GREENLEAF TRUST

Perspectives

A Greenleaf Trust Newsletter

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William D. Johnston
President, Greenleaf Trust

Update

Each January for the past few years I've used this space to update clients and friends of Greenleaf Trust on our company, the year ahead for us, as well as a brief review of our economic forecast for the next twelve months.

The challenges of managing a rapidly growing company are many and we are certainly thrilled that we have the opportunity to meet those challenges.

As a Michigan Chartered Bank, Greenleaf Trust is now 13 years old. Historically, the combined lineage of Greenleaf Asset Management and Greenleaf Trust dates back to October of 1991, revealing 20 years of serving clients' financial planning, investment management, wealth management, trust administration and retirement plan administration needs.

The core pillars of our business culture which focus on no conflicts of interest, a team service delivery model, institutional continuous improvement and fiduciary excellence wrapped in a devotion to honest and honorable, have been rewarded in the marketplace. For the past thirteen years, we have earned a compounded annual growth rate of 21%. We are thrilled, as well as humbled by these results.

Current account statistics reveal that we now have almost 3,000 accounts and slightly in excess of 900 client relationships. Eighty-eight percent of those relationships are individuals, corporations, endowments and foundations, and 12% of our business is managing and administering qualified retirement plans for over 120 plan sponsors and 12,000 plan participants.

Our original team of seven employees has grown dramatically and our work force today stands at 73. As amazing as that seems, our staffing plan for 2012 will bring that total to 87 talented team members by mid 2012.

Although we will provide a much more detailed report in April when we issue our annual report, we are very likely to finish 2011 with $5.0 billion in total assets, $3.7 billion in discretionary assets and $18.0 million of excess capital on our balance sheet.

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Update, continued

To serve our existing client base as well as prepare for growth, we are adding to our team in the following divisions:

Operations Division:	2 Processing Technicians
	1 Tax, Reporting and Compliance Team Lead
Personal Trust Division:	3 Trust Relationship Officers
	3 Team Service Coordinators
Wealth Management Division:	1 Wealth Management Advisor
	2 Research Analysts
Retirement Plan Division:	1 Recordkeeping Analyst
	1 Retirement Plan Service Specialist
	1 Recorded Line Attendant
Administration:	1 Internal Auditor
	1 Chief Fiduciary Officer
	1 Senior Executive Vice President for Strategic Initiatives

Our selection and recruitment team has been very busy during the past six weeks and we are well on our way to filling the above positions with our target for completion being June of 2012 .

Growth and the addition of new talent also provide great internal opportunity for advancement and promotion. As the President of Greenleaf Trust I am extremely proud that we have been able to coach and lead our talent to grow in role impact, division impact and companywide contributions. This process results in our sustained ability to promote from within.

"As the President of Greenleaf Trust I am extremely proud that we have been able to coach and lead our talent to grow in role impact, division impact and companywide contributions."

It gives me great pleasure to share with you the following advancements:

Michael Odar, CFA, previously Executive Vice President and Director of our Wealth Management Division. Mike will now assume the newly created role of Senior Executive Vice President and Director of Strategic Initiatives. Mike will lead the execution of critically important initiatives across several divisions. He will also serve as Vice Chair of our Executive Leadership Team.

James Gray, CFA, previously serving as Assistant Director of Wealth Management and Director of Research. Jim will now assume the Executive Vice President and Director of Wealth Management position previously held by Mike Odar. Jim will continue to lead our research division as well as join our Executive Leadership Team.

Dan Rinzema, CFP, CFA, will continue in his role as a Wealth Management Advisor to Greenleaf Trust clients, and will be promoted to Vice President and Assistant Director of the Wealth Management Division where he will serve as leader of the Wealth Management Advisor Team. Dan will also join our Executive Leadership Team.

Kathleen Waldron performs a wonderful role serving as plan manager for all of our retirement plan sponsors. Kathleen has also led our recordkeeping analysts as they perform the regulatory required plan testing responsibilities. Kathleen will be promoted to Vice President and will join our Executive Leadership Team.

South East Michigan: The growth of our business in South East Michigan now requires that we staff our Birmingham office with a full client centric team. We are actively recruiting and beginning the selection process for what we know will be a truly dynamic team that includes a Trust Relationship Officer, Wealth Management Advisor, Team Service Coordinator and Business Development Officer in residence in our Birmingham office. We anticipate that the team will be well received not only by the South East Michigan market, but also by our existing client base in that region of our state.

We are, of course, thankful for the consistent growth in our business that allows us to budget for new talent to join our already great workforce. Beyond investing in human capital, we will continue our annual investment in technology, productivity and efficiency tools. During the past 13 years, we have doubled our size every 4.8 years and we expect to do so far into the future. Critically important to our growth strategy is to make certain that client service and attention to detail are never sacrificed. Our consistent investing in human capital as well as technology is our commitment to execute that strategy.

Those that attended our year end 2012 forecast seminar or requested a CD recording of it know that we are not forecasting a robust year either for our economy or equity markets.

We are less than 36 months into an economic recovery that we forecasted would be 60 months in duration and characterized by lower than average (2.5%) growth of domestic product.

Primarily due to global austerity measures due to significant structural deficits, we feel it will be a very challenging year for American exports. Coincidentally, sustained high unemployment and a continued weak housing market will add little fuel to consumer driven economic gains.

Once into an economic recovery, equity markets move forward in anticipation of growth of future earnings. Earnings are highly correlated to the prospects of economic growth.

In essence with little reason to forecast a higher GDP growth rate and with P/E multiples currently in the fair valuation range, we come to the conclusion that the economy will grow at about 2.1% and stocks will produce a 5-6% return inclusive of dividends. European concerns will remain with us and while the incidents are likely to diminish, volatility will still be with us. Incremental growth as we have experienced for the past 32 months will continue and over time will lead to improving the economic condition we are in. In the election year ahead of us, expect no legislative assistance for growth.

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Michael F. Odar, CFA
Executive Vice President
Director, Wealth Management Div.

"If a portfolio is never rebalanced, it tends to gradually drift from its target asset allocation as the weight of higher-return, higher-risk assets increases."

Rebalance Twice a Day or After Each Meal

The American Dental Association has recommended guidelines for brushing our teeth in order to reduce the adverse health risks associated with plaque. Automobile manufacturers provide us with guidelines on how often we should change the oil in our cars to reduce the risk of engine failure. There are recommended guidelines for almost every aspect of our lives and most are generally accepted. So, why hasn't a definitive resource for portfolio management provided us with guidelines on how often to rebalance our portfolios?

Well, there isn't a right or wrong number. What's really important is just that you do rebalance.

Rebalancing plays an integral role in the portfolio management process. If a portfolio is never rebalanced, it tends to gradually drift from its target asset allocation as the weight of higher-return, higher-risk assets increases. The primary reason to rebalance your portfolio is to ensure its risk characteristics are aligned with your risk tolerance. Misalignment can lead to a lot of unneeded angst. Studies have also shown that 80-90% of a portfolio's long-term return is determined by its asset allocation.

In a research paper by Vanguard in July 2010 titled *Best Practices for Portfolio Rebalancing*, they demonstrated that how often a portfolio is rebalanced has very little impact on its long-term risk-adjusted returns. They analyzed three different rebalancing strategies on a 60% equity/40% fixed income portfolio with risk and return data going back to 1926 (and ending in 2009). The first strategy, "time-only," was based on a set time schedule such as monthly, quarterly, annually, and so on. The average annual return and volatility measurement (standard deviation) were virtually the same for the monthly rebalanced portfolio and the annually rebalanced portfolio. The second strategy, "threshold-only," was based on a portfolio deviating from its target asset allocation by a predetermined minimum percentage, such as 1%, 5%, 10%, and so on. Again, the magnitude of the differences in the average annual return and in the volatility did not warrant the additional costs associated with a 0% threshold versus a 10% threshold. Finally, even a hybrid approach that involved aspects of both strategies did not highlight a clear beneficial method. Vanguard's conclusion was that for most broadly diversified stock and bond portfolios, annual or semiannual monitoring, with rebalancing at 5% thresholds, produces a reasonable balance between risk control and cost minimization.

At Greenleaf Trust, Wealth Management Advisors take more of a hybrid "time-and-threshold" approach to rebalancing client portfolios. Asset allocations versus target are monitored on a weekly basis and at the 5% threshold rebalancing actions are considered in the context of each client's unique situation.

Greenleaf Trust Named One of The Nation's Best and Brightest

BEST AND BRIGHTEST™ COMPANIES TO WORK FOR WINNER 2011

On December 13, 2011, the National Association for Business Resources (NABR) recognized Greenleaf Trust as one of the Best and Brightest Companies To Work For™ in the United States.

"Our goal is to consistently exceed the wants, needs and desires of our clients with an unparalleled degree of commitment. Achieving that goal is possible only through the collective efforts of our exceptionally skilled and dedicated team members. This prestigious national award is a tribute to them," said William D. Johnston, President and Chairman of Greenleaf Trust.

The winning companies were assessed by an independent research firm that reviewed key measures relative to other national winners. The measurements include Communication, Community Initiatives, Compensation and Benefits, Diversity and Multiculturalism, Employee Education and Development, Employee Engagement and Commitment, Recognition and Retention, Recruitment and Selection, Small Business and Work-Life Balance.

"Nationally recognized award recipients keep innovative human resource initiatives at the forefront of their company culture and make it a priority to consider their workforce as an essential aspect in their company success. Our Association is proud to recognize and honor these winning companies for this fine achievement," said Jennifer Kluge, NABR president.

"Our goal is to consistently exceed the wants, needs and desires of our clients… through the collective efforts of our exceptionally skilled and dedicated team members. This prestigious national award is a tribute to them."

Kevin E. Jawahir, CTFA
Trust Relationship Officer

Applicable Exclusion Amount and the Marital Portability Election

In December 2010, President Barack Obama signed the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 (2010 Tax Act). The 2010 Tax Act extended several provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), also known as Bush-era tax cuts, through December 31, 2012.

The 2010 Tax Act provides individuals an applicable exclusion amount of $5,000,000. The amount is indexed for inflation and the Internal Revenue Service (IRS) announced, in October of this past year, that the amount is being increased from $5,000,000 to $5,120,000 beginning in 2012. Please note, the annual gift tax exclusion amount remains at $13,000 per recipient for 2012.

"The 2010 Tax Act extended several provisions of the ...Bush-era tax cuts, through December 31, 2012."

Essentially, the applicable exclusion amount exempts a decedent's estate from federal gift and estate tax up to this amount. Below is a table detailing historical applicable exclusion amounts and corresponding estate tax rates:

Year	Applicable Exclusion Amount	Estate Tax Rate
2008	$2,000,000	45%
2009	$3,500,000	45%
2010	$5,000,000 (estates can elect out of estate tax)	35%
2011	$5,000,000	35%
2012	$5,120,000	35%
2013	$1,000,000 (unless amended by further legislation)	55%

Marital Portability Election

A distinctive characteristic allowed by the 2010 Tax Act is the portability feature. This feature "allows estates of married taxpayers to pass along the unused part of their exclusion amount, $5,000,000 in 2011 and $5,120,000 in 2012, to their surviving spouse." The unused part of the exclusion amount may be referred to as the deceased spouse unused election amount (DSUEA).

The DSUEA can be added to the basic amount of the surviving spouse. For example, if Mr. Smith passed away on December 31, 2011 and had only used $1,000,000 of his $5,000,000 exclusion amount, Mrs. Smith may now have exclusion amount of $9,120,000 [$5,000,000 – $1,000,000 + $5,120,000 (indexed for inflation)].

In order to preserve the DSUEA, there are four requirements to be met as prescribed by the IRS.

1. The executor of the decedent (the first spouse to die) must file a timely Form 706 (United States Estate Tax Return). The executor may also file Form 4768 to obtain an automatic six month extension.
2. If a timely Form 706 is filed by the executor, the presumption is effective that the portability election has been made regarding DSUEA.
3. If an executor chooses not to make the portability election, Form 706 will provide the steps required to give notice of portability non-election to the IRS.
4. The marriage portability election applies only to a decedent who passed away after December 31, 2010.

In many cases a Form 706 is not filed unless the estate is larger than the exemption amount. Regardless of the size of the estate, the requirements outlined above must be met in order to make certain that marital portability is allowed. This may cause the estate of the first spouse to die to incur additional costs (appraisal, legal, accounting fees, etc.) in order to preserve the election. It is recommended, however, that all estates of married decedents consider use of the portability election. If the election is made, the option is preserved. If the election is not made, it is lost. It should also be noted that the portability election can only be used with the spouse to whom you were most recently married.

As stated above, these changes are only temporary as the provisions of the 2010 Tax Act will expire on December 31, 2012. You should always consult with your professional legal and tax advisors concerning estate planning, gift and tax matters. This is particularly important in today's environment of constantly changing tax laws and regulations. With proper due diligence and effective utilization of your estate planning team, you can successfully navigate the intricacies of the 2010 Tax Act. We wish you a Happy New Year and a prosperous 2012.

"...the portability feature... 'allows estates of married taxpayers to pass along the unused part of their exclusion amount... to their surviving spouse.'"

Kathleen J. Waldron, QKA
Assistant Vice President
Retirement Plan Manager

“Some are even calling 2012 ‘the year of disclosure,’ with good reason.”

Fee Disclosure Requirements

The U.S. Department of Labor (DOL) has finalized the regulations requiring more detailed disclosures of underlying retirement plan expenses for both plan participants and service providers [the “408(b)(2) regulations”]. We have discussed these disclosures in a previous article, and as the New Year is upon us it is a perfect time to revisit this significant change this year. Some are even calling 2012 “the year of disclosure,” with good reason.

Service provider fee disclosures.

Retirement plan providers and third-party administrators serving as “Covered Service Providers” must reveal comprehensive information regarding the investment expenses and service provider fees to plan sponsors. This includes information on direct and indirect compensation they receive. Plan sponsors should use this information to determine whether the underlying service arrangement is appropriate for the plan and whether fees are reasonable. Thus, although service providers are tasked with developing the required disclosures, plan sponsors face fiduciary responsibility for ensuring that such disclosures are received, for reviewing them and ensuring that their arrangements with providers are reasonable. It is important to point out that Greenleaf Trust’s retirement plan service fees have always been very open, and are considered direct compensation; we have never entered into any indirect or related-party compensation arrangements.

Participant-level fee disclosures.

Employers, as plan fiduciaries, will be required to disclose what participants’ share of plan costs are. The new rules require plan sponsors to disclose the expense ratio of the investment funds offered in the Plan. The Department of Labor hopes fee disclosures will allow future retirees to comparison shop among a plan’s investment options. It is also assumed, but yet untested, that employers and workers alike will benefit from the increased transparency provided by these fee disclosure rules. Greenleaf Trust will take the lead in assisting our plan sponsor clients with the preparation and dissemination of the participant-level fee disclosures.

Fee transparency and full disclosure of fees has always been emphasized by Greenleaf Trust. Costs should be reasonable and in line with the quality of investments and supporting services plan sponsors and participants receive. Our goal has always been to assist every participant to retire well and this will only enhance this goal.

Additional information will soon be provided to Greenleaf Trust Retirement Plan Division clients regarding both of these important disclosures.

Dave P. Mange, CFA
Vice President
Senior Research Analyst

I Was in the Right Place, but it Must Have Been the Wrong Time

My title is a line from the 1973 pop music hit *Right Place Wrong Time* by "Dr. John." I wish that we had the technology to attach my incredible vocal rendition of the title line for you, in case you don't recall this classic hit, but some may be grateful that this is not possible in print at the present time. At the beginning of 2011, "everyone" knew that interest rates were due to rise in the US, but reality had its often contrary way with the expert forecasts. They were in the right place, but just too early, perhaps? The consensus wisdom from the same experts for 2012 is that rates will finally rise, just not by very much.

"At the beginning of 2011, 'everyone' knew that interest rates were due to rise in the US, but reality had its often contrary way with the expert forecasts."

In short, the conventional wisdom said that interest rates would rise in 2011, and they fell instead. The yield on the benchmark 10-year US Treasury bond began the year at 3.49%, while ending at 1.92%.[1] Our concern today will not be whether the similar 2012 forecast is correct; this is more of a "story problem" using simple math to determine the price effect of changing interest rates on bond prices.

According to Bloomberg's semi-annual survey of its favorite 70 or so economists, the 10-year Treasury bond yield will follow this gradual upward slope throughout the year: 2.19% by March 31, 2.35% by June 30, 2.50% by September 30 and 2.6% by December 31. On the scale of cosmic events, with a "one" being grass calmly growing in silence and a "ten" being earth struck by a meteor the size of Texas, this is only a 1.5 to a 2.0, but everyone likes it when the bond market is *not* the lead story for the year in review editions of news magazines.

Let's make our exercise simple by ignoring the quarter-by-quarter progression of rates, and simply use the beginning and ending numbers. All bonds can be described as having a specific "duration," which is a statistic that measures how that bond will react to changes—up or down—in interest rates. We will not go into the specifics of how the statistic is derived[2] other than to say that it is a combination of the time to maturity and the coupon rate (interest rate) of the bond. The 10-year Treasury bond currently has a duration of 8.9.

If the prevailing rate on the 10-year Treasury rises to 2.60% from the current 1.92%, as the consensus of learned economists predicts, that will be a change of 0.68%, or 68 basis points, as bond market participants speak of it. We can then multiply 0.68 (change in interest rate) x 8.9 (duration) to find how the price of the 10-year bond will change. Remember that rising interest rates cause bond prices to decrease, while falling interest rates cause bond prices to rise.

0.68 x 8.9 = 6.05%. In other words, the price of the 10-year Treasury bond would decline by 6.05% tomorrow if the interest rate rose by 0.68% tomorrow. This is only a small oversimplification.[3] However, the forecast is not for a change of 68 basis points tomorrow, the forecast is for the end of 2012. If that is true, the duration of today's 10-year Treasury bond will bleed off approximately 1 duration point to 7.9. Therefore, a better answer to our story problem would be an estimate that the price would fall 5.37% over the course of the full year. With 1.92% interest, the total return for the year would be approximately negative 3.45%.

A negative yield for a one year period on bonds would not be at all surprising, given how low interest rates are at present, but it might come as a shock to an entire generation of investors who have known only falling interest rates for the last 35 years or so. As we mentioned earlier, we do not know that this year's forecast is any better than last year's, but it is rather easy to model results bond by bond and across a portfolio as interest rates change.

Greenleaf Trust has managed the fixed income component of portfolios under management to limit duration risk. Even if rates do rise slightly in 2012 and beyond, most portfolios will have maturing positions to roll over into higher rates, and for those who hold bonds to maturity the worst that will happen is that the total interest received will be rising more slowly than the market. But, with rates as low as they have been, there is good reason to avoid excess duration risk. Better days may be coming to put new money to work in the bond market. The first priority is to avoid losses so that we have cash available to take advantage of better interest rates whenever they come along.

"… we do not know that this year's forecast is any better than last year's, but it is rather easy to model results bond by bond and across a portfolio as interest rates change."

[1] December 29, 2010 starting date to December 29, 2011 ending date based on deadlines for this article.

[2] Which we expect will be a popular omission, but if you actually would *like* to know, drop me an e-mail and I will gladly reply with the formula.

[3] We also need to account for the concept of convexity, with which we assume that only the rarest of readers is concerned. If this is you, we sincerely appreciate your interest and refer you to footnote #2 above.

Stock Market Pulse

Index	12/31/11	% Change Since 12/31/2010
SS&P 1500	290.12	1.75%
DJIA	12,217.56	8.35%
NASDAQ	2,605.15	-0.51%
S&P 500	1,257.60	2.11%
S&P 400	879.16	-1.73%
S&P 600	415.07	1.02%
NYSE Composite	7,477.03	-6.11%
Dow Jones Utilities	464.68	19.71%
Barclays Aggregate Bond	110.25	7.69%

P/E Multiples	12/31/11
S&P 1500	13.8
Dow Jones Industrials	12.7
NASDAQ	15.3
S&P 500	13.5
S&P 400	16.8
S&P 600	16.8

Key Rates

Fed Funds Rate	0% to 0.25%
T Bill 90 Days	0.02%
T Bond 30 Yr	2.89%
Prime Rate	3.25%

Current Valuations

Index	Aggregate	P/E	Div. Yield
S&P 1500	290.12	13.8	2.13%
S&P 500	1,257.60	13.5	2.22%
DJIA	12,217.56	12.7	2.52%
Dow Jones Utilities	464.68	NA	3.86%

Spread Between 30 Year Government Yields and Market Dividend Yields: 0.76%

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