and you wish to disinherit him or her.
- ✔ You decided to make sizable donations of cash or assets to charity.
- ✔ You've accumulated significant digital assets and need to provide for their disposition.
- ✔ Your health has declined and you want to change your preferences regarding life-sustaining medical treatment.

You should update financial and health care powers of attorney (or other medical directives), periodically, even if you're not naming a new representative. Some health care providers and financial institutions are reluctant to honor older documents.

Good idea

Even if nothing has changed in your life, it's important to review your estate plan every few years. Check in with your estate planning advisor for help. ■

About Integrated Financial



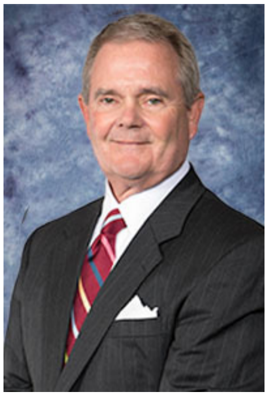
The Integrated Planning Process™

Over the last four decades, successful individuals, entrepreneurs, privately owned companies, foundations, and Fortune 1000 corporations have provided Integrated Financial with daily opportunities to address diverse estate, financial and business planning challenges.

Through this experience, we have developed a process that provides a strategic approach to addressing the important financial concerns that our clients encounter. This unique four-step process, The Integrated Planning Process™, assists our clients in gaining clarity and insights as to their Vision and Goals for themselves, their family, their business and their community.

We believe that success breeds success. While we acknowledge there are many qualified advisors to choose from, very few can match the combination of our experience, resources, perspective and success.

Meet Michael



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- Founder of Integrated Financial - Tulsa, Oklahoma
- BS/BA in Economics and Finance, University of Tulsa, Tulsa, Oklahoma
- National Association of Estate Planners & Councils (NAEPC) – Past Board Member

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Kirk G. Quaschnick
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- Accredited Retirement Plan Consultant (ARPC)
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