

Best Practices for Investment Clubs

MARCH 2024



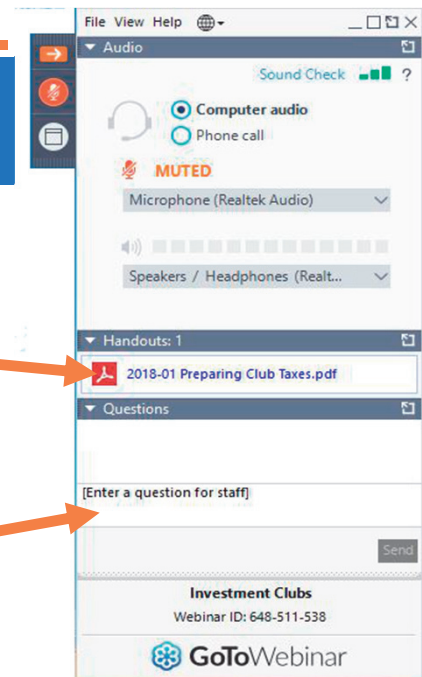
Doug Gerlach



Handout & Questions

Handout in PDF format is available in Handouts tab.

Type questions in Questions box.



In This Presentation



- Best practices for handling tasks related to investment club accounting.
- Best practices for efficiently operating an investment club.
- Best practices for using myICLUB for club accounting & operations tasks.
- Best practices for thoughtfully managing an investment club's portfolio.

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Complicated Isn't Better



- In nearly all areas of investment club accounting & management, keeping things simple brings great benefits.
- Instead of focusing on administrative tasks, clubs can devote fuller resources to company research & portfolio management.
- Keep club procedures **simple**.
- Keep club policies **reasonable**.
- **If it's not simple or reasonable, ask yourself "why?"**

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BEST PRACTICES FOR INVESTMENT CLUB OPERATIONS

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Your Operating Documents Rule



- Club's partnership agreement/bylaws should be followed in every situation (adding members, processing withdrawals, dates of valuations used for meetings & withdrawals).
- **Never deviate** from provisions of these documents, especially related to withdrawals.
- When necessary, update them.

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Update Operating Documents As Required



- Partnership agreement and/or by-laws can be revised as needed.
- If (especially after this presentation) you wish to update documents, go for it!
 - Partnership Agreement: Must be agreed & signed by all partners. Usually contains top-level requirements. Update document on file with brokerage if necessary.
 - Bylaws: Can be amended regularly, include specifics.

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Form as General Partnership, not LLC



- LLCs provide negligible extra benefits over general partnership for investment clubs but do create extra costs & reporting.
- New rules in 2023 from U.S. Dept. of Treasury require additional reporting for LLCs.
 - Rules aim to make financial crimes more difficult.
 - LLCs (but **not** general partnerships) must report "beneficial ownership information" (BOI) to Financial Crimes Enforcement Network (FinCEN) of Dept. of Treasury.
 - NOTE: There have been legal challenges to this new reporting requirement, with appeals currently underway.

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Understand Issues with Trusts as Members



- Partnerships with trusts as partners may **not** opt out of IRS Centralized Partnership Audit Regime.
 - These rules favor IRS & can cause current partners to be assessed penalties for liabilities incurred in past.
- If trusts are allowed, new members must be notified of liabilities they may be asked to assume if IRS has any issue with past tax returns.

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Don't Try to Keep Members "Equal"



- "Equal ownership" of partners is impossible to maintain fairly over time using unit value accounting.
 - Timing of member payments & transactions affects each transaction, so late or missed payment can unfairly disadvantage some members.
- myICLUB does not support clubs attempting to fudge books to accommodate "equal" ownership.

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Rotate Officer Positions



- Avoid “lifetime” officers.
- Many clubs have policy that all members must eventually serve in every officer position.
- This spreads workload but also contributes to better understanding of investment, portfolio management, accounting, & tax preparation tasks.

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Make Education a Priority



- Investment clubs should be learning opportunities.
- Each meeting should ideally contain learning component.
- Assign/elect one member to coordinate presentations from members or outside guests.
- Consider broad range of financial topics, not exclusively concerned with club investment opportunities.

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BEST PRACTICES FOR USING MYICLUB.COM

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Use Online Collaborative Tools



- Many clubs shifted to online communications tools during pandemic.
 - Offer easy way to conduct operations without meeting in person.
- Consider utilizing these to:
 - Replace in-person meetings.
 - Add additional meetups in between regular meetings, for education or portfolio management tasks.
- Explore myICLUB's Voting & Email List functions & implement into club's regular operating procedures.

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Stop Printing Paper Reports



- myICLUB.com provides view-only access to all club data & reports for all members.
- Members can view, download, save or print own copies.
- Treasurer can use provided link to email members to remind them to view reports before meeting.

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Customize Your myICLUB Club Website



- Admin can add club logo which appears on site and reports.
- Go to **Accounting > Utilities > Update Club Settings** to upload logo or choose from myICLUB graphics library.

myICLUB

Your Clubs:
All-World Investors

Home Accounting Reports Watch List Taxes People Voting Discussions

All-World Investors

Club Portfolio What's this?

Expiration Dat

Your myICLUB subscrip (BI) clubs receive a \$52 registration pays for itse

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Use myICLUB File Storage



- Save stock studies, financial statements, meeting minutes in File Storage library of myICLUB.
- Can set in People profiles who can upload/organize/delete files & folders.
- Also includes **Free Resources from myICLUB** library, such as Quick Start & User Guides.

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Backup Club Data Regularly



- Get familiar with myICLUB Backup Manager.
- myICLUB automatically makes backups if you don't, but don't rely on this.
 - We back up all data regularly to protect from server hardware/software failure, but Backup Manager protects you from yourself!
- Have regular backup routine to save accounting data online & off.
- Use "File Takeout" feature in File Storage to download all files.
- Make redundant copies of all backups & store in different secure locations.

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Review myICLUB People Permissions



Member Position and Permissions

Role:

Allow this member to: **Manage Treasurer Duties**

Record accounting information / receive renewal notices

Manage Club Details and Members

Modify club name and settings

Invite and eject members

Edit member profiles and permissions

Manage Voting, StockWatchers, and Watch List

Create and delete ballots

Edit Watch List and StockWatcher assignments

Manage/Access Message Board

Access membership discussions*

Post to message boards*

Delete message board postings

Create and delete message boards

Manage/Access File Storage

Upload files*

Delete files uploaded by other members

Create and delete folders

Make files public

Manage Calendar

Create, edit, and delete events

* Default permissions for all members.

- Admin can set permissions & positions for all members in their People profiles.
- Customize to allow members to accomplish certain tasks.
- **Do not** give all members Treasurer Duties – this will allow anyone to delete/change transactions.

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BEST PRACTICES FOR INVESTMENT CLUB ACCOUNTING

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Create No More Than 1 Valuation per Month



- **Don't create "temporary" or "unofficial" Securities Valuation** just to reconcile your brokerage statement,
- **Don't create "temporary" or "unofficial" Securities Valuation** before processing member withdrawal.
- Only other valuation in year should be year-end Valuation created on 12/31.
- Follow club operating documents with respect to how club's portfolio is valued.

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Create Valuations Close to Meeting



- Monthly Securities Valuations should be created as close as possible to club meeting.
 - Use prices from most recent market close.
 - Members should be able to refer to Valuation Statement & other reports during meeting for current stock prices.
- Most clubs shouldn't need to align valuations with brokerage statement.
 - Use myICLUB Reconciliation Wizard check books against brokerage.
 - If you insist on using Securities Valuation to reconcile books to brokerage, better to switch club meeting date to accommodate.

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Reconcile Books Each Month



- Take time to make sure brokerages & bank accounts match club's books **each & every month.**
- Tiny errors compound & become increasingly difficult over time to find & fix.
- myICLUB Reconciliation Wizard helps match club records to bank & brokerage.
- Make sure all transactions are entered, number of shares for each security match, & cash balances match.
- Portfolio value is not important to match if dates of myICLUB valuation & brokerage statement differ.

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Don't Use Dividend Reinvestment.



- Dividend Reinvestment creates 2 transactions: receipt of dividend income & buy of shares.
- Because of IRS rules for brokerage reporting of capital gains, **additional purchase lots from reinvested dividends can make tax prep more difficult.**
 - Each lot in club's books must have its gains/losses reconciled to Form 1099 reported to IRS by brokerage.
 - There will be **lots of additional pain** when IRS Form 1065 tax return is prepared.
- When selling, clubs often neglect to turn off dividend reinvestment & create wash sale that **further complicates tax return preparation.**
- BetterInvesting rules only say to "reinvest earnings," **not** to reinvest in same stock that paid them.

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Don't Enter "Cost per Share"



- When recording buy & sell transactions, let myICLUB.com calculate cost per share.
- **Don't worry** if cost per share doesn't match brokerage statement or confirmation.
- **Total cost & number of shares** is what's important to match.

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Don't Use Member Fees to Cover Expenses



- **All member payments should be used to purchase units.**
- Fees should only be used in penalty situations, such as for bounced checks.
- Even worse: collecting member fees to cover equally-allocated expenses penalizes members with lesser levels of investments in club.

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Don't Charge Late Fees



- Collecting & recording fees only **makes treasurer's job harder.**
- Members who miss making monthly payment only hurt themselves.
- Club's portfolio value should move up over time, so late members will be buying in at higher values.

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Always Allocate Expenses by Ownership



- IRS rules say that expenses should be **allocated by percentage ownership** *unless* partnership agreement specifies otherwise.
 - You wouldn't allocate profits equally!
- Can cause problems if you then collect member fees to offset those expenses.
- *Alternative: Keep expenses off club's books entirely.*

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Don't Unfairly Inhibit Withdrawals



- Withdrawal fees are no longer considered reasonable.
- **Do not charge withdrawal fees** in excess of any actual costs.
- **Don't "lock in" members capital** for designated periods after joining.
- It's each partner's money, so you shouldn't restrict access.
 - If member needs cash or is no longer interested in being member, it works to no one's favor to make them remain in club.
- You can add suggestion/understanding to partnership operating documents, but avoid hardline requirements.

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Use "Member Withdrawal Scenario Calculator"



- This unique myICLUB tool determines best options for paying out full & partial member withdrawals with stock or cash, to **benefit of both club & member**.
- Some withdrawals are best paid out in cash, others in stock.
- Some withdrawals should **never** be paid in stock.
- Calculator will prevent options & list in preferred order.

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Use Withdrawals to Clean Up Portfolio



- Nearly all clubs have holdings that **probably should be sold due to underperformance or uncertain prospects.**
- For any withdrawal, selling shares to raise cash & that generate capital loss can be effective portfolio management strategy.
 - Consider sale to be “temporary.”
 - Revisit stock in 30+ days to consider repurchase (to avoid wash sale).

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Stop Getting Paper Statements



- Sign up for **electronic bank & brokerage account statements & confirmations.**
- Good practice to store these as PDFs in club’s File Storage area for all members to view.

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Have Members Pay Electronically



- Members can send funds electronically to club's account via ACH or online bill pay.
 - Contact bank & brokerage for information on process.
- Treasurer can use "penny method" to assign different cents amounts for each member to identify deposits.

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Don't Treat Money Markets as Securities



- Money Market dividends are treated as interest by IRS, so **handling in myICLUB as Security with Dividends is unnecessary.**
- May help reconciling books, **but** creates extra transactions since money market shares have to be sold whenever cash is used to buy security.
- myICLUB will show Money Market Securities in **Securities** portion of Valuation, not as **Cash**.

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Don't Enter Transactions on 12/31



- Keep last day of year clear for annual Allocation Of Income & Expenses to members.
- Move any 12/31 transactions to 12/30
 - Add note that has actual transaction date.
- For dividends paid in January but specifically designated to prior year, enter on 12/30 with note.
 - This way they will be picked up in tax reporting.

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Audit Club's Books Each & Every Year



- Convene **Audit Committee of club members each year.**
- Committee should review books for accuracy & completeness.
- Can catch errors before they magnify.
- Introduces other members to treasurer tasks.
- Helps create mandate for simplified club operations & accounting best practices.

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File Tax Returns Every Year on Time



- March 15th is current IRS deadline, & penalties can add up fast for late or missed filings.
- IRS e-Filing from myICLUB makes it easier than ever!
- Many states also require filing, so check with your state to be sure you're following their laws.
- **Some states require filings from non-resident partners even if partnership is outside state.**

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Train Next Treasurer Now



- Assign/elect **Co- or Assistant Treasurer.**
 - Can take over some tasks, or follow along as Treasurer manages books.
- Don't wait to hand over reins, potentially during crisis.
- Some clubs have rule that every member must eventually serve in every officer position.
- myICLUB.com makes it easy to change Treasurers or add Co-Treasurer.

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BEST PRACTICES FOR PORTFOLIO MANAGEMENT

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Stick to Common Stocks



- Very difficult to determine portfolio's true diversification when you hold securities like mutual funds & ETFs that hold hundreds/thousands of stocks.
- Also impossible for members to effectively integration scattershot club portfolio into their personal portfolio management.
- Use club's educational focus to experience investing in many different types of companies, including those in difficult-to-analyze industries (financials) or categories (small-caps).
- In addition, many non-stock securities create problems for treasurer.

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Avoid “Headache” Securities

- Some securities create problems for treasurers when preparing tax returns & should be avoided:
 - Gold/Precious Metals/Commodities (or ETFs that hold).
 - Real Estate Investment Trusts (REITs).
 - Business Development Companies (BDCs).
 - Royalty Trusts.
 - Publicly Traded Partnerships (PTPs).
 - Master Limited Partnerships (MLPs).
 - Cryptocurrency (or ETFs that hold).
 - Equity options.
- Best to avoid these in club portfolio & **stick to common stocks**.

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Understand Issues with Foreign Companies



- Changes to IRS rules around foreign income have created additional reporting requirements by partnerships.
- Now, distributions paid by any non-US company must be reported on Form 1065 with country of origin & amounts.
 - If amounts exceed limits, then Schedule K-2 (sent to IRS) & K-3 (for each partner & sent to IRS) must be prepared each year.
- Some clubs may wish to avoid non-US companies due to these difficulties.

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Link Club Stocks to Member SSGs



- Members can link Stock Selection Guides from BetterInvesting's SSG Plus to stocks they have been assigned in myICLUB.
 - When members update study data, prices, & judgment in SSG Plus, myICLUB reports are updated.
- This streamlines portfolio management considerably!
- Require each member to have BI membership & access to SSG Plus to enable this feature.

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Develop Club's Stock Watcher Routine



- Use Stock Watcher system to have members regularly update evaluate performance of companies in your portfolio.
- Members should report on followed stocks at least 4 times a year.
- **Do not** rely on price changes for insight into how well an investment is likely to do in future.
 - Focus on fundamental progress company is making.

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Build a Diversified Stock Portfolio



- Diversify portfolio by:
 - Company size (good target: 25% small, 50% mid, 25% large).
 - Sector & industry (good target: at least 7 sectors & each stock in different industry).
- Diversification helps protect portfolio from damage caused by underperforming stocks, industry downturns, & economic swings.

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Don't Overweight with Large-Caps



- Too many clubs focus on “brand name,” consumer-facing companies.
 - These large-caps can add stability, but they also deliver lower returns over time.
- Small & mid-sized companies are more volatile but also will boost returns above overall market averages.
- Venture outside comfort zone to research companies in non-consumer industries, smaller companies.

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Don't Hold Tiny Stock Positions



- Any stock less than 3% of club's portfolio is **not helping your returns.**
- Either sell position or add to it.
 - Sometimes is better to add shares of company with which you are familiar even if at upper limit of buy zone.

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Don't Own Too Many Stocks



- Research shows that a portfolio of 20-30 stocks provides optimal levels of risk & reward.
- Own as many as your membership can follow.
- Too few stocks increases risk.
- Too many stocks causes returns to tend to regress to market averages (in which case you might as well buy an index fund!).

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Keep Costs Low



- Every dollar you spend in commissions & expenses reduces overall returns.
- Investment expenses are no longer deductible for members.
 - Even when they were “deductible,” few individuals got any tax benefit.

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Review Performance Periodically



- Use myICLUB benchmark report to compare club to broad market index.
 - Don't obsess over this or CAR on Valuation Statement.
 - Annualized returns are highly distorted when large changes occur in short periods.
 - Look at performance perhaps once or twice a year.
- If in first few years of operation you don't beat market, don't sweat it.
 - Every investor & club has learning curve, & startup expenses often eat up capital at onset.

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FINAL THOUGHTS

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Putting Our Best Practices to Work



- Longstanding clubs may use different policies, but there is always room for improvement.
- Don't reinvent the wheel!
 - There are good reasons why our best practices have been shared with clubs.
 - Problems arise when clubs try to “get fancy” or come up with new “solutions” that only get them into trouble.

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For More on Club Operations & Accounting

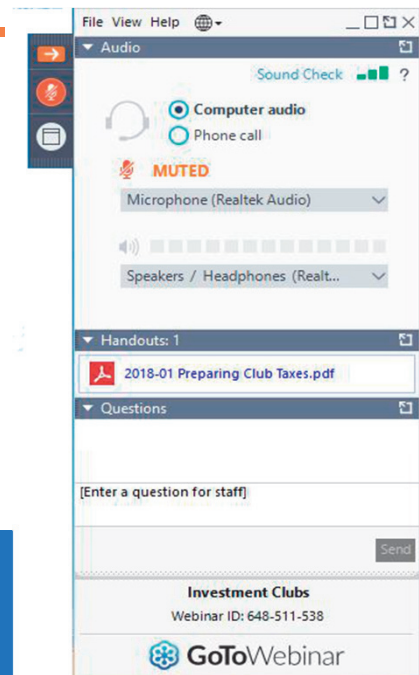


- Visit the ICLUBcentral YouTube channel for webinar replays on topics like:
 - Disaster preparedness.
 - Tax preparation.
 - IRS audit rules.
 - Training new treasurers.
 - Backup procedures.
 - And more.
- Visit www.YouTube.com/ICLUBcentral and www.myICLUB.com.

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QUESTIONS

USE QUESTIONS BOX IN WEBINAR APPLET



Thank You!



Doug
Gerlach



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