



CYPEN & CYPEN NEWSLETTER for September 19, 2019

Copyright, 1996-2019, all rights reserved
Stephen H. Cypen, Esq., Founding Editor
Robert D. Klausner, Esq., Senior Editor

Never Forget September 11, 2001
and
Always Remember May 2, 2011

1. INVESTMENT UPDATE: HOW DO PUBLIC PLANS VALUE THEIR ASSETS?

A new government accounting standard requires state and local pension plans to categorize assets based on the method used to determine the fair market value. Level 1 includes frequently traded assets like equities. Level 2 includes less liquid assets like corporate bonds. Level 3 involves appraisals like real estate. For assets that lack a “readily determinable” fair market value, plans can instead use the net asset value (NAV) per share. However, it is possible to assign these “NAV assets” to Levels 1, 2, or 3 by matching them with comparable assets in each level. This reallocation shows that about one quarter of total assets are likely valued based on appraisals (Level 3), which, by definition, are more subjective. See full brief [here](#). Jean-Pierre Aubry and Kevin Wandrei, State and Local Pensions Plan Number 68 (SLP#68), Center for Retirement Research at Boston College, September 2019.

2. ARE YOU READY FOR MEPS?

As the industry once again seems to stand on the brink of action with regard to multiple employer plans (MEPs), we asked Summit Insiders to tell us where they stood on open MEP or asset pooling arrangements. MEPs continue to be a hot topic of conversation, promising to help close the current coverage gap, provide a more efficient means for more employers to offer a retirement plan (which would help close the coverage gap), provide additional ways for providers to (more profitably) serve that market (and thus to help close the coverage gap) – well, you get the point. Little wonder that the concept has been hotly debated since 2012, when the DOL released Advisory Opinion 2012-04A clarifying its stance that open MEPs (that is, those open to any adopting employer rather than closed to a select group of employers) were not single plans under ERISA but rather a collection of single plans for each adopting employer. More recently, a directive to explore the opportunities to expand retirement plan access was issued by President Trump to the Labor Department, and versions of open MEPs (renamed “pooled employer plans,” or PEPs) have been included in recent legislative proposals, including the SECURE Act, which was approved by the House of Representatives in May, and the Retirement Enhancement and Savings Act (RESA) currently pending in the Senate. For the most part, respondents to the 2019 NAPA Summit Insider seemed to be in a “wait and see” mode regarding MEPs – and who can blame them, considering the fits and starts with these proposals. In fact, a slim plurality (36%) said they were “looking to sell if ‘open MEP’ officially passes.” That said, nearly as many (34%) seemed ready to go, indicating they wanted to “learn more about asset pooling” to scale their practice. And as it turns out, 15% were currently selling asset pooling arrangements – though that was matched by the 15% who said they “don’t see any advantages or understand the opportunity.” NAPA Net Staff, National Association of Plan Advisors (NAPA), September 12, 2019.

3. BACK TO SCHOOL WITH SOCIAL SECURITY:

It typically takes people a lifetime of planning to reach their retirement goals. The earlier young workers know about saving for their future, the better chance they’ll have at achieving a comfortable retirement. This is why Social Security has created a resource specifically for teachers and students. Our Information for Educators page contains a toolkit with information and resources to educate and engage students on Social Security programs and services. Within the toolkit, you’ll find:

- Two lesson plans with objectives
- Infographics and handouts for each lesson plan
- Links to Social Security webpages
- Talking points

- Quiz questions and answers

It's important for students to understand why Social Security was created and why it is essential to their lives today and in the future. This knowledge and understanding will provide students a strong base on which to build their financial future. You can access the [webpage and toolkit](#) on our website. Young workers can also see how [Social Security directly relates to them](#). Encouraging young people to save now for long-term goals that are decades away can be somewhat difficult. Let them know they have a better chance of realizing their dreams if they start planning and taking action early. And also let them know that they can share this information with friends, both in person and on social media. Darlynda Bogle, Assistant Deputy Commissioner, Social Security Administration, September 12, 2019.

4. THIS MAN SPENT DECADES TEACHING RETIREMENT PLANNING. HERE'S WHAT HE LEARNED FROM PLANNING HIS OWN:

Like many on the cusp of retirement, David Littell felt excited and a little nervous. But the 65-year-old differed from his peers in one key way: He spent the bulk of his career teaching retirement planning to financial advisors. Littell is a Professor Emeritus at the American College of Financial Services, where he co-created the [Retirement Income Certified Professional®](#) designation. In other words, he's a pro at one of the most complex tasks retirees face: turning a lump sum of savings into a reliable income stream that will last for life. And as he approached retirement himself, Littell discovered some key differences between what the textbooks say and the way things play out in real life. "In financial planning, we tend to think it's all about the numbers," says Littell, of Ardmore, Pa. "But I want to own the emotions. The idea that you don't have a paycheck anymore is rather terrifying." He's addressed this fear in his planning process. Here's what Littell has learned by finally living what he's taught all these years:

Start with Something

Financial advisors love to ask their clients detailed questions about their future plans: When are you going to retire? Will you work in retirement? If so, how much? In reality, "it's hard to nail that down until you're close to it," Littell says. "I've changed my plans four or five times." For starters, you don't know how your health will hold up. Some 43% of workers retire earlier than planned, and of those 35% stop working due to a health problem or disability, according to the Employee Benefit Research Institute. Also, while you're still working full-time, you're probably not looking for a part-time job to supplement your retirement income. So you don't know how feasible it is to get the kind of part-time work you want, or how much you might earn once you find it. Alternatively, if you'd rather continue working for your former employer on a part-time or consulting basis, you won't

likely broach the topic with them until you've given your notice. All this means that it's hard to have real numbers to plug into retirement income calculations in advance. Yet that doesn't mean you shouldn't try, Littell says. There's a good reason advisors ask all these questions, to try to make accurate projections of your retirement income. It's helpful to know how much you'll have coming in, to make sure it's enough to meet your needs. (To ballpark those needs, Littell suggests a simple method: [use your most recent paycheck as a proxy for the retirement income you'll need each month](#) -- assuming, of course, that you live within your means and aren't racking up credit card debt to fund your lifestyle.) So go ahead and make some assumptions, and do your calculations based on those. But understand that estimates are just that, and are subject to change. Revisit your plan regularly, and make sure the numbers are going to work before you give up your full-time gig. "People should think really carefully before they leave full-time work," Littell says. Many people get tired of the grind and let their emotions govern the decision of when to quit, he says. But if you leave the workforce and then regret your decision, it's very hard to re-enter at the same salary with the same benefits. For his part, Littell recently cut back to working three days a week and plans to further reduce his hours as he shifts to a consulting role early next year.

Listen to Your Gut

Littell's father lived to age 104. Aware he might have similar longevity, Littell didn't want to risk outliving his savings. So he bought several annuities, [insurance products that turn your lump sum into guaranteed income for life](#). Financial advisors commonly recommend that clients use annuities to cover their essential spending. This way, all of your necessary needs will be covered by a "floor" of guaranteed income, and you can use your 401(k) or IRA withdrawals for discretionary fun. The logic behind this strategy is that, if stocks take a dive, you can always curtail your travel plans, but you can't suddenly stop paying your mortgage or your Medicare premiums. To determine your essential spending, you would tally up what you pay for housing, health care, food and other necessary categories. Then, you calculate how much of the total would be covered by Social Security and any pensions you might have. An annuity or annuities would be used to cover any shortfall. But Littell didn't go through this exercise. Instead, bought annuities with the percentage of his portfolio that he felt comfortable parting with: about 25% of the total. Many consumers balk at annuities because they reduce your liquidity. Littell was willing to give up control over a quarter of his portfolio in return for guaranteed income, and staying within that comfort zone -- rather than imposing textbook calculations -- helped him execute that strategy. "The intellectual and the reality didn't match very well," he says. "The reality for me was, how much are you willing to give up?" He's deferring claiming Social Security until age 70, and he estimates that once he reaches that age, about 75% of his essential and discretionary needs will be covered by guaranteed income. The annuities will help him

sleep at night and not fret about outliving his savings. "I have no intention of worrying about that," Littell says. Elizabeth O'Brien, *Money*, September 11, 2019

5. ILLIQUID ASSETS IN MUTUAL FUNDS COULD SPARK 'FIRE SALE' CRISIS – FED STUDY:

Holdings of illiquid assets by U.S. mutual funds have risen in the last decade, sparking concern that funds could be in trouble in the event of an economic downturn, a recent study from the Federal Reserve said. The study, published last month, found that the 10 largest bank loan mutual funds have increased their holdings of the hardest-to-value, generally most illiquid assets over the past decade. Moreover, the average fraction of liquid assets -- by the study's measure -- to total assets held by bank loan mutual funds have held relatively stable over the same period. "This combination of rising hard-to-value, illiquid holdings amid generally stable liquid holdings might indicate rising liquidity risks," the study said. One key concern is that large investor redemptions from mutual funds could lead the funds to sell assets at "fire sale" prices, which could negatively impact other financial markets. Net assets in bank loan mutual funds stood at almost \$112 billion, as of March, up from about \$24 billion at year-end 2009. Similarly, net assets in high-yield mutual funds have increased to almost \$250 billion in March from about \$157 billion in December 2009, the study found. Assessing the liquidity profile of mutual fund holdings is very difficult, largely due to the scarcity of comprehensive, high frequency market data and the lack of related disclosures by mutual funds. Study authors -- Kenechukwu Anadu, a senior financial markets specialist at the Federal Reserve Bank of Boston's risk and policy analysis unit, and Fang Cai, chief of financial stability assessment at the Federal Reserve Board -- collected a "novel set of data" from publicly available Securities and Exchange Commission forms. The research found that for bank loan mutual funds, the liquidity ratio appears relatively stable over the years, on average, although its range has narrowed since 2012, while the illiquidity ratio has trended up. For high-yield mutual funds, liquidity ratios have been relatively stable, on average, while average illiquidity ratios have narrowed in recent years. The authors concluded by saying there's more work needed on the topic. "While these indicators can serve as useful monitoring tools, more detailed data and more empirical work is needed to better understand the degree to which bank loan and high-yield corporate bond mutual funds' liquidity (and illiquidity) profiles have evolved over the years," the study said. Brian Croce, *Pensions & Investments*, September 11, 2019.

6. ADVISING PENSIONS AND ENDOWMENTS IN ROCKY MARKETS:

From 100-year bonds to sophisticated hedging, the world of pension plan investing is different from the DC plan domain. Given his role as head of client solutions and multi asset for Legal & General Investment Management America (LGIMA), Jodan Ledford

spends more time thinking about pensions than defined contribution (DC) plans. He says the conversation about retirement readiness in the U.S. tends to focus on DC plans, given their increasingly important role as a foundation of the private-sector retirement system. However, the U.S. pension plan market remains highly dynamic and represents a great opportunity set for expert financial advisers to apply their skills. In terms of the investment outlook pension plans face in an increasingly volatile, late-cycle market, LGIMA has advised institutional investors to come “closer to home on risk in the fixed-income portfolio, and to focus on identifying good value when it comes through the market.” As an example, he points to the recent issuance by the University of Pennsylvania of a 100-year bond. Press reports indicate the University successfully priced \$300 million in “century bonds” at a yield to maturity of 3.61%. “There was tremendous demand for it,” Ledford says, citing institutional investors’ thirst for safe and stable assets paying returns above those of long-dated government treasuries. Offering some perspective on the broader marketplace in which pension plans are operating, David Chapman, Ledford’s colleague and head of multi-asset portfolio management for LGIMA, says there has been a healthy amount of debate among his colleagues in terms of what the next five or 10 years may bring. “I would say there is lots of debate and I would not say there is a lot of consensus, but this is purposeful because it allows us to deliberate and let the best ideas rise to the top,” Chapman says. “Generally, we do agree that we are in a late-cycle economy, but how to approach this and predicting exactly how the dominoes might fall and [spark a recession](#)--that’s where the real differences of opinion are focused.” Chapman notes that, historically speaking, equity returns tend to be very strong in the year leading up to a recession--and his firm only projects about a 25% chance of a recession in its forecast for 2020. “So, you can see how the returns given up by reducing your equity risk too early in this cycle--it can mean you effectively achieve the same result as suffering the losses incurred once markets start to decline, if you follow me,” Chapman says. “For pensions, navigating the volatility is about focusing on the level of risk you should take given your objectives and time-frame.” According to Ledford, 2019 has seen “a decently robust demand” for liability driven investing (LDI) strategies for pensions and other institutional investors, including strategies that include some pretty sophisticated hedging techniques. The overall demand has diminished somewhat compared with 2018, but there has been a healthy flow into custom LDI strategies, Ledford says. “For pension plans and other institutions, market volatility can be addressed through diversification and through hedging, and through really understanding what the investment goals are,” Chapman says. “As we look forward, it is a difficult market to project. Late-cycle markets tend to have more volatility, but that fact doesn’t mean that equity markets are going to correct a significant amount tomorrow, next week or next month.” Chapman says investment managers generally are very conscious of the tough position the U.S. Federal Reserve is in. “The flattening and inversion of the yield curve that has happened, it is a reflection of

the inflation outlook and concerns about growth which come from being in the late cycle-- as well as the political environment around tariffs,” Chapman adds. “There are challenges, but none of this goes to say that institutional investors should panic and do anything rash. It’s a great opportunity to reflect on how your risk budget is allocated. If the volatility in the last month has been hard to tolerate, that might mean that the objectives for your investments should be reconsidered.” Like their DC plan counterparts, pension plans seem to be experiencing a [new normal in terms of low interest rates](#). Pointing to a newly updated five-year capital markets assumptions report, Bob Browne, chief investment officer, Northern Trust, expects low-growth pressures will provide an inherent interest rate relief valve in the foreseeable future. He says President Donald Trump’s assertive attitude towards trade disputes has challenged the economy’s “Goldilocks” underpinnings. “We believe global growth, while positive, will modestly disappoint investor expectations, and we are concentrating on ‘lower risk’ assets such as U.S. high yield and U.S. equities,” Browne says. “Political impacts on fundamentals will be partially diffused through continued low rates, enabled by ‘stuckflation’ and central banks, importantly the U.S. Federal reserve, begrudgingly accepting the bond market’s messages.” As a result of these pressures, Northern Trust-managed portfolios are overweight interest-rate sensitive assets, such as global real estate and listed infrastructure. When it comes to risk cases, Browne points first to “inflation tariff proliferation.” He explains that subdued inflation has been a key driver of favorable risk asset returns over the last few years. According to Northern Trust’s projections, an unexpected jump in cyclical inflation would put at risk the interest rate relief valve programmed into the base case above. “While not ideal, the U.S.-- and, for the most part, the global--economy can withstand a concentrated trade war with China,” Browne concludes. “Risks arise if the United States (or others) [meaningfully target other countries.](#)” John Manganaro, *Planadviser*, September 10, 2019.

7. HELP FOR EMPLOYEES FALLING BEHIND ON RETIREMENT SAVINGS:

Educating employees about the power of time on their savings, encouraging them to log into their retirement plan accounts and starting them at a higher deferral rate are some ways employers can help boost employees’ retirement savings. In 2018, 19% of Ascensus plan participants who used its online Retirement Outlook Tool found that they were on track for a successful retirement. In fact, across all generations, the outlook is rather grim, but it is especially challenging for those younger than 25. Of all savers who were “on track” to meet their goals, only 3% of those younger than 25 fell into this group. Only 21% of “on track” savers were between the ages of 25 and 24, 20% were between 25 and 44, 24% between 45 and 54, and 26% between 54 and 65. As to what plan sponsors can do to rectify this dismal situation, Rick Irace, chief operating officer for Ascensus’ retirement division, says, “to start, plan sponsors should focus on educating employees on the fundamentals of their plan” the benefits of enrollment, including matching contributions if

they're offered. For younger generations of employees, many plan sponsors and financial advisers also find it useful to highlight why it makes sense to start saving now, even if it's at a very modest rate. Many plan providers, including Ascensus, provide educational tools and calculators that illustrate to these younger employees the clear advantages of putting time on their side." Irace says digital tools can also be helpful, such as a mobile enrollment app. He adds that after first-time users of Ascensus' Retirement Outlook Tool used it, they increased their savings to 8% within three weeks. So, helping people assess where they stand and how their current savings is projected to turn into retirement income can help, Irace says. Even something as simple as logging into their 401(k) account can prompt a participant to improve their outlook, he says. "A saver who logged into our participant website at least once in 2019 shows an average 401(k) account balance 25% higher than a saver who has not logged in since 2018, 46% higher than one who has not logged on since 2017, and 67% higher than one who has not logged on since 2017." Richard Rausser, senior vice president at Pentegra says plan sponsors should automatically enroll and automatically increase deferrals for participants in the plan. Rather than starting at a 3% deferral rate, Pentegra recommends 6% and has found that a mere 5% to 7% of participants opt out at this rate. "Starting at 3% is selling employees short," he says. Lee Barney, *PlanSponsor*, September 6, 2019.

8. DID YOU KNOW BENJAMIN FRANKLIN SAID THIS?:

I didn't fail the test, I just found 100 ways to do it wrong.

9. PONDERISMS:

If money doesn't grow on trees, then why do banks have branches?

10. INSPIRATIONAL QUOTES:

When you reach the end of your rope, tie a knot in it and hang on. - Franklin D. Roosevelt

11. TODAY IN HISTORY:

On this day in 1985, 8.1 earthquake in Mexico City kills an estimated 10,000 and leaves 250,000 homeless.

12. REMEMBER, YOU CAN NEVER OUTLIVE YOUR DEFINED RETIREMENT BENEFIT.

Copyright, 1996-2019, all rights reserved.

Items in this Newsletter may be excerpts or summaries of original or secondary source

material, and may have been reorganized for clarity and brevity. This Newsletter is general in nature and is not intended to provide specific legal or other advice.