



NCM Client Notification

NOVEMBER 7, 2008

A publication of Northern Capital Management, Inc.

To our Clients:

Uhhhg! I wrote this tax notice last night.....and somehow it disappeared into the bits and bites black hole! I fear my first dispatch was better written.

We are in the process of initiating a series of trades which may appear spastic to clients. So, to make certain you do not think we have lost our minds (completely), below is our explanation. The program is referred to as **Capital Gain Tax Neutralization Project**.

While you may already be upset with your financial advisor, I can guarantee you will be furious when you receive your 2008 tax bill, unless we take action in the next six to eight weeks. Mutual funds potentially will experience one of the largest capital gain declaration years in recent memory. This is unbelievable given the likely 2008 portfolio losses. The cause for these distributions is rooted in how mutual fund accounting works.

A mutual fund is compelled to declare a gain when they sell a holding for more than they paid for it. For example, if a fund purchased Johnson & Johnson in 1965 and sold it this year at a substantial gain, a distribution to all shareholders who owned the fund on the "*date of record*" would result. Usually the *date of record* is near the end of the year when a majority of fund gains and losses have been realized for the year.

What many fail to understand is when a fund manager experiences a rash of sell orders, he/she is compelled to liquidate assets they own to pay off redeeming shareholders. With the significant volume of redemptions in September and October (both record months...in a bad way), many fund managers were forced to sell long time holdings where gains existed. Hence, the anticipated capital gain declarations for 2008.

In an effort to minimize and potentially eliminate these gains from hitting your tax return, we will be liquidating as many funds as possible where capital losses exist, as these can be used to offset gain declarations. Further, where possible we will attempt to miss the *date of record* entirely, in which case you will not have to report the gains at all. Here is how the strategy will work.....

Assume a fund has a *date of record* of December 4th. This means all shareholders as of that date will receive the gain. Remember, the "gain" is an accounting function only and has no bearing on the value of your account. Our objective will be to sell this fund in the next couple of weeks, hopefully at a capital loss (that sounded weird). We will swap the proceeds into a no transaction fee index fund with comparable investment characteristics to the one liquidated. We will remain out of the liquidated fund for 31 days so we qualify to write off the loss (referred to as the wash sale rule). Further, our objective is to be out of the fund on the **date of record** thereby missing the declaration entirely. After at least 31 days we will repurchase the previously liquidated fund to complete the round trip.

This program is a massive undertaking and will cause a spike in activity in your taxable accounts. Please recognize we will not be able to harvest every loss or protect from every gain distribution. However, it will be our primary objective to effectively reduce any tax liability which might be created by this bizarre market year accounting phenomenon.

If you have further questions or concerns, please e-mail or call.

Investment Committee
Northern Capital Management, Inc.