

ACCOUNTING FOR TAXES

Turning to ETFs to Help Manage Your Bottom Line

RECEIVING TAXABLE CAPITAL GAINS DISTRIBUTIONS ON YOUR MUTUAL FUND INVESTMENTS? TIME TO CONSIDER ETFs

First, the Bad News

The year-end reality for mutual fund investors can be the potential exposure to an entire year of capital gains from mutual fund securities sales, regardless of when they invested in the fund.

Next, the Good News

There is a solution that may help minimize exposure to capital gains through exchange-traded funds (ETFs). Offering a variety of benefits to investors, an ETF's tax-efficient structure, as outlined below, is one of its most prominent benefits when compared to open-end mutual funds. So whether you are anticipating a year-end distribution announcement from your mutual fund or reviewing the capital gains figures on your 1099, isn't it time to ask your advisor about the potentially tax-efficient structure of ETFs?

ETFs (EXCHANGE-TRADED FUNDS)

Portfolios of securities that trade like individual stocks on major stock exchanges and can be bought or sold throughout the trading day. Constructed to track the holdings and performance of a defined index of securities, before expenses, ETFs enable investors to purchase a cost-efficient and more widely varied portfolio of securities than an investment in an individual security.

The Typical Structure of an ETF—Designed for Tax Efficiency and Lower Expenses

Constructed to track the holdings and performance of an index, many ETF portfolios experience relatively lower turnover, resulting in fewer gains to pass on to investors. Periodically, an ETF rebalances its portfolio to account for security changes in the index. To the extent possible, rebalancing is handled in-kind, which is generally not a taxable event to the ETF and its ongoing shareholders. However, in some cases, the ETF must sell securities that are no longer represented in the index for cash and buy other securities which are new to the index for cash. These cash transactions could give rise to capital gains which might need to be distributed to shareholders.

In contrast, actively managed mutual fund portfolios may continually change based on the managers' research. This structure may not only result in higher expenses for the managers' efforts, but may also result in capital gains for investors from securities sales as holdings are removed from the portfolio. Keep in mind that some mutual funds are managed with the goal of achieving tax efficiency.

An In-Kind Creation and Redemption Process—Helping to Minimize the Potential for Taxable Events

The way both small and institutional investors transact with ETFs compared to mutual funds may also help minimize taxes.

RETAIL INVESTORS BUY AND SELL SHARES OF AN ETF ON

A STOCK EXCHANGE. This activity generally should not create significant tax implications for the ongoing ETF shareholders, though the transactions may result in brokerage costs and other transactional fees for the investor placing the trade.

This contrasts with the mutual fund purchase and redemption process which occurs directly between the investor and the fund. If the fund receives a large number of redemption requests (typically during times of significant market volatility), the fund may have to sell portfolio securities to cover the requests if it doesn't have enough cash on hand. If gains are realized on the securities sales, the transactions create taxable events for all remaining mutual fund shareholders, generally resulting in capital gains distributed at year end.

CONVERSELY, INSTITUTIONAL INVESTORS TYPICALLY BUY AND SELL DIRECTLY FROM AN ETF THROUGH IN-KIND

TRANSACTIONS. An in-kind transaction, which is the exchange of stocks versus cash, where typically the lowest cost basis stock is transferred out and is not generally a taxable event for the ETF and its ongoing shareholders. There can be a comparatively small exchange of cash at redemption which is considered a taxable event to the receiving party, but does not generally impact the ETF. This in-kind creation and redemption process helps to significantly reduce the number of taxable events incurred by an ETF compared with open-end mutual funds.

>> FOR MORE INFORMATION ABOUT THIS PROCESS, [CLICK HERE TO VIEW 'LOOKING FOR TAX EFFICIENCY? CONSIDER AN ETF'](#)

The table below compares the treatment of potential taxable events in ETFs and mutual funds.

| TAX EFFICIENCY COMPARISON BY EVENT FOR ETFs AND OPEN-END MUTUAL FUNDS | | |
|---|--|--|
| Potential Taxable Event | Exchange-Traded Funds | Open-End Mutual Funds |
| Shareholder Redemption | No. Redemptions are generally handled in-kind for large investors and the lowest cost basis stock is transferred out. In-kind transactions are not generally taxable events for the ETF and its ongoing shareholders. | Yes. If securities are sold at a gain to cover redemptions, the remaining shareholders will receive capital gains distributions at year-end which represent a taxable event. |
| Portfolio Turnover | Not always. Similar to shareholder redemptions, rebalancing is handled in-kind to the extent possible and those transactions are not generally a taxable event for the ETF and its ongoing shareholders. In some cases, the ETF must sell securities no longer in the Index for cash and buy other securities which are new to the Index for cash. Any cash transaction represents a taxable event for the ETF. | Yes. Open-end funds generally buy and sell holdings in an effort to generate favorable returns for shareholders. If there are gains realized because of this turnover, shareholders will receive capital gains distributions at year-end which represent a taxable event. |
| Corporate Actions (Acquisitions, stock splits, etc.) | Not always. Similar to shareholder redemptions, the sale of securities due to corporate actions is handled in-kind to the extent possible and those transactions are not generally a taxable event for the ETF and its ongoing shareholders. In some cases, the ETF must sell securities for cash and buy other securities for cash. Any cash transaction represents a taxable event for the ETF. | Yes. Open-end fund managers may choose to sell part or all of the stock of a company that has merged or been acquired if the new company no longer fits their investment thesis or represents a combined position that is larger than allowed by the fund's prospectus. If the securities are sold at a gain, shareholders receive capital gains distributions at year-end which represent a taxable event. |

The Bottom Line

Taxes have a direct impact on an investor's long-term growth of capital and can erode an investment's return if not properly managed. No matter how well your investments perform, the return is only as valuable as the amount kept after taxes. Adding ETFs to your portfolio may be a lower-cost, more tax-efficient solution regardless of which direction the market may be heading.

As with mutual funds, Guggenheim Funds ETFs are required to distribute portfolio gains to shareholders by year-end. Certain traditional mutual funds may also be tax efficient. The above material is not intended to be tax advice. The tax consequences of distributions may vary by individual investor. Investors should consult their tax professional or financial advisor for more information with regard to their specific situation as Guggenheim Fund Distributors, Inc. does not offer tax advice.

RISKS AND CONSIDERATIONS The information contained herein is for educational and illustrative purposes and should not be regarded as tax advice. While ETFs have some tax efficient attributes, their structure was not designed with tax benefits as an objective. If shares of an ETF are sold at a price other than their purchase price, the transaction will typically represent a taxable event. This information does not represent an offer to sell securities of Guggenheim Funds ETFs and it is not a soliciting an offer to buy securities of Guggenheim Funds ETFs.

There can be no assurance that an ETF will achieve its investment objective(s). There are risks involved with investing, including, but not limited to, investment risk, which is the possible loss of the entire principal amount you invest. There is a risk that the value of the securities held by an ETF will fall due to general market and economic conditions, perceptions regarding the industries in which the issuers of securities held by the ETF participate, or factors relating to specific companies in which the ETF invest. Investing in non-U.S. issuers may involve unique risks, including, among others, greater market volatility than U.S. securities and less complete financial information than for U.S. issuers. ETFs are not "actively" managed and therefore, would not necessarily sell a stock because the stock's issuer was in financial trouble unless that stock is removed from the index. ETFs are also subject to potential tracking errors and their returns may not match the returns of the indices. ETFs that focus

on micro-, small- or medium-sized companies generally experience greater price volatility and risk than investing in more established companies. ETFs that concentrate in a particular industry or sector can be more susceptible to factors affecting that industry or sector and can cause greater price fluctuations than the overall market. An investment in an ETF involves additional risk including but not limited to: Non-Correlation Risk, Replication Management Risk, Issuer-Specific Changes, and Non-Diversified Fund Risk. In addition to the risks described above, there are certain other risks related to investing in ETFs. These risks as well as additional risks specific to a particular ETF are described further in each ETF's respective prospectus. Please read the prospectus for more detailed information.

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Consider the investment objectives, risks, charges and ongoing expenses of any ETF carefully before investing. The prospectus or summary prospectus, if available, contains this and other relevant information. Please read the prospectus carefully before investing. To obtain a prospectus, visit www.guggenheimfunds.com or contact a securities representative or Guggenheim Funds Distributors, Inc. 2455 Corporate West Drive, Lisle, IL 60532, 800-345-7999.