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FINRA SETS SIGHTS ON 529 PLANS. SHOULD ADVISERS BE WORRIED?

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Ed Slott: Every adviser must master IRA withdrawal strategies
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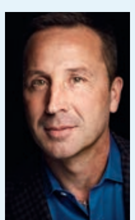
EDITOR'S NOTE

Covering 529 news with deeper analysis

Our timing was so good on this week's cover story, you'd think we'd planned it.

The Financial Industry Regulatory Authority Inc. last Wednesday extended the deadline on its initiative to identify problems with sales of high-fee 529 college savings accounts. It also published a list of frequently asked questions advisers and others have put forward about the self-regulatory organization's newly launched 529 Plan Share Class Initiative.


FRED GABRIEL

This week's cover story, "Inspecting 529 shares," is perfectly timed to inform financial advisers and brokers about whether they should be worried about the initiative — and take part.

Of course, if you purposely put clients into a higher-cost share class in the hopes of making a little more money for yourself, you should be worried. Now would also be a good time to take advantage of the regulator's offer of leniency to firms and advisers who self-report such duty-of-care violations.

Our story, written by *InvestmentNews* reporter Ryan W. Neal, takes a close look at Finra's crackdown and offers readers insights on what it is the regulator is really looking for. Our package also includes a sidebar, written by senior reporter Mark Schoeff Jr., on a series of recent bills making their way through Congress that would enhance the college savings vehicles as well as tackle student debt.

By almost any measure, 529 plans are a success. Nearly 14 million accounts in 529 savings and prepaid plans have $311 billion in assets invested, as of the fourth quarter of 2018, according to data from 529 Conference.

Finra is right to scrutinize how these products are being sold to investors.

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Cetera offers fee-for-service

BY RYAN W. NEAL

KEY POINTS
- Cetera is adding AdvicePay tool to collect fees not tied to commissions or AUM.
- Advisers can set their own prices for services like financial planning.
- Customers can pay by credit card.

CETERA FINANCIAL Group is embracing the fee-for-service business model.

The network of six independent broker-dealers is adding AdvicePay, a payment processing tool launched by XY Planning Network founders Alan Moore and Michael Kitces, to its technology platform to allow Cetera advisers to collect fees not tied to commissions or assets under management.

AdvicePay lets advisers set their own prices for services like financial planning and accept payments via credit card, debit card or Automated Clearing House transfers without requiring a brokerage account. Advisers can collect one-time payments and ongoing, subscription-style fees.

Cetera's business consulting group will also offer training to firms looking to add fee-based services to their practice. The idea is to help advisers expand their offering beyond investment management and grow client bases by lowering the cost of entry, said Cetera president Adam Antoniades.

LETTER
Moore bids farewell to industry
PAGE 33

"The whole issue with the advice game is we've bundled planning and advice into the investment management process," Mr. Anto-

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Merrill cross-selling hits market

Merrill Lynch's effort to get advisers to cross-sell financial services products has the potential to provide a formidable competitive advantage.

BRUCE KELLY
ONADVICE

Merrill Lynch and its parent, Bank of America Corp., right now are offering to shave off up to half a percent from a client's Bank of America mortgage in select markets if the client increases business with Merrill or the bank.

Cross-selling is a practice that involves financial institutions getting clients to buy multiple products and services. By all accounts it is lucrative for banks. And Merrill Lynch has made it clear that it believes clients are happier and feel more secure if their financial life, from banking to managing their money, is at one institution.

Merrill's recent efforts appear to be having an impact in the financial advice marketplace.

One financial adviser at a

CONTINUED ON PAGE 34

BB&T reaches settlement for bilking clients

BY GREG IACURCI

BB&T SECURITIES, a wholly owned brokerage subsidiary of BB&T Corp., has reached a $5.7 million settlement with the Securities and Exchange Commission over allegations that it misled clients and caused them to overpay for advisory services.

BB&T agreed to pay $4.7 million in disgorgement to retail investors, $497,000 in interest and a $500,000 penalty to settle charges levied by the SEC. BB&T neither admitted nor denied the claims.

The settlement, announced last Tuesday, concerns alleged breaches at Valley Forge Asset Management, a $2.8 billion advisory firm BB&T Securities acquired in 2014 as part of the Susquehanna Bank acquisition. It was merged into BB&T Securities in March 2016.

$5.7M
AMOUNT OF BB&T SETTLEMENT WITH SEC

The SEC alleged Valley Forge swayed clients to select in-house, full-service brokerage services over less expensive outside options by deceiving them into thinking they were getting a high level of service at a low cost. Valley Forge, the SEC said, charged commissions averaging 4.5 times more than clients would have paid at other brokerage firms, and "obscured" the price difference by stating it was giving clients a 70% discount off its retail commissions.

BB&T Securities has since amended Valley Forge's cost structure and disclosures, the SEC said.

"BB&T Securities is pleased to have been able to resolve this legacy matter," BB&T spokesman David White said. "The best interest of our clients has always been, and continues to be, our number one priority."

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BLOOMBERG

Fidelity fees face Galvin inquiry

BLOOMBERG NEWS

FIDELITY INVESTMENTS is facing more scrutiny over fees it charges some mutual funds for using its platform to access retirement plan customers.

The Massachusetts Secretary of the Commonwealth said its securities division sent a letter Feb. 27 to Boston-based Fidelity requesting information about those fees. The inquiry follows a Feb. 21 lawsuit against Fidelity by an investor in T-Mobile USA Inc.'s 401(k) plan that claims the firm conceals so-called infrastructure fees.

The fees are also being probed by the Labor Department, the Wall Street Journal reported last month. A spokesman for the Department of Labor said the agency declined to comment on that report.

The Secretary of the Commonwealth's office declined to provide a copy of the letter but said in an email to Bloomberg it has requested the following information:

- Identity of all Massachusetts pension and retirement plans for which Fidelity is a fiduciary or service provider.
- Details of all fees payable by funds to Fidelity.
- Description of the infrastructure fee payable by funds on the network.
- Identity of Fidelity units that receive the fee.
- Whether the fee is disclosed to investors, and if so, how the disclosure is provided.

Fidelity spokesman Vincent Loporchio said that the company doesn't comment on communications with regulators. He said in a statement Feb. 27 that the "infrastructure fee has been fully disclosed to 401(k) plans and their sponsors via a disclosure that Fidelity sent to over 20,000 401(k) plans." Fidelity denies the lawsuit's allegations and will vigorously defend itself, Mr. Loporchio said.

KEY ROLE

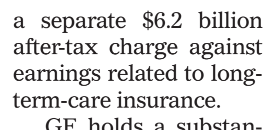
The state securities division is overseen by Secretary of the Commonwealth William Galvin, who has played a key role in policing the mutual fund and securities industries.

In 2002, Mr. Galvin's office, along with then-New York Attorney General Eliot Spitzer, played a key role in probing whether Wall Street firms misled investors with biased investment research. In an agreement with state, federal and industry groups several firms agreed to pay $1.4 billion to settle such claims.

Fidelity had $2.4 trillion in assets under management as of Dec. 31.

GE expects $1.7B LTC rate hike

BY GREG IACURCI


BLOOMBERG

GENERAL ELECTRIC expects to institute $1.7 billion in premium increases for its long-term-care insurance policyholders over the next several years, the company said last Thursday. The company is the latest of several insurers to raise premiums for customers as they contend with market forces making the policies costlier for them to underwrite.

GE will institute the premium increases through 2029. It has 274,000 in-force long-term-care policies on its books, all more than a decade old.

State regulators have already approved $500 million of the increases, which haven't yet been implemented. The remaining $1.2 billion have been filed with regulators or are expected to be filed in the future, GE disclosed in an investor presentation.

SHORING UP THE BUSINESS

The disclosure follows GE's announcement last year that it would need to inject $15 billion into reserves over a seven-year period to shore up its long-term-care business, a revelation that sparked an investigation by the Securities and Exchange Commission. (The company has since revised that figure to $14.5 billion.) At the time, GE also disclosed a separate $6.2 billion after-tax charge against earnings related to long-term-care insurance.

GE holds a substantial legacy LTC business through a subsidiary, North American Life and Health Insurance, which covers costs related to nursing-home stays, assisted living and home health care via reinsurance transactions with other insurers. GE stopped underwriting LTC policies in 2008. The company acquired these reinsurance obligations after spinning off Genworth Financial Inc. in 2004 and selling Employers Reinsurance Corp. to Swiss Re in 2006.

GE has $20 billion in reserves to cover future long-term-care claims for the more than 340,000 people covered by its insurance policies.

GE and other insurers say premium increases are justified given a number of economic challenges, such as a prolonged low interest rates, longer lifespans and increased health-care costs. Many insurers also made some faulty actuarial assumptions, such as overestimating the number of policyholders who would lapse their policies.

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10 key stats about target-date funds

Here are some stats about increasingly popular target-date funds, with combined assets in mutual funds and collective investment trust funds approaching $1.8 trillion, according to Sway Research.

1. The 10 largest TDF providers control more than 90% of the assets.

2. Target-date collective investment trust funds held $677 billion at the end of 2018, roughly 38% of total TDF assets. The share of TDF assets held in mutual funds dipped to 62% from 68%.

3. Passive TDFs hold 53% of total assets, up from 47% in 2015. Assets held in active TDFs have declined in lockstep, to 38%. The remainder are hybrid TDFs.

4. American Funds was second only to Vanguard in TDF asset growth over the past three years, taking in $69 billion, which represents an average annual growth rate of 43%.

5. The overwhelming majority of TDF assets, 95%, are held by asset managers that employ a single proprietary approach.

6. Money managers with affiliated record-keeping businesses control the vast majority of the TDF market. Fidelity, Vanguard and T. Rowe Price, the three largest providers, hold 85%.

7. T. Rowe Price holds the most actively managed TDF assets, with $211 billion, or 31.5% market share.

8. Vanguard holds $649 billion in passively managed TDF assets, controlling nearly 69% of the passive market share.

9. Asset-weighted expense ratios for TDFs are decreasing, in line with broader trends in asset management.

10. Of the 15 largest TDF series, only three have a "to" glidepath, which means the funds stop winding down their equity allocations at retirement.

— Greg Iacurci

Vanguard expands TDF dominance

BY GREG IACURCI

VANGUARD GROUP extended its dominance over the target-date fund market last year as the flow of retirement assets into index funds continued unabated, with employers seeking to reduce the cost of their 401(k) plans.

Vanguard swelled its target-date assets by $26 billion in 2018, the biggest increase of any firm, according to Sway Research, which studies asset management distribution in retirement plans.

MORE
Vanguard ends checking service.
PAGE 18

With $649 billion held in its target-date mutual funds and collective investment trust funds, the index fund behemoth now controls nearly 37% of the roughly $1.8 trillion market, according to Sway. The asset manager's market share has swelled five percentage points, from 32%, in the last three years.

Fidelity Investments and T. Rowe Price, the second- and third-largest TDF providers, respectively, behind Vanguard, saw their market shares decline over the same time period. Fidelity's decreased three points to 13.9%, and T. Rowe's fell two points to 12.6%, according to Sway.

37%
PORTION OF $1.8 TRILLION TDF MARKET CONTROLLED BY VANGUARD

Meanwhile, Vanguard's share of passively managed TDFs — those whose underlying investments are primarily index funds — sits at nearly 70%.

"Their share of passive assets is obscene," said Chris Brown, founder and principal of Sway Research.

Vanguard and other index-focused providers, such as BlackRock Inc. and State Street Global Advisors, have ridden the trend of passive investing in retirement plans and the broader market as investors seek lower costs.

FIDUCIARY CHOICES

The slew of lawsuits targeting employers for excessive 401(k) investment and administration fees have concerned plan sponsors, Mr. Brown said. In addition, the Labor Department's fiduciary rule, parts of which went into effect in 2017 but which was subsequently killed in court, caused plan sponsors and their advisers to focus more keenly on their fiduciary responsibilities.

"It's hard to see much changing this right now," Mr. Brown said of the trend toward index TDFs. "The focus is still so much on fees right now."

Vanguard's target-date mutual

CONTINUED ON PAGE 34

Risk-averse clients push advisers to be creative

BY JEFF BENJAMIN

ONE OF THE biggest challenges financial advisers face when working with clients in or near retirement is convincing them to embrace an appropriate level of investment risk, which is often where psychology must partner with reality.

When considering the extreme example of a client wanting no part of stock market risk, most advisers suggest turning back time and saving more money.

But considering the slim chances of a client having access to a time machine, advisers admit there are some creative ways to protect the portfolios of the most risk-averse clients — assuming those clients are willing to accept the trade-offs.

"There is no free lunch out there, but we have done this for clients in a variety of ways," said Daryl Deke, chief executive of New Market Wealth Management.

If clients just can't stomach the idea of stock market volatility, Mr. Deke said he helps them construct diversified portfolios of traditional bonds, master limited partnerships, business development companies and real estate investment trusts.

"Think of it as combining credit and duration into a portfolio, and it's especially valuable inside a retirement account because you can be less concerned about the tax consequences," he said. "There are still risks, because there's price volatility, but you can build a portfolio where there will be less risk than you get in the stock market."

Unless clients have more money than they could possibly spend in retirement, the biggest risk is usually time. And staying ahead of inflation is difficult when abandoning the growth potential of the equity markets.

Consider, for example, that over CONTINUED ON PAGE 36

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CNI22022 02/19

Transaction tax gains steam among Democrats

BLOOMBERG NEWS

EXPECT TO HEAR a lot about financial transaction taxes. These are small levies on stock and bond trades meant to curb high-frequency trading and speculative betting, which can lead to chaotic swings in the market. Sen. Brian Schatz of Hawaii became the latest Democrat to propose the idea, introducing his version last Tuesday.

The bill, which is more a political message than a plan likely to be signed into law in the coming years, would levy a 0.1% tax on trades of stocks, bonds and derivatives.

"Over the last decade, Wall Street has made record profits from high-risk trades that have made the market dangerously volatile, while doing nothing to add real value to our economy or raise wages for workers," Mr. Schatz said in a statement. Rep. Peter DeFazio, D-Ore., is sponsoring the idea in the House.

> **"WALL STREET HAS MADE RECORD PROFITS FROM HIGH-RISK TRADES."**
>
> SEN. BRIAN SCHATZ, D-HAWAII

Mr. Schatz's 0.1% tax would go further than a proposal from Sen. Bernie Sanders, I-Vt. Mr. Sanders, making his second presidential run, has introduced a levy of 0.03% on all Wall Street transactions. Fellow senator and presidential candidate Kirsten Gillibrand of New York has backed both plans.

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EDITORIAL / LETTERS / OP-ED / GUEST BLOGS

How advisers can help improve financial literacy in America

THE UNITED STATES IS one of the richest countries in the world, yet many of its citizens are woefully ignorant about the nuts and bolts of such financial vehicles as loans and retirement savings plans. In fact, a Standard & Poor's survey ranked the U.S. No. 14 globally in terms of its citizens' financial literacy and rated just 57% of U.S. adults financially literate.

As *InvestmentNews* reporter Greg Iacurci's cover story last week pointed out, Americans' lack of knowledge about these topics can damage their personal financial well-being, and financial illiteracy also places a burden on the economy as a whole.

The problem starts with the U.S. educational system. Just a third of states require students to take personal finance in high school, and in many cases the subject is just a component of another course, such as social studies or math.

Given a study showing that 15-year-old students with bank accounts score higher on financial knowledge than students without accounts, the hurdles that lower-income people face in accessing such financial vehicles as savings or checking accounts also seems to militate against financial literacy.

Still, it's not just lower-income people who come up short when they're quizzed on topics like compound interest and risk diversification. Seventy-eight percent of financial advisers surveyed by *InvestmentNews* agree that financial literacy is a problem, and 49.2% agree strongly that they have encountered financial literacy issues among their clients — individuals who are likely to have a decent amount of wealth.

SIGNIFICANT DECISIONS

It's not as though people have a lifetime to pursue an expertise in financial topics, either. By the time they're in their late teens, students face significant financial decisions when it comes to choosing whether to pursue a college degree and if so, at what college and how to finance that. The mountain of debt that many students take on in the course of acquiring a degree can burden them for decades to come. That student loan debt also is seen as a factor limiting young adults' ability to purchase a home.

But perhaps the biggest area of concern relates to retirement savings. Over the last few decades, U.S. companies have moved away from pension plans, whose investments are selected by the employer, to instead offer defined-contribution plans like 401(k)s in which workers make the decisions for themselves. Questions before the average person range from how much to contribute and what to invest in to how to draw down those savings in retirement. Employees' choices could have a big influence on their financial security in retirement.

WAYS TO CONTRIBUTE

There's a lot advisers can do to improve financial literacy, and you are a prime group to do it. Mr. Iacurci's cover story explored efforts such as working to get more states to mandate the teaching of personal finance, volunteering with schools and other groups to provide such education to students, or helping companies figure out how to make their 401(k) plans and other benefits more fail-safe for their employees.

The promotion of financial literacy is perhaps most squarely in your wheelhouse.

In fact, the *InvestmentNews* survey featured in the cover story showed that a big chunk — 41.3% — of advisers are already involved in efforts to improve financial literacy. Last week's story included profiles of advisers working with schools and other groups to raise the level of financial literacy among young people, as well as suggestions from an advisory board about which groups are the most effective to volunteer with.

Advisers' involvement makes sense. Of all the opportunities for volunteering and activism out there, the promotion of financial literacy is perhaps most squarely in your wheelhouse. It's never too late to get started.

WE WANT TO HEAR FROM YOU. Send a letter to the editor with your thoughts about a story we've published, and include your name, title, company, address and telephone number for verification. Keep your letter under 250 words, and email it to Frederick P. Gabriel Jr. at fgabriel@investmentnews.com. All letters will be edited.

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A new Finra initiative wants brokerage firms to check their supervisory practices and fess up if they are selling clients high-cost college savings plans

BY RYAN W. NEAL

Finra is primed to start flexing its muscles against broker-dealers that allow t heir advisers to sell high-cost college savings plans. But rather than plowing ahead with penalties, the regulator is offering clemency to encourage reform. Will firms bite?

The Financial Industry Regulatory Authority Inc. finds brokerage firms aren't doing enough to reasonably supervise the share classes their brokers recommend in 529 plans. The agency launched an initiative Jan. 28 that allows firms to self-report potential supervisory and suitability violations related to such recommendations. If firms can successfully address problems and deliver a plan to return money swiftly to harmed customers, Finra's department of enforcement will recommend a settlement that doesn't include a fine. If a firm doesn't self-report, it would not be eligible for an automatic fee waiver if the agency later finds a violation.

It's a new direction for Finra, according to Susan Light, partner at law firm Katten Muchin Rosenman and former Finra senior vice president and chief counsel for enforcement. Though the agency has always required that brokerage firms self-report violations, never before has it said it will waive fines in exchange for cooperation

CONTINUED ON PAGE 10

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and reimbursing investors.

"If I owned a brokerage firm, whether I had five brokers or 5,000, I would be looking under my tent to see if I sold 529s — Did I pay attention to share classes? What is my exposure, and what are my supervisory procedures?" Ms. Light said. "I think it would be foolhardy for any brokerage firm that sold 529s to not do their own self-assessment."

Despite the incentive, it remains to be seen how many firms will actually follow through and self-report.

NO SMALL TASK FOR FIRMS

Tracking down all the information needed to calculate restitution for customers is no small task. Few have the capabilities in-house to get it done, and many firms haven't retained the necessary transaction details in their own systems, said Alex Russell, managing director of securities litigation and regulatory enforcement for consulting firm Bates Group.

"Getting the data together and getting it into a shape where you can analyze it is actually very complicated," he said.

The clock is already ticking. Finra initially gave broker-dealers until April 1 to inform the enforcement division of plans to participate, and until May 3 to submit the required information to remedy the matter.

"Finra has left very little time to get your hands around the subject," Mr. Russell said. "It's too early in the game to know how many firms are going to end up self-reporting, or what the level of restitution is going to be."

The regulator must have heard such complaints about the deadline, as it announced last week it would give firms until April 30 to announce plans to participate, and until May 31 to submit information.

Finra hopes firms recognize the self-reporting initiative as an opportunity to identify and improve their supervisory practices around 529 plan share classes. It's now up to firms to take action — or roll the dice with their existing programs.

Susan Schroeder, Finra executive vice president and head of enforcement, said the 529 Plan Share Class Initiative emphasizes some of the cornerstones of Finra's new streamlined approach to enforcement: improving compliance while getting money back to harmed customers more quickly.

"The idea of a no-fine settlement based on a firm's self-reporting and then working closely with Finra to remediate and pay restitution, that's consistent with our current cooperation policy," Ms. Schroeder told *InvestmentNews*.

A 529 plan is a municipal security investors can use to save money tax-free for a beneficiary's future education expenses. Only a small percentage of families take advantage of 529 plans, but usage has grown since 529s were introduced in 1996 as part of the Small Business Job Protection Act. Nearly 14 million accounts invested $311 billion in assets in 529 savings and prepaid plans during the fourth quarter of 2018, according to data from 529 Conference.

Plans are commonly sold as Class A shares, which have a front-end sales charge but lower annual fees, or as Class C shares with higher annual fees without front-end sales charges. For customers with more than seven years to invest in the plan — a college fund set up for a young child, for example — the aggregate cost of a C share exceeds that of an A share.

The problem is some advisers don't recommend the share class that would be most cost-effective for investors.

"Let's be honest, 20 years ago you saw a lot of situations where people would either use an A share to jam somebody in and get that big upfront commission, or use a C share because it was someone who is going to invest for a long period of time and pay the 1% [annual fee] forever and ever," said Brock Jolly, founder of The College Funding Coach.

But even advisers with the best intentions can slip up.

"The reality is that advisers are spread pretty thin at times," Mr. Jolly said. "You're just trying to get something processed. Maybe there's an element of laziness, but a lot of times people aren't paying attention to details."

Finra has been concerned about share class suitability violations for a long time, Ms. Light said. The issue has made it into exam priorities in the past and the regulator has brought charges against firms.

So why bring the focus to 529 plans in particular in 2019? For starters, the new tax code stemming from the 2017 tax reform law opened up 529 plans to more than just college tuition. Now investors can use them for K-12 expenses, complicating the issue of share class suitability based on the length of time the money will be invested.

Another catalyst for Finra's new effort is the success of a similar initiative by the Securities and Exchange Commission in early 2018. That program allowed self-reporting by investment advisers who had improperly invested clients in high-fee mutual funds share classes. According to Mr. Russell, who helped more than a dozen firms participate in the SEC program, Finra is essentially modelling its program after the SEC's.

QUALITATIVE VS. QUANTITATIVE

Ms. Schroeder said the primary difference with her agency's program is that it is a qualitative assessment of supervisory structures and share class suitability rather than a purely quantitative look at fees.

In other words, Finra isn't saying Class C shares are always bad. It wants firms to ensure investors are getting the right investment to fit their needs. In particular, Finra wants to see improvements in how brokers are trained on the costs and benefits of different 529 plan share classes, how firms receive data on plans sold, and how firms review the suitability of recommendations.

Though many broker-dealers welcome the opportunity to improve supervisory systems and procedures, firms are less pleased with the initiative's disclosure

Congress takes on 529s, debt

BY MARK SCHOEFF JR.

While the Financial Industry Regulatory Authority Inc. examines whether brokers are recommending 529 plans that are too expensive, Congress wants to enhance the savings vehicles.

A series of bills, supported mostly by Republicans, would allow 529s to cover the costs of apprenticeship programs and home schooling, and additional educational expenses beyond tuition. They also would enable account holders to tap 529s to help pay down student debt for a sibling of the beneficiary.

The changes would follow major modifications introduced by the 2017 tax-reform law, which enhanced 529s to cover tuition for K-12 education. A few recently introduced bills also target student debt.

529 EXPANSION BILLS

The Family Savings Act (H.R. 1084): Would expand 529s to cover apprenticeship programs, home-schooling expenses and student loans.

Enhancing Educational Opportunities for Home School Students Act (H.R. 65): Would expand 529s to cover home schooling.

Student Empowerment Act (S. 157 and H.R. 621): Would expand 529s to cover a range of educational expenses in elementary and secondary school.

STUDENT LOAN BILLS

Employer Participation in Repayment Act (S. 460 and H.R. 1043): Would allow companies to contribute up to $5,250 per year tax-free to their employees to reduce student loan balances.

Student Loan Repayment Assistance Act (H.R. 655): Would encourage employers to offer student-loan assistance by giving them a 10% tax deduction for repayments up to $6,000 annually.

Graduate Student Savings Act (S. 448): Would allow graduate students to deposit funds from their stipends or fellowships into individual retirement accounts.

STATE-LEVEL ACTION

There's also activity on the state level. On March 4, more than two dozen states launched a campaign, "For Their Future Movement," to limit college debt for new generations, according to a statement.

Some states, however, are resisting the expansion of 529s. A bill in the Oregon legislature would allow the state to ignore federal rules extending the program to cover K-12 education.

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requirements, Mr. Russell said. Firms need to look for violations dating back to 2013, and go back to 2008 to calculate restitution for investors.

"So you can imagine that if you went to a plan sponsor and said you needed transaction-level information going all the way back to 2008, you're going to get a myriad of responses," he said. "Some can't do it; some only have data for some of the years."

Firms have to crunch the numbers to figure out whether or not a client was harmed, then calculate exactly how much to pay back. Though Finra suggested two approaches — an aggregate statistical approach or a customer-specific analysis — both will take significant time.

In addition to extending the deadline, Finra said it will be flexible with firms on timing. The regulator has set up a dedicated email account (529Initiative@finra.org) for firms to request an extension for either their initial supervisory review or for collecting the required information.

"I do think it's important to say that the first step of this initiative would not be data gathering; it's qualitatively assessing the supervisory process," Ms. Schroeder said.

For firms that ultimately decide not to participate, Finra won't automatically waive fines, but neither will it increase the sanctions it would have imposed before the initiative was offered.

UPHILL BATTLE

Mr. Jolly thinks Finra's initiative is a good thing, but says it faces an uphill battle getting the industry to participate. It's like watching the referees in an NFL game: It can be hard to remember that the ones blowing the whistle and issuing penalties also have the players' best interests at heart.

"The point is, Finra is like this Big Brother that's always out there looking over your shoulders," Mr. Jolly said. "If you're not breaking the law, you've got nothing to worry about. But if I accidentally screw something up, am I going to get slapped on the wrist?"

The additional regulatory risk is unlikely to discourage many advisers from selling 529 plans, said Mark Kantrowitz, publisher and vice president of research at SavingForCollege.com. Finra is giving firms plenty of time to clean their act up before the regulator starts "knocking heads together."

Mr. Kantrowitz thinks the initiative will ultimately influence advisers to be more deliberate in assessing a client's risk tolerance and time horizon, which they should have been doing already.

"More families are contributing to 529 plans than previous years," he said. "That's why it's good that Finra is applying this extra scrutiny now."

Ross Riskin, assistant professor of taxation and CFP program director at The American College, suggested increased awareness around fees could actually be beneficial for adviser-sold plans, especially with the new tax law complicating share class suitability.

"It's not one-size-fits-all," Mr. Riskin said. "Working with a competent, well-informed adviser is still the right way to go with these things."

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Choices: Sen. Sherrod Brown introduced the Arbitration Fairness for Consumers Act on March 1.

Mandatory arbitration target of legislation

BY MARK SCHOEFF JR.

NEW LEGISLATION that would prohibit mandatory arbitration for customer disputes involving investments could raise the issue's profile among decision-makers.

Sen. Sherrod Brown, D-Ohio, ranking member of the Senate Banking Committee, introduced on March 1 the Arbitration Fairness for Consumers Act, which would end arbitration agreements that are part of almost every brokerage contract and many investment-adviser contracts.

Mr. Brown is primarily focused on student loans, credit card agreements and employment contracts, but his bill also would apply to the arbitration system for broker-customer disputes run by the Financial Industry Regulatory Authority Inc., as well as to the American Association of Arbitration system that most investment adviser clients use.

BROADER IN SCOPE

Another bill introduced at the end of February in the House and Senate, the Forced Arbitration Injustice Repeal Act, is broader in scope than Mr. Brown's bill and would amend the Federal Arbitration Act. It also would affect Finra arbitration and that of investment advisers.

The legislative activity was welcomed by the Public Investors Arbitration Bar Association, which is a critic of mandatory arbitration. The group asserts that customers should have the option of arbitration or the courts when filing claims against financial professionals.

"It's certainly positive that we've got a number of arbitration bills being introduced right now covering a wide range of dispute resolution," said PIABA president Christine Lazaro, who is also a law professor at St. John's University.

A Finra spokesperson was not immediately available to comment.

But the arbitration legislation must navigate difficult terrain on Capitol Hill. It's likely the GOP will resist arbitration reform.

"Neither of these bills is going to get enacted," said George Friedman, former director of Finra arbitration. "They will pass the House. I expect they will die in the Senate."

But Finra and Securities and Exchange Commission officials may be summoned to Congress to testify on the bills — or on Finra arbitration generally. The Dodd-Frank financial reform law gave the SEC authority to end mandatory arbitration.

> **"IT SETS THE TABLE FOR AN IMPORTANT ELECTION-YEAR ISSUE IN 2020."**
>
> ANDREW STOLTMANN
> SECURITIES ATTORNEY

"It's not going to be smooth sailing for Finra or the SEC," said Mr. Friedman, an adjunct professor of law at Fordham University. "The commission may feel some pressure to take a look at arbitration given that Dodd-Frank authorizes it to study the process."

Democrats like Mr. Brown, a potential presidential candidate, may be playing a long game on arbitration. In recent rulings, the Supreme Court has upheld arbitration rights.

Mr. Brown's bill "faces an uphill climb legislatively, but it sets the table for an important election-year issue in 2020," said Andrew Stoltmann, a Chicago securities attorney and PIABA board member. "And if we get a Democratic president, there's a real chance this legislation or similar legislation could end mandatory arbitration."

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Nevada fiduciary rule challenged

BY MARK SCHOEFF JR.

THE FINANCIAL INDUSTRY and investor advocate groups split on whether Nevada can implement its own investment advice standard.

In comment letters filed on Nevada's proposal to strengthen advice rules, the Securities Industry and Financial Markets Association, the Financial Services Institute and the Investment Adviser Association told the state to back off. They argued that a state-level advice standard would conflict with federal securities laws.

But 16 investor advocacy groups said Nevada has the authority to promulgate the regulation, which would require financial professionals in the state to act as fiduciaries.

The Nevada legislature passed a law requiring advisers to follow a fiduciary standard, and the securities bureau is in the midst of drawing up regulations.

> **KEY POINTS**
> - Nevada proposal to strengthen advice rules elicits split reaction from trade associations and advocates.
> - SIFMA warns against 'uneven patchwork' of state approaches.

The Investment Adviser Association said state regulation of advisers registered with the Securities and Exchange Commission violates a 1996 law, the National Securities Markets Improvement Act.

"We urge the [Nevada] Securities Division to amend the draft regulations … to clarify that they do not and are not intended to apply to SEC advisers or their representatives," wrote Gail Bernstein, IAA general counsel.

SIFMA cited that law as well as seven others it said would trump a Nevada fiduciary rule.

"The foregoing preemption and other legal infirmities render the proposed regulations as drafted invalid and ultimately unenforceable," wrote SIFMA managing director and associate general counsel Kevin Carroll.

FSI asserted that Nevada can't enact a reg that would add new broker books and records rules to those contained in federal law.

But investor advocates, including the Consumer Federation of America and the Committee for the Fiduciary Standard, praised Nevada's proposed rule, saying it is tougher than the SEC's advice proposal, the centerpiece of which is the Regulation Best Interest broker standard.

"We greatly appreciate states such as Nevada that are willing to step in to fill the regulatory void by providing the protections investors need and expect," the groups wrote. "Contrary to arguments from industry groups, Nevada is well within its authority in proposing this rule. Nothing in the proposal imposes an affirmative obligation on broker-dealers to keep new or additional records."

In a comment letter last Thursday, the North American Securities Administrators Association said Nevada's proposal would increase investor protection.

"The draft regulations should curb abusive sales practices in Nevada," wrote Vermont Commissioner of Financial Regulation and NASAA president Michael Pieciak.

OTHER STATES FOLLOWING

In addition to Nevada, New Jersey is working on its own fiduciary rule and the Maryland legislature is considering legislation that would require financial advisers in the state to be fiduciaries.

The SEC could release a final advice reform rule by summer. SIFMA said the SEC should promulgate a "uniform, nationwide" standard of conduct for brokers.

"A state-by-state approach would result in an uneven patchwork of laws that would be duplicative of, different than and/or in conflict with federal standards," Mr. Carroll wrote.

But the investor advocacy groups assert that the SEC's Regulation Best Interest is weaker than the current suitability standard governing brokers.

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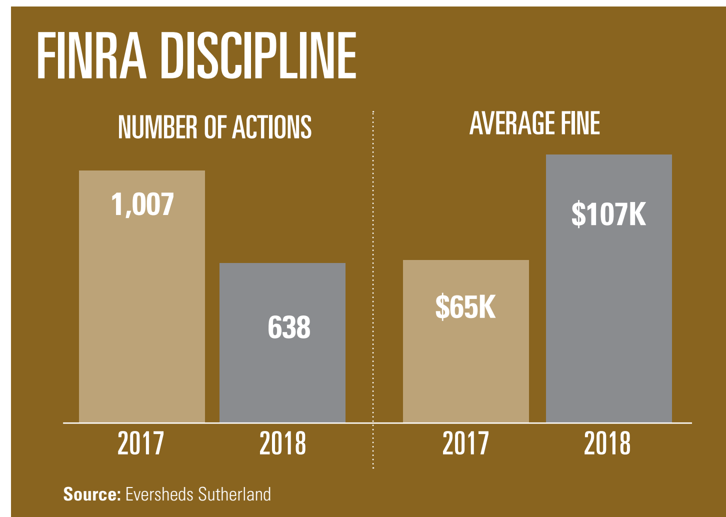

GPB Capital Holdings on FBI's radar

BY BRUCE KELLY

ALREADY THE FOCUS of inquiries by the SEC and Finra, GPB Capital Holdings said last month the FBI made an unannounced visit to the investment firm's office in New York.

GPB Capital has raised $1.8 billion from accredited investors through private placement funds that invest in auto dealerships and the waste management industry.

Registered reps from dozens of independent broker-dealers sold the high-risk, high-commission private placements.

In December, *InvestmentNews* reported that the Financial Industry Regulatory Authority Inc. and the Securities and Exchange Commission launched investigations into GPB, citing industry sources.

DISCLOSURES, PERFORMANCE

The focus of the SEC's inquiry was the accuracy of disclosures made by GPB to investors, the performance of various funds and the distribution of capital to investors.

The firm has been working on enhancing its oversight and auditing practices, a company spokesperson said in a statement. The FBI entered the firm's Manhattan offices Feb. 28, along with officials from the New York City Business Integrity Commission.

The commission regulates the public wholesale markets and the private carting and shipboard gambling industries.

"Recently, we have been cooperating with inquiries from various authorities and the visit on Feb. 28, 2019, from the FBI and the New York City Business Integrity Commission, while unscheduled, was a part of that process," according to an email from a GPB spokesman.

"We will continue to cooperate with inquiries and are confident that as we move forward our portfolio companies are stable and well-positioned for the future."

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SEC orders broker to pay for churning

BY JEFF BENJAMIN

THE SECURITIES and Exchange Commission obtained a final judgement against a broker charged with excessive churning of client brokerage accounts.

William Gennity, who has been suspended from the industry by the Financial Industry Regulatory Authority Inc., was ordered to pay $302,483, which includes $127,686 in disgorgement, $14,797 in prejudgment interest, and a civil penalty of $160,000.

According to the SEC complaint filed in the U.S. District Court of the Southern District of New York, between July 2012 and August 2014 Mr. Gennity "recommended to four customers a pattern of high-cost, in-and-out trading without any reasonable basis to believe that his customers could make a profit."

Mr. Gennity's recommendations resulted in losses for the customers and gains for Mr. Gennity, according to the SEC.

According to Finra's BrokerCheck database, Mr. Gennity worked at 10 different brokerage firms during his 12-year career, and was employed at New York-based Alexander Capital when he was churning the client accounts.

"This is indicative of a bigger problem in the industry because it shows that firms are not properly supervising to look for churning activity," said Adam Gana, attorney at Gana Weinstein, who was not involved in this case.

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Medicare and high-cost drugs

MARY BETH FRANKLIN

ONRETIREMENT

Howard Sorkin, a financial adviser in Chicago, is on a mission to educate clients and other advisers about the high cost of prescription drugs for some Medicare beneficiaries. People requiring specialty drugs for cancer, multiple sclerosis, hepatitis and other serious illnesses may be on the hook for thousands of dollars a year.

"Even though, as an adviser, I discussed these topics with clients, I never fully understood the true costs of medications under Part D until I was confronted with it myself," Mr. Sorkin wrote to me in an email.

Mr. Sorkin was diagnosed with stage 4 nonsmokers lung cancer, including a brain tumor, in 2016, when he was 68. Fortunately, he has qualified for a new targeted drug therapy in lieu of chemotherapy.

Unfortunately, the drug is very expensive. It retails for about $18,000 per month, although he is able to buy it at a discounted price of about $15,000 per month through his hospital.

Since its inception in 2006, the Medicare Part D prescription drug benefit has helped improve the affordability of medications for millions of people with Medicare. Yet many beneficiaries continue to face high out-of-pocket costs for their medications. Prescription drugs accounted for $1 in every $5 that Medicare beneficiaries spent out-of-pocket on health-care services in 2016, not including premiums, according to a new report by the Kaiser Family Foundation.

Specialty tier drugs — defined by Medicare as drugs that cost more than $670 per month in 2019 — are of particular concern for Part D enrollees, according to a recent analysis by the nonprofit organization. While specialty tier drugs are taken by a relatively small share of enrollees like Mr. Sorkin, spending on these drugs now accounts for over 20% of total Part D spending, up from 6% to 7% before 2010.

OUT-OF-POCKET COSTS

Median annual out-of-pocket costs in 2019 for 28 specialty tier drugs reviewed by Kaiser range from $2,622 for Zepatier (for hepatitis C) to $16,551 for Idhifa (for leukemia), based on a full year of use, according to the Kaiser analysis.

Part D plans are allowed to charge between 25% and 33% coinsurance for specialty tier drugs before enrollees reach the coverage gap. Then they pay 25% of the cost of their drugs. Once their total out-of-pocket spending exceeds an annual threshold of $5,100 in 2019, enrollees pay 5% of the total drug costs above the catastrophic coverage threshold.

In Mr. Sorkin's case, 5% of his $15,000-per-month drug cost translates into $750 per month. There is no upper limit on out-of-pocket spending.

MONTHLY PREMIUMS

In addition, there are monthly premiums for Medicare Part B and Part D, including additional high-income surcharges, and hundreds of dollars of monthly vitamins and supplements not covered by insurance.

"My medical costs have far exceeded what I ever thought I would need to spend at my age," said Mr. Sorkin, who is 71 and still working part time. "I am fortunate, but how many seniors can afford this expense?"

Medicare Part D out-of-pocket costs are scheduled to grow exponentially in the future unless Congress acts, said Mary Johnson, a Social Security and Medicare policy analyst with The Senior Citizens League.

(Questions about Social Security? Find the answers in my ebook at InvestmentNews.com/MBFebook.)

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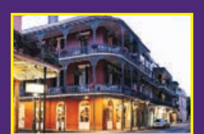
Best and worst cities for money management

WalletHub has come up with a ranking of the money management skills of U.S. cities. Here are the top and bottom five, with some of the factors considered in the ranking.

WORST

5. DETROIT
Overall score: 55.96
Median credit score: 552
Credit card debt to income ratio: 5.28%



4. NEW ORLEANS
Overall score: 55.79
Median credit score: 647
Credit card debt to income ratio: 7.08%

3. SAN ANTONIO
Overall score: 55.77
Median credit score: 651
Credit card debt to income ratio: 7.53%

2. MIAMI
Overall score: 54.84
Median credit score: 668
Credit card debt to income ratio: 8.46%

1. MEMPHIS
Overall score: 50.46
Median credit score: 592
Credit card debt to income ratio: 6.03%

BEST

5. MINNEAPOLIS
Overall score: 71.10
Median credit score: 722
Credit card debt to income ratio: 4.82%

4. BOSTON
Overall score: 73.67
Median credit score: 723
Credit card debt to income ratio: 4.88%

3. SAN JOSE, CA
Overall score: 75.00
Median credit score: 730
Credit card debt to income ratio: 3.94%

2. SEATTLE
Overall score: 77.42
Median credit score: 741
Credit card debt to income ratio: 4.48%

1. SAN FRANCISCO
Overall score: 80.28
Median credit score: 745
Credit card debt to income ratio: 3.58%

Donor-advised funds may draw more scrutiny

BY MARK SCHOEFF JR.

AN INCREASINGLY popular way to make charitable donations while maintaining the tax benefits of philanthropy could face greater regulatory scrutiny.

The tax reform law of 2017 eliminated many deductions, including those for charitable contributions, while increasing the standard deduction to $24,000 for couples. In response, donor-advised funds have become a hit.

'TAKING OVER'

"They're in the process of taking over the philanthropic landscape," said Ray Madoff, professor at Boston College Law School. "There's no end in sight to their growth."

A donor-advised fund allows benefactors to group donations into one contribution that would make it worthwhile to itemize one year versus taking the standard deduction. Such a fund — which can be set up at Fidelity Charitable, Schwab Charitable and similar platforms — can then distribute gifts for years thereafter to various causes.

Unlike a private foundation, gifts from a DAF are anonymous. Although the fund is independent from the donor, it usually follows his or her advice on where to direct contributions.

Ms. Madoff, who is also director of the Forum on Philanthropy and the Public Good at Boston College, believes increased regulatory oversight is likely.

"The more people learn about the lack of rules governing donor-advised funds, the more they're going to think there is a need for more regulation of funds to ensure the money goes to charitable purposes within a reasonable period of time," Ms. Madoff said.

97% PORTION OF GRANTS FROM SCHWAB CHARITABLE THAT INCLUDE DONOR NAMES

ATTRACTIVE FEATURES

One of the most attractive features of a DAF is benefactors "get the upfront charitable deduction and ongoing functional control," she said.

If the donor had set up a private foundation, that entity would have to file an IRS Form 990 annually and provide much more transparency about its operations.

But in a statement, Schwab Charitable said approximately 97% of grants from its accounts include donor names.

"Annual payout rates for national DAF providers and for Schwab Charitable average about 20% of assets, which is 4 to 5 times that of private foundations," according to Schwab Charitable, which works with more than 1,800 investment advisers. "At Schwab Charitable, roughly 80% of contributions have been fully distributed to charity within 10 years."

A DAF gives donors more latitude and efficiency in making larger gifts, said Tim Steffen, director of advanced planning at Baird Private Wealth Management.

"Congress may feel that people are taking advantage of that flexibility and they may feel the need to step in and regulate," Mr. Steffen said. "That would be unfortunate."

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Getting to know the new Form 1040

To analyze the impact of taxes for your clients, you first need to know their marginal and effective tax rates. Then go through Page 2 of the new Form 1040.

GUESTBLOG
FRANK PAPE

Line 2a: Tax-exempt interest. Is the client's marginal tax rate so low that municipal bonds may not make sense? Evaluate the tax-equivalent yield of municipal bonds versus taxable bonds.

Line 2b: Taxable interest. Conversely, is the client's marginal tax rate enough to erode after-tax income? Clients always want to focus on the yield of a given investment and often fail to consider the after-tax yield.

Line 3a: Qualified dividends. Qualified dividends are taxed at long-term capital gains rates. Does the client's situation require generating income? Perhaps a strategy focusing on capital appreciation or a similar tax-smart approach focusing on capital appreciation versus high dividends is warranted.

Line 3b: Ordinary dividends. Sometimes referred to as nonqualified dividends, these dividends are taxed as ordinary income and can be taxed at higher rates than qualified dividends. Many non-U.S. equity mutual funds (active and passive) have nonqualified dividends greater than 20% of the total dividend amount. Tax-smart funds will look to minimize this amount.

Schedule 1, Line 13: Capital gain or (loss). Look to Schedule D to see the source of gains for line 13. Are the investments creating capital gains that are too high as a percentage of the investment amount? In 2018, the average U.S. equity mutual fund paid out capital gains equal to 11% of its net asset value. Does the distributed gain reflect an amount larger than this? Even 11% is painful and can likely be improved upon with a more tax-friendly approach.

Does Schedule D show turnover (the selling of mutual funds, stocks or bonds) that appears too high given the value of the investment amount? There may be a reason for the high turnover, such as harvesting losses or generating income, but one should understand the investment purpose of the turnover on Schedule D. Nonproductive turnover can lead to increased taxes.

Frank Pape is senior director of the North America portfolio consulting group at Russell Investments.

SALT encouraging wealthy to move?

BLOOMBERG NEWS

THE REPUBLICAN tax overhaul signed by President Donald J. Trump over a year ago provides plenty of perks for the rich. But a controversial provision that helps pay for huge corporate tax cuts punishes residents of states with higher income taxes.

By setting a $10,000 cap on how much Americans can deduct in state and local taxes, or SALT, Washington created a pricey problem for the privileged in some parts of the country. Now that the first tax season under the overhaul is here, that reality is hitting home — and the thought of moving to a low-tax state may suddenly look more attractive.

But even before the law, there were rich people in blue states trying this strategy. Some actually moved, while some just pretended to — and that's where state tax auditors come in. Officials in places such as California and New York don't make it easy for the rich to say goodbye, with investigators who dig deep, forcing residents to prove they really have cut ties in favor of cheaper pastures.

"You have to abandon the old and establish the new," said Karen Tenenbaum, a New York lawyer who specializes in residency disputes. "The more ties you cut, the better — auditors like to see a moving van and an itemized list of what was moved."

James Gazzale, a spokesman for New York's Department of Taxation and Finance, echoed her sentiment, albeit more formally.

"Ensuring taxpayers pay their fair share is a top priority; therefore, our nonresident audit program continues to be very active," he said.

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"A BUSINESS COACH ONCE TOLD ME, 'IF YOU IDENTIFY A WEAKNESS AND DON'T ADDRESS IT, YOU HAVE NO DESIRE TO BE IN BUSINESS FIVE YEARS FROM NOW.'"
— ERIC CLARKE, FOUNDER AND CEO, ORION ADVISOR SERVICES

IBDs take different paths with their technology

The catchphrase, "We can no longer just be an X company, we have to be a technology company," is so much of a cliché, it sounds like a punch line from HBO's "Silicon Valley."

But there is truth behind the saying. Some argue that every company is now a tech company, and the idea of a "technology industry," as it existed in the halcyon days of Intel and Hewlett Packard, is an antiquated concept. So it was interesting to see a leading broker-dealer employ the phrase literally and start offering its proprietary technology as a standalone product.

KEY POINTS

- Commonwealth spun off its Advisor360 tech platform and is licensing it externally.
- Cambridge is instead focused on pulling together third-party tech.

Just before Valentine's Day, Commonwealth Financial Network showed just how much it loves its proprietary technology platform, Advisor360, by licensing it out to Massachusetts Mutual Life Insurance.

While another cliché goes, "If you love something, give it away," this is hardly the way things are traditionally done in the brokerage business. Why spend a half billion developing technology to later spin it off into an independent entity and make it available to the competition?

Even more of a head-scratcher is the newly independent Advisor360's place in the landscape of adviser technology vendors. The company offers a full suite of back-office, adviser-facing and client-facing technology, bringing it into competition with tech startups, custodians and Envestnet, the 800-pound gorilla in the industry. Does an independent broker-dealer really think it can keep pace?

The cost of competing is a reason Commonwealth decided to spin off its technology into an independent company, said Darren Tedesco, president of Advisor360. While there was internal concern about giving up one of Commonwealth's crown jewels in recruiting, the firm realized it needed to drastically increase Advisor360's user base to bring in the money necessary to keep the platform competitive.

RYAN W. NEAL

ONTECHNOLOGY

"We've got to giddy-up because by 2025, there are only going to be four or five fintechs left standing, and I plan for Advisor360 to be one of them," Mr. Tedesco said.

The money brought in from MassMutual and future contracts will accelerate development of the platform, which will ultimately benefit Commonwealth advisers. It also will allow the broker-dealer to focus on other parts of its business without being distracted with being a technology company.

But don't expect Commonwealth to kick off a trend throughout the IBD industry. Few firms have the resources or expertise needed. For those, it's probably smarter to focus on partnering with existing tech providers.

THIRD PARTIES

That's the strategy taken by Cambridge Investment Research, another IBD that revealed a new adviser technology platform last month. Instead of building something it can sell, Cambridge is focusing on pulling together third-party technologies, using a customized version of eMoney to tie them together and integrate with Cambridge's core digital station.

Jeff Vivacqua, Cambridge chief marketing officer, said the firm made an intentional decision not to build its own technology platform. Advisers are already using eMoney, he said, they just demanded better integration.

Cambridge CEO Amy Webber said that while firms like United Capital have been successful, it's a difficult and expensive business proposition. Ms. Webber is skeptical that a broker-dealer can provide enough to differentiate its technology.

"You have to be confident that you can hit the marketplace in a big, differentiated way," she said. "People far more brilliant than I have said forever that you can't be all things to all people."

She would rather provide a flexible, modern tech platform, while focusing more on other competitive advantages, such as Cambridge's culture and private ownership.

"We've never been one to fight in the red ocean, so to speak," she said. "We are a blue-ocean firm — we go a different direction than anyone else."

Or as Mr. Vivacqua put it: "We don't refer to ourselves as a technology firm … we're a financial solutions firm."

And that's OK. First of all, it remains to be seen just how successful Advisor360 will be. Also, consider how Walmart responded to the threat of Amazon. After it acquired e-commerce startup Jet.com, Walmart has rejuvenated sales.

It's true that every firm needs to modernize its practice to avoid disruption. But not every firm has to become a technology company. If tech isn't already a core competency, there are enough vendors on the market to buy or partner with to remain competitive.

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Custodians no longer core of data hub

BY RYAN W. NEAL

THE RELATIONSHIP BETWEEN custodians, registered investment advisers and technology vendors is evolving.

RIAs today are demanding deeper and more robust data on clients so they can provide new services like financial planning, but these advisers are increasingly turning to third-party technologies or even their own data warehouses instead of relying on a custodian, according to a new report from Aite Group.

As a result, custodians find they are no longer at the core of an RIA's tech nor its client relationships.

"The custodial value proposition is diminishing," said Greg O'Gara, senior research analyst for Aite Group's wealth management practice and author of the report. "They have to bring new ways to leverage data that they do have, and data that they can get, to create a new value proposition for their clients."

After investing heavily in proprietary technology as a differentiating factor, custodians are coming to terms with the fact that advisers just aren't using these tools, Mr. O'Gara said. RIAs want choice, which is why you see firms like Schwab Advisor Services focus less on proprietary products and more on tight integration with third parties.

SUPPORT VS. PROVIDE

Noel Stave, RBC Correspondent and Advisor Services chief operating officer, agreed that custodians can be more valuable to RIAs by supporting technology instead of trying to build their own.

"The pure processing aspect of a custodian is just a commodity at this point," Mr. Stave said, adding that all the major firms do a good job with the core services. "Where the value-add now is what level of tech enablement we can bring to their practices that helps them differentiate."

RBC offers support for a menu of third-party technologies, and then with a handful of "best-in-breed" vendors builds even tighter integrations through its RBC Black platform.

But even as custodians build "open-architecture" platforms to support third-parties, RIAs are finding they can assemble their own technology stacks using their favorite tool as the hub, often the firm's CRM, portfolio accounting system or an investment management platform.

Even more challenging for custodians is that these technology tools can offer valuable client data that custodians typically don't have access to, Mr. O'Gara said.

Third-party tech also can support RIAs working with multiple custodians and provide information on held-away assets and other products like insurance and annuities.

"In order to support holistic financial planning, you need to know a lot about the client," Mr. O'Gara said. "You see a lot of RIAs collecting it on their own and storing it with vendors to leverage the relationship."

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How to make a splash on Instagram

I opened my last column with these words: A solid plan and strategy is the key to every social media success.

Let's use those words again for this month's column about Instagram for financial advisers.

You may know Instagram as that photo-sharing service your teenage kids are obsessing over, but what you may not know is that it's so much more.

ONSOCIALMEDIA

Here's a statistic reported by my colleague Ryan W. Neal in his story about Hearsay Systems adding Instagram to its social media platform in an effort to help advisers overcome compliance hurdles: About 70% of Instagram's 1 billion users are younger than 35, a demographic still evading many advisers.

Nothing's easy and Rome wasn't built in a day, but with a well-planned strategy, Instagram can be a wildly successful part of your social media toolbox.

Here's what you must consider:

What will your Instagram be about? The first thing you need to decide is the same thing you need to decide when starting any social media presence: What is your ultimate goal?

You don't use social media because "everyone else does" or "I have to." You use it because you have a clear vision of the message you want to send and how it fits into your branding and messaging.

Instagram is like no other platform you use. Make sure you go into it with this top of mind. You aren't going to recycle tweets and put them on Facebook and you aren't going to put your Instagram photos on LinkedIn. And if anyone tells you this is a good idea because it'll save you time, run away. Run fast.

Instagram isn't just about selfies, GIFs and food. I love how UBS uses Instagram. The company's bio reads "Passionate about the future. About the world we live in. About change." And it uses the account to focus on important topics such as pollution, recycling and climate change. The photos are artistic and compelling.

What do you stand for? In the UBS example above, 30 seconds looking through the feed makes that abundantly clear. Do the same with yours. What you stand for and how you ultimately share that might lead you to your next customer.

Your Instagram can be anything — as long as it's not boring. Mix video and photos. Be creative and colorful. If volunteering is a part of your company culture, show your employees volunteering. Let your clients get to know you and your firm. Tag people. Encourage sharing.

Give an inside, behind-the-scenes glimpse. Maybe you have an office in a city experiencing notable weather. Ask someone to take a photo and share it. My pro tip for this one is to ask anyone who has taken a photo of a rainbow to share it with you. Rainbows can be evergreen photos that can be posted with just about any caption. Plus they are beautiful, and people love to click on them.

HAVE A CLEAR VISION OF THE MESSAGE YOU WANT TO SEND ON SOCIAL MEDIA.

Hashtags matter, so use them wisely and correctly. Take a look around Instagram to see what other people in the industry are using. Create one that's just for your brand and apply it to everything. There are all kinds of ways to do it, but the key is to #alwaysbeconsistent.

Make it enjoyable. It's hard to put into words, but it's easy to tell when an Instagram account is the real deal or just going through the motions. Take everything you've read above into consideration. Once you know your message, you can work out how you want everything to look.

If you have a social media question or an idea for a column topic, please let me know. Tweet them to me with the hashtag #onsocialmedia or email me.

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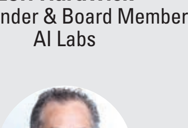
The fintech space is evolving rapidly and advisers want to find a way to stay on the cutting edge. But what can they do to stay ahead of the curve without getting overwhelmed by the status quo disguising itself as innovation?

Join *InvestmentNews* for the next episode of its Innovators video webcast series where we examine, "What's next in fintech?". Experts and thought leaders will sit down with Matt Ackermann, *InvestmentNews'* director of multimedia, and James Gallardo of *InvestmentNews* Research and examine:

- Big trends in fintech: What do advisers need to know now?
- How to separate your fintech needs from your fintech desires?
- Where is the puck headed in fintech?
- What are some of the biggest fintech innovations you cannot afford to ignore?

SPEAKERS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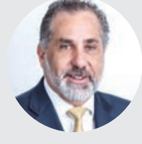
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3 NUMBER OF STARS PIMCO TOTAL RETURN BOND FUND RECENTLY RECEIVED FROM MORNINGSTAR INC. FOR OVERALL PERFORMANCE, AFTER BEING AT FOUR STARS FOR ITS 32-YEAR HISTORY

Faith-based firm wins overall award

BY JEFF BENJAMIN

THE 2019 LIPPER FUND Awards by Refinitiv for the best risk-adjusted mutual fund performance recognizes more than 300 individual fund winners across multiple categories, but one of the biggest winners this year is a fund company that didn't win a single fund award.

> **KEY POINTS**
> - GuideStone Capital didn't pick up a single fund award, but won small-company category.
> - Vanguard dropped to fourth place in number of trophies.

Dallas-based GuideStone Capital, a faith-based firm that manages $13 billion across 24 funds, pulled off the unusual feat of winning the overall fund company award in the small-company category.

"Guidestone has no individual winning funds but has the best risk-adjusted return for all their funds added up; that means these guys are top-performers for each fund they manage," said Tom Roseen, head of research services at Lipper.

David Spika, Guidestone president, said the overall small-company award falls in line with what the asset manager is hoping to accomplish.

"We're not trying to be first decile every year, our goal is to be in the top 30%, preferably top quartile," he said. "If you're the best, you're probably taking on too much risk."

The annual Lipper Awards, which were announced last Thursday at a ceremony in New York, recognizes individual mutual fund performance over 3-, 5-, and 10-year periods. Eleven funds stood out this year for ranking first in all three time periods.

ENTIRE LINEUP

But the company awards, which are divided into groups of firms with more than and less than $76.8 billion, considers the fund company's entire lineup over the trailing three-year period.

Pacific Investment Management Company is this year's overall large-company winner.

Pimco also won the award for best performance as a large-company equity fund manager, and won 17 individual fund awards, earning the firm a fifth place ranking in terms of individual awards.

TIAA Investments won the award for large-company mixed assets for the fourth consecutive year, and Morgan Stanley Investment Management won the large-company award for fixed income funds for the third straight year.

MIXED-ASSET CATEGORY

In the small-company asset-class categories, Thrivent Mutual Funds won the mixed-asset category again this year after winning it from 2015 through 2017, but missing it last year.

Primecap Management Company won the equity category for the fourth consecutive year.

Ashmore Funds won the fixed-income category for the second straight year.

In terms of total trophy count, T. Rowe Price Group leads the pack this year with 22 winners, edging out Fidelity Investments, which brings home 21 trophies.

> **"OUR GOAL IS TO BE IN THE TOP 30%, PREFERABLY TOP QUARTILE."**
> DAVID SPIKA, PRESIDENT GUIDESTONE

The Vanguard Group, which led all fund companies last year by taking home 29 trophies, dropped to fourth place this year with 19 trophies.

As Mr. Roseen points out, the awards are based on quantitative risk-adjusted performance measurements that are designed to reward positive gains over declines, which tends to eliminate strategies that swing for the fences and experience more volatile performance.

TARGET-DATE FUNDS

At T. Rowe, where 10 of the 22 winning funds were target-date strategies, portfolio strategist Joe Martel said the target-date funds are managed both on a glide path as well as some "tactical movements around that glide path based on our shorter-term view of the markets."

"For example, for much of the past 18 months, we've been underweight stocks relative to bonds based on our view of risk in the markets," he added. "But we closed that to neutral in 2019."

Steve Neff, head of Asset Management at Fidelity Investments, said the firm's 21 awards "are a reflection of our dedication to helping individual investors and financial advisers and their clients achieve their long-term investment goals."

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Bill Gross talks deficit, autism

BLOOMBERG NEWS

EVEN AFTER one of the most storied careers in financial markets, Bill Gross has a few surprises left.

For one, he's been diagnosed with Asperger's syndrome, the autism-spectrum disorder. Mr. Gross said he lived most of his life unaware of the condition and now believes it helps explain not only why he was such a successful investor for so long but also why he could, by his own admission, rub people the wrong way.

Mr. Gross, long one of the most vocal critics of post-crisis stimulus, now sounds like a near-convert to modern monetary theory. He said deflation poses a huge challenge for central banks, admires what Japan has done to revive its moribund economy and thinks the U.S. government should consider doubling the size of its deficit.

And the billionaire and registered Republican agrees with Democratic Rep. Alexandria Ocasio-Cortez, D-N.Y., that the rich should pay more in taxes — if not quite the 70% she's proposing at the margin. It's a "necessary evil" to correct the failings of American capitalism, Mr. Gross said, adding that if inequality persists there'll be a "revolution at the ballot box."

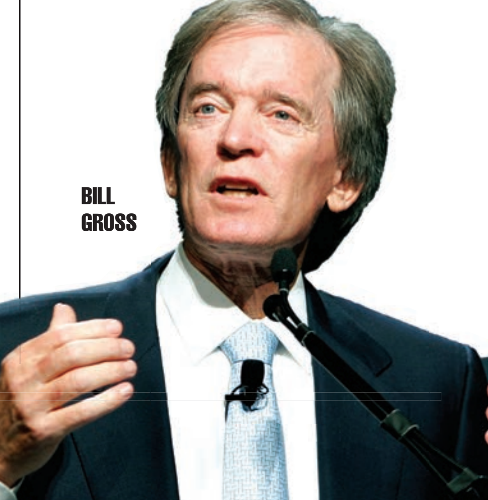
March 1 was Mr. Gross' last day as a portfolio manager with Janus Henderson Group, the firm he joined in 2014. He said he wants to be remembered for investing clients' savings profitably and helping build a "wealth-creating machine" at Pimco.

That leaves one question: Will there be another bond market king?

Probably not, according to Mr. Gross. One reason is the proliferation of passive investment vehicles.

If anyone, he said it might be Scott Minerd, chief investment officer at Guggenheim Partners, partly for his "great, long-term perspective."

Read an extended version of Mr. Gross' interview at InvestmentNews.com/Gross.



BILL GROSS

Vanguard ends check-writing service

INVESTMENTNEWS

VANGUARD GROUP will end a service for larger customers on July 31 that lets them write checks and pay bills from a Vanguard account.

The VanguardAdvantage program was launched in 2002 as a way to compete with banks. Customers who had between $500,000 and $1 million at Vanguard were charged an annual fee, while it was free for those with at least $1 million invested.

Less than 2% of eligible clients are using it, according to a Wall Street Journal report, and only half were active users in recent months.

In a letter to clients obtained by the Journal, Vanguard said it regretted any inconvenience that ending the program may cause customers. Separately, it said it is exploring other cash management options it may offer.

> **<2%** PORTION OF ELIGIBLE CLIENTS USING THE SERVICE

While only a tiny portion of Vanguard customers may have used the program, the news of its demise has generated hundreds of comments on Bogleheads.org, a web forum for investors who use Vanguard funds.

Many commenters expressed their disappointment.

"The Advantage Account served my needs well," said one commenter. "I will now seek alternatives for my investing needs. Been a good 43 years with Vanguard."

Others discussed possible alternatives to VanguardAdvantage.

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Award	Firm Size*	Management Company Name
Overall	Large Company	PIMCO
Overall	Small Company	GuideStone Funds Trust
Equity	Large Company	PIMCO
Equity	Small Company	PRIMECAP Management Co.
Fixed Income	Large Company	Morgan Stanley Investment Management Inc.
Fixed Income	Small Company	Ashmore Investment Management Ltd.
Mixed Assets	Large Company	TIAA Investments
Mixed Assets	Small Company	Thrivent Mutual Funds

**Large and small breakpoint set at $76.8 billion AUM*

AWARDS METHODOLOGY

FUND CLASSIFICATION AWARDS

The currency for the calculation corresponds to the currency of the country for which the awards are calculated and relies on monthly data. Classification averages are calculated with all eligible share classes for each eligible classification. The calculation periods extend over 36, 60 and 120 months. The highest Lipper Leader for Consistent Return (Effective Return) value within each eligible classification determines the fund classification winner over three, five or 10 years.

For a detailed explanation, please review the Lipper Leaders methodology document on **http://lipperalpha.financial.thomsonreuters.com/lipper/our-methodology/.**

Fund classification awards are given to the company that has the day-to-day responsibility of investing and monitoring the assets under management within the fund's portfolio in order to achieve the investment objectives of the fund. This company is also referred to as a portfolio management company or investment adviser. The award goes to the fund management company in case no such company has been appointed or several such companies share the task.

ASSET CLASS GROUP AWARDS

Fund groups with at least five equity, five bond or three mixed-asset portfolios in the respective asset classes are eligible for a group award. The lowest average decile rank of the three years' Consistent Return measure of the eligible funds per asset class and group will determine the asset class group award winner over the three-year period. In cases of identical results, the lower average percentile rank will determine the winner.

Asset class group awards will be given to the best large and small groups separately. Small groups will need to have at least three distinct portfolios in one of the asset classes – equity, bond or mixed asset.

OVERALL GROUP AWARD

Fund groups with at least five equity, five bond and three mixed-asset funds are eligible for an overall group award. An overall group award will be given to the group with the lowest weighted-average decile 1 ranking of its respective asset class results based on the methodology described above. In cases of identical results, the lower average percentile rank will determine the winner.

An overall group award will be given to the best large and small group separately. Small groups will need to have at least three equity, three bond and three mixed-asset funds.

No asset class and/or overall group awards are handed out if there are fewer than three competing companies.

Asset class and overall group awards are given to the company that is responsible for establishing the fund by appointing the fund management company, promoting and/or distributing the fund, the brand of the fund and the product range. This company is also referred to as the promoter or sponsor company.

ASSETS-UNDER-MANAGEMENT BREAKPOINT CALCULATION

UNITED STATES: All eligible open-end funds (see Specific Methodology Issues for the U.S.) with sales permission in the United States will be considered. The assets-under-management breakpoint is found at 85% accumulated weight value.

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Management Company	Lipper Classification	Full Fund Name	Ticker Symbol
Vanguard Group Inc.	Corporate Debt A-Rated Funds	Vanguard Long-Term Investment-Grade Fund, Admiral	VWETX
Euro Pacific Asset Management LLC	Precious Metals Equity Funds	EuroPac Gold Fund, A	EPGFX
Morgan Stanley Investment Management Inc.	Corporate Debt BBB-Rated Funds	Morgan Stanley Institutional Corporate Bond Portfolio, I	MPFDX
Nuveen Fund Advisors LLC	California Municipal Debt Funds	Nuveen California High Yield Municipal Bond Fund, I	NCHRX
Vanguard Group Inc.	California Intermediate Municipal Debt Funds	Vanguard California Intermediate-Term Tax-Exempt Fund, Admiral	VCADX
Franklin Templeton Investments	Convertible Securities Funds	Franklin Convertible Securities Fund, Advisor	FCSZX
ProFunds Group	Dedicated Short-Bias Funds	ProFunds Short Oil & Gas Fund, Investor	SNPIX
Fidelity Management & Research Co.	Emerging Markets Funds	Fidelity Advisor Emerging Asia Fund, I	FERIX
Nuveen Fund Advisors LLC	Alternative Equity Market Neutral Funds	Nuveen Equity Market Neutral Fund, I	NIMEX
Invesco Funds	European Region Funds	Invesco European Small Company Fund, Y	ESMYX
Capstone Asset Management Co.	Global Equity Income Funds	Steward Global Equity Income Fund, Institutional	SGISX
Dodge & Cox	Global Large-Cap Value Funds	Dodge & Cox Global Stock Fund	DODWX
OppenheimerFunds Inc.	General & Insured Municipal Debt Funds	Oppenheimer Rochester AMT-Free Municipal Fund, A	OPTAX
Morgan Stanley Investment Management Inc.	Global Multi-Cap Growth Funds	Morgan Stanley Institutional Global Opportunity Portfolio, I	MGGIX
Fidelity Management & Research Company	Global Multi-Cap Value Funds	Fidelity Series Intrinsic Opportunistic Fund	FDMLX
Grantham, Mayo, Van Otterloo & Co. LLC	Global Natural Resources Funds	GMO Resources Fund, IV	GOVIX
OppenheimerFunds Inc.	Global Small-/Mid-Cap Funds	Oppenheimer Global Opportunities Fund, I	OGIIX
PIMCO	General U.S. Government Funds	PIMCO Long-Term U.S. Government Fund, Institutional	PGOVX
Fidelity Management & Research Co.	Health/Biotechnology Funds	Fidelity Select Medical Technology and Devices Portfolio	FSMEX
OppenheimerFunds Inc.	High-Yield Municipal Debt Funds	Oppenheimer Rochester High Yield Municipal Fund, Y	ORNYX
Fidelity Management & Research Co.	Industrials Funds	Fidelity Select Defense & Aerospace Portfolio	FSDAX
Vanguard Group Inc.	International Large-Cap Growth Funds	Vanguard International Growth Fund, Admiral	VWILX
BlackRock Inc.	Intermediate Municipal Debt Funds	BlackRock Strategic Municipal Opportunities Fund, Institutional	MAMTX
PIMCO	International Multi-Cap Core Funds	PIMCO StocksPLUS International Fund (U.S. Dollar-Hedged), Institutional	PISIX
Morgan Stanley Investment Management Inc.	International Multi-Cap Growth Funds	Morgan Stanley Institutional International Advantage Portfolio, I	MFAIX
Hartford Funds	International Multi-Cap Value Funds	Hartford International Value Fund, Y	HILYX
Harvest Global Investments Limited	International Income Funds	Harvest Asian Bond Fund, Institutional	HXIIX
Fidelity Management & Research Co.	International Small/Mid-Cap Core Funds	Fidelity International Small Cap Fund	FISMX
OppenheimerFunds Inc.	International Small/Mid-Cap Growth Funds	Oppenheimer International Small-Mid Company Fund, Y	OSMYX
American Funds	Intermediate U.S. Government Funds	American Funds Mortgage Fund, R-6	RMAGX

2019 TROPHY WINNERS

Management Company	Lipper Classification	Full Fund Name	Ticker Symbol
T. Rowe Price Associates Inc.	Large-Cap Growth Funds	T. Rowe Price Institutional Large Cap Growth Fund	TRLGX
DoubleLine Funds	Large-Cap Value Funds	DoubleLine Shiller Enhanced CAPE, I	DSEEX
T. Rowe Price Associates Inc.	Mixed-Asset Target 2020 Funds	T. Rowe Price Retirement 2020 Fund	TRRBX
American Funds	Mixed-Asset Target 2035 Funds	American Funds 2035 Target Date Retirement Fund, R-6	RFFTX
American Funds	Mixed-Asset Target 2050 Funds	American Funds 2050 Target Date Retirement Fund, R-6	RFITX
T. Rowe Price Associates Inc.	Mixed-Asset Target 2025 Funds	T. Rowe Price Retirement 2025 Fund	TRRHX
American Funds	Mixed-Asset Target 2040 Funds	American Funds 2040 Target Date Retirement Fund, R-6	RFGTX
American Funds	Mixed-Asset Target 2045 Funds	American Funds 2045 Target Date Retirement Fund, R-6	RFHTX
Thrivent Mutual Funds	Mid-Cap Core Funds	Thrivent Mid Cap Stock Fund, S	TMSIX
GW Capital Management LLC	Mid-Cap Value Funds	Great-West Mid Cap Value Fund, Investor	MXMVX
AQR Capital Management LLC	Multi-Cap Core Funds	AQR Large Cap Defensive Style Fund, I	AUEIX
Copley Financial Services Corp.	Multi-Cap Value Funds	Copley Fund	COPLX
Nuveen Fund Advisors LLC	Minnesota Municipal Debt Funds	Nuveen Minnesota Municipal Bond Fund, I	FYMNX
Wells Fargo Funds Management LLC	Mixed-Asset Target Allocation Conservative Funds	Wells Fargo Diversified Income Builder Fund, Institutional	EKSYX
Wells Fargo Funds Management LLC	Mixed-Asset Target Allocation Growth Funds	Wells Fargo Diversified Capital Builder Fund, I	EKBYX
Fidelity Management & Research Co.	Retirement Income Funds	Fidelity Advisor Managed Retirement 2025 Fund, I	FIRFX
Vanguard Group Inc.	New Jersey Municipal Debt Funds	Vanguard New Jersey Long-Term Tax-Exempt Fund, Admiral	VNJUX
ICON Funds	Natural Resources Funds	ICON Natural Resources Fund, S	ICBMX
OppenheimerFunds Inc.	New York Municipal Debt Funds	Oppenheimer Rochester Fund Municipals Fund, Y	RMUYX
Vanguard Group Inc.	Ohio Municipal Debt Funds	Vanguard Ohio Long-Term Tax-Exempt Fund, Investor	VOHIX
OppenheimerFunds Inc.	Pennsylvania Municipal Debt Funds	Oppenheimer Rochester Pennsylvania Municipal Fund, A	OPATX
Thrivent Mutual Funds	Small-Cap Core Funds	Thrivent Small Cap Stock Fund, S	TSCSX
Virtus Investment Partners Inc.	Small-Cap Growth Funds	Virtus KAR Small-Cap Growth Fund, I	PXSGX
Thompson IM Funds Inc.	Short-Intermediate Investment-Grade Debt Funds	Thompson Bond Fund	THOPX
Eaton Vance Management	Short-Intermediate Municipal Debt Funds	Eaton Vance Short Duration Municipal Opportunities Fund, I	EMAIX
Eaton Vance Management	Short-Intermediate U.S. Government Funds	Eaton Vance Government Obligations Fund, I	EIGOX
OppenheimerFunds Inc.	Short Municipal Debt Funds	Oppenheimer Short Term Municipal Fund, Y	ORSYX
Eaton Vance Management	Short U.S. Government Funds	Eaton Vance Short Duration Government Income Fund, I	EILDX
PIMCO	Ultra-Short Obligation Funds	PIMCO Short-Term Fund, Institutional	PTSHX
Nuveen Fund Advisors LLC	Virginia Municipal Debt Funds	Nuveen Virginia Municipal Bond Fund, I	NMVAX

Caution is PIMCO's byword for the remainder of the year

Fund giant says full valuations, uncertainty translate into formula for defensiveness

Considering its prowess in fixed-income investing, PIMCO's achievement as Lipper's Large Company Fund Family winner in the overall as well as equity categories is particularly noteworthy. To find out how the Newport Beach, Calif.-based manager of $1.7 trillion in assets sees 2019 unfolding across the investment spectrum, *InvestmentNews* Custom Strategy Studio recently chatted with Dan Ivascyn, PIMCO's Group Chief Investment Officer and a member of its Executive and Investment Committees. Edited comments are below.

IN Custom Strategy Studio: ***Overall, what's PIMCO's view of 2019?***

Dan Ivascyn: When we look at the world today, we see an environment with increased uncertainty and valuations that are pretty full, and in many areas, expensive. Since our clients are looking to us to preserve capital, that means we're being more defensive and more cautious. We are focusing on quality and credit exposure, especially in the corporate sector. As an active fixed-income asset manager focused on liquidity, we can be defensive and patient during periods of ordinary or high valuation and be aggressive during periods of volatility.

INCSS: ***Let's get back to the corporate sector, where many people consider current leverage levels to be a potential problem. How does PIMCO see it?***

DI: Corporate indebtedness is a concern. Over the last several years, when we've seen a steadily growing global economy, credit has performed reasonably well. But problems can emerge when an economic slowdown occurs. We don't see that happening over the near term, but there has been a steady deterioration in credit fundamentals in the corporate market, which we believe to be one area prone to overshooting fundamentals in the event of a recession. It's where we're most defensive as a firm.

INCSS: ***What about other areas of the credit market?***

DI: We continue to find housing-related credits attractive, directly in the corporate sector and in the form of asset-backed securities. Housing markets have done very well over the past 10 years, and you can find yields in the housing-related market comparable to the yields in the corporate market for BB- and BBB-rated credits, but with much more resilient credit profiles. As a result, we have a solid allocation to housing-related risk.

INCSS: ***And what about credit markets outside the U.S.?***

DI: We see some opportunity there. Segments of the emerging markets look attractive. But you have to remember that while a lot of emerging markets did poorly in the first half of 2018, many of them quietly finished the year with very strong performance. So there are still opportunities there, but it's important to be careful.

Our outlook on equities is somewhat neutral. We have a slight preference for the U.S.; we're a bit constructive on emerging markets over the longer term; and we're more cautious on Europe, where valuations look attractive, but where there is considerable uncertainty, a lot of it political. It's hard for us to get excited about Europe at this time.

INCSS: ***Where does PIMCO see the biggest risks? What do you worry about?***

DI: The biggest source of risk for investors is that there is still too much debt in the world relative to global growth rates. We're a decade past the financial crisis, yet debt is at all-time highs and our deficits are headed toward 6% of GDP, which is assuming economic growth. If there's a recession, the deficit could go to 10%.

> "Since our clients are looking to us to preserve capital, that means we're being more defensive and more cautious."
>
> **Dan Ivascyn, Chief Investment Officer, PIMCO**

As far as the U.S. dollar is concerned, a lot of people are calling for a weaker dollar, but we're much more neutral. One big reason is that while the Federal Reserve is being seen as becoming more dovish, when you look globally and see a broad slowing of economies, a weaker U.S. dollar would require the rest of the world to become a bit stronger — and we just haven't seen that.

INCSS: ***What's the PIMCO view on equities?***

DI: The equity strategy for which we won the recognition looks to replicate a popular equity index while we run a straightforward, high-quality bond portfolio beneath it. We've been doing this for more than 20 years, and the idea is to earn incremental returns from an equity portfolio with very little excess volatility over the index.

As a fixed-income investor, we have to be very careful about how debt dynamics will play out over time. During the next slowdown, we're likely to see lower rates, QE used again and — if the political will is there — supportive fiscal policy. But that doesn't necessarily mean that the same policies will continue to work going forward. Over time, the tools of policymakers are becoming less effective.

INCSS: ***The takeaway?***

DI: We're becoming more defensive and cautious. We expect lower returns over the next 10 years and greater uncertainty, which leads to more volatility. It's time to play good defense. ■

BEST OVERALL SMALL FUND FAMILY 2019

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Investing involves risk, including the potential loss of principal. **The funds may experience negative performance and past performance does not guarantee future results.**

The U.S. Lipper Fund Awards for Best Overall Small Fund Family is based on a review of 29 fund families for 2019 and based on risk-adjusted performance for the three-year period ended November 30, 2018.

In order to qualify for Lipper's Overall Small Fund Family Group Award, a fund family will need to have at least three distinct portfolios in each of the following asset classes: equity, bond and mixed-asset. An overall Group Award will be given to the fund family with the lowest average decile ranking of its respective asset class results based on the three-year Consistent Return measure of the eligible funds per asset class and group. The Lipper Leader for Consistent Return rating, which is a risk-adjusted performance measure, is calculated over 36, 60 and 120 months. The fund with the highest Lipper Leader for Consistent Return (Effective Return) value in each eligible classification wins the Lipper Fund Award. The Lipper Fund Awards, granted annually, highlight funds and fund companies that have excelled in delivering consistently strong risk-adjusted performance relative to their peers. Additional information is available at *LipperFundAwards.com.*

Group Award Methodology: For the 2019 Lipper Fund Awards from Refinitiv, a small fund family is defined as having assets of $76.8 billion or less.

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As of December 31, 2018, GuideStone Funds has $12.1 billion in assets, which makes GuideStone Funds the nation's largest faith-based mutual fund family. No other fund family with a Christian screen exceeds GuideStone Funds in asset size.

You should carefully consider the investment objectives, risks, charges and expenses of the GuideStone Funds before investing. A prospectus with this and other information about the Funds may be obtained by calling ***1-888-GS-FUNDS*** *(1-888-473-8637) or downloading one at* GuideStoneFunds.com/Funds. *It should be read carefully before investing.*

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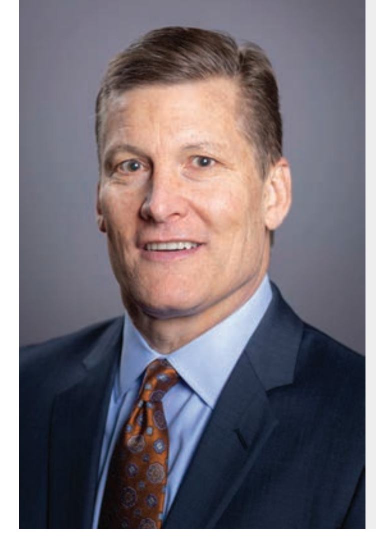
An investing approach based on values and long-term value

GuideStone looks for investments in line with its century-old mission

Recognized for excellence in the past, this year's Overall Lipper Award Fund Family winner in the Small Firm category is GuideStone Funds Trust. *InvestmentNews* Content Strategy Studio recently spoke with David S. Spika, President of GuideStone Capital Management, the investment adviser to the GuideStone Funds. He also is part of the executive leadership team of the parent company, GuideStone Financial Resources, chairs the firm's Socially Responsible Investing Committee and oversees management of the unregistered alternative investments held by the firm. His edited comments follow.



"One of the things we've done for our investors is create strategies that perform better during periods of volatility. We offer a defensive, low-volatility strategy fund and a liquid-alternatives fund, which are designed to be good diversifiers during periods of greater volatility."

David Spika, President, GuideStone Capital Management

INCSS: ***GuideStone Financial Resources' history is somewhat unusual for a financial services company. Tell us about it.***

David Spika: We recently celebrated the 100th anniversary of our founding in 1918 as a subsidiary of the Southern Baptist Convention to provide financial support to pastors and their widows. We have grown into a diversified financial services firm over the years, historically providing insurance, retirement and investments to Convention entities such as churches, schools, mission-sending groups, hospitals and universities.

In 2014, we decided to offer our mutual funds to the broader public, and today we have about $13 billion in assets under management in the fund complex, most of that from the Southern Baptist community. Most of our growth is coming from outside that community, and we're currently on 50 platforms to serve broker-dealers and RIAs. We're still committed to our mission of serving the Lord and providing Christian-screened funds, while at the same time believing there is a broad market for our funds among advisers interested in our philosophy, our process and our Christian underpinnings.

INCSS: ***Explain the GuideStone process, which sounds similar to SRI or ESG investing.***

DS: We like to call it investing according to faith-based principles. We screen out industries operating in five areas: alcohol, tobacco, gambling, pornography and abortion. We also have the ability to screen out companies based on other activities, such as anything to do with child labor or predatory lending. Our aim is to promote the emotional and physical well-being of society through our investments, and one of the other ways do that is by advocating for change among companies that we own. One of our efforts currently is trying to reduce the incentives to produce and sell opioids.

INCSS: ***Let's talk about your equity investing process and what you see ahead for stocks.***

DS: We have a multi-manager process, in which there are two to five sub-advisers for each of our funds. Our philosophy is based on having a fundamental, long-term, risk-management focus.

As we head into the 11th year of a bull market, we're seeing the Fed pause in its rate-raising and the impact of tax cuts in the rear-view mirror. With sentiment weakening and growth slowing globally, we believe we're nearing the end of the cycle, which means that returns are growing harder to come by and volatility moves higher, and we're starting to move into a period where the market anticipates an impending recession.

Because we've always managed for retirement, we're very focused on fundamentals, managing risk and managing for the long term, which are especially important now, when the market can overreact to something like a tweet. Many people in the market today, professionals and individual investors alike, have never experienced a recession or a downturn and will be caught off guard when that happens. It's important not to bail out at those times, which is why we want to own companies that are best positioned for the long term.

INCSS: ***What's GuideStone's fixed-income outlook?***

DS: We believe rates probably have peaked for the current cycle. The 10-year Treasury note is below 3%, and the yield curve is relatively flat. Particularly at the long end, rates will be a function of growth expectations and inflation. On the other hand, we have to watch spreads. After widening in December's market sell-off, spreads between corporates and Treasuries have returned to being very narrow. When the economy starts to turn, spreads will widen out again, and many kinds of debt will underperform. That's something we're watching because prices may become volatile again even if interest rates don't go down.

One of the things we've done for our investors is create strategies that perform better during periods of volatility. We offer a defensive, low-volatility strategy fund and a liquid-alternatives fund, which are designed to be good diversifiers during periods of greater volatility.

INCSS: ***And everything meets your standards?***

DS: Yes. We have two analysts whose job is to evaluate securities and create a restricted list of those that don't meet our standards. That list is given to all our sub-advisers. ■

Morgan Stanley's award-winning team sees a risk-on year

The backdrop for bonds is 'much better,' but being too aggressive may not be wise

Looking ahead to the remainder of 2019, Michael Kushma, Chief Investment Officer for Global Fixed Income at Morgan Stanley Investment Management, sees a "radically different" environment from that which prevailed at the start of 2018.

"Instead of worrying about rising yields, a Federal Reserve hell-bent on raising rates and concerns about the economy overheating, we're now in a world where the Fed is neutral, the monetary environment is benign and volatility is low. This creates a much better backdrop for bonds than last year," said Mr. Kushma, whose firm captured the Lipper Fund Family Award in the Fixed Income, Large Company category for the second consecutive year.

Optimistic about performance in the coming months, Mr. Kushma sees a positive trend, but nothing as torrid as the outsize gains of January and February when markets made a U-turn from the downdrafts of December.

"Riskier investments should perform best, but their valuations are such that investors should be wary of jumping in," he said. "We believe this is a good environment in which to take risk, but not as aggressively as the market may suggest."

One area that has done well for the firm over the past several years has been mortgage- and other asset-backed securities, Mr. Kushma said.

"That market outperformed in 2018, although we don't expect it to do as well in 2019, so we're not expanding our exposure," he said.

Always mindful of risk, one of the firm's big worries is complacency.

"People may be expecting news that is too good," he said. "Trade could be a problem, and markets are pricing in good results for Brexit and the auto trade negotiations coming up later in the spring. If there are setbacks, the market could come down."

> "After looking at countries, rates and currencies, the senior leaders of research and portfolio management come up with strategies that reflect our view of where to focus, what to overweight and what to underweight."
>
> **Michael Kushma**
> **CIO, Global Fixed Income**
> **Morgan Stanley**
> **Investment Management Inc.**

Another big question mark is China.

"They have been trying to slow their credit growth while at the same time trying to stimulate the economy," he said. Because of its size, China exerts a powerful effect on the global economy, and its credit easing and tightening has an outsize effect on global fixed-income volatility, Mr. Kushma added. In its portfolios, Morgan Stanley Investment Management tends to focus on larger, state-owned companies that have the support of the government, he said.

Overall, the firm has integrated investment-grade and high-yield rates and currency research globally and applies top-down and bottom-up methodologies. Credit analysts are based in London, New York, Singapore and Tokyo.

"After looking at countries, rates and currencies, the senior leaders of research and portfolio management come up with strategies that reflect our view of where to focus, what to overweight and what to underweight," he said.

Executing those strategies in the fixed-income market demands other skills, especially understanding the business motivations of market participants, which play a role in market liquidity and pricing.

Part of the reason for the sharp drop in the market in December, Mr. Kushma explained, was dealer reluctance to increase bond inventory as the end of the year approached because they didn't want to derail their targeted performance commitments. With dealers less active, it didn't take much selling to drive prices lower, he said, while at the same time making purchases difficult because inventories were low.

"These other factors likely were part of the reason for the strong rally in January and February," he said. ■

Ashmore sees stronger EM credit returns for 2019

Second-year award winner says emerging markets will outperform developed world

For the second consecutive year, Ashmore Investment Management is Lipper's top Small Company Fund Family winner in the fixed-income category. With a specialization in emerging-market debt that goes back to the 1980s, London-based Ashmore has a value focus that Jan Dehn, Global Head of Research, explains below — along with his outlook for 2019.

> "We are one of the larger emerging-market firms, we've built a full stable of counterparties in local markets and we treat all counterparties with respect, which serves us well during times when liquidity is tight."
>
> **Jan Dehn**
> **Global Head of Research**
> **Ashmore Investment Management Ltd.**

With benchmark indices now covering 153 individual markets, emerging-market (EM) bonds are now the most diverse fixed-income asset class in the world. Specializing in that market for more than a quarter century, Ashmore Investment Management expects 2019 performance in EM credit "to rebound to the patterns seen in 2016-2017 as the unwinding of so-called quantitative-easing trades resumes." That translates into emerging-market credits outperforming developed-market fixed-income investments.

"Returns in 2019 may be marginally stronger than their five-year average," said Mr. Dehn.

Although performing strongly over the past three years, EM fixed-income markets suffered a setback in 2018 due to the U.S. corporate tax cut and the imposition of import tariffs, which caused "a sharp but temporary rebound in the dollar, which in turn adversely impacted sentiment toward EM fixed income and its performance," said Mr. Dehn, who views 2018 as an interruption in the trend of market forces pushing the dollar lower. The trend, "rooted in excessively long positions in dollars in response to quantitative-easing policies," is likely to shape flows in global markets for years to come as "distorted positions" are unwound, he said.

What could go wrong in such a rosy scenario for EM debt?

"A few EM countries will, of course, screw up in 2019," Mr. Dehn said. "This happens every year due to elections, policy mistakes, external shocks, etc. Such risks are best handled with active management."

In the case of Ashmore, the active management process is tailored to what Mr. Dehn says are the three unique conditions of emerging-market market credit: excessive volatility relative to underlying risk, occasional "spectacular" defaults and cyclical liquidity.

The excessive volatility in EM credit arises from the tendency of investors to lump all EM countries into one basket without considering differences. Mr. Dehn notes that a blowup in one EM country could pummel the price of another EM country's debt — even if the two have little or no economic connection.

"The volatility often has nothing to do with fundamentals, and we can take advantage of it," he said, which means that the value-oriented Ashmore tends to buy into sell-offs and sometimes builds positions in falling markets, which in the short term may translate into underperformance.

To avoid defaults, Ashmore relies on thorough credit research and analysis.

And, finally, because attraction to emerging-market debt in developed countries runs hot and cold, EM debt markets tend to be very liquid when the asset class is in favor, and extremely illiquid when investors in developed markets turn away.

During those periods of illiquidity, being a long-term, consistent investor in emerging-market credits is invaluable, Mr. Dehn said.

"We are one of the larger emerging-market firms, we've built a full stable of counterparties in local markets and we treat all counterparties with respect, which serves us well during times when liquidity is tight," he said.

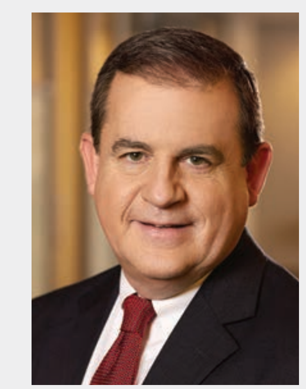
On the big question of the market for emerging-market debt — the future course of Federal Reserve interest-rate moves, which have an enormous impact on the value of the dollar and the attractiveness of EM debt versus U.S. securities — Mr. Dehn is sanguine.

"Emerging-market bonds currently price in more Fed tightening than the Fed is likely to deliver, which provides a healthy cushion against interest rate volatility," he said. ■

Seven-time award winner TIAA on 2019: Volatile

Mixed-asset leaders see challenges, but no recession in the coming months

For an unprecedented seventh consecutive year, TIAA Investments has been selected as the Lipper Award Winner in the Large Company Mixed Assets category. TIAA Investments is the largest investment affiliate of Nuveen, itself a unit of insurer TIAA. The award winner manages many investment strategies, including the TIAA-CREF Lifecycle Fund and TIAA-CREF Lifecycle Fund Index series, which contributed to winning the mixed assets honor. Recently, *InvestmentNews* Content Strategy Studio spoke with representatives of the winning investment team — Robert Doll, Chief Equity Strategist and Senior Portfolio Manager; Frank van Etten, Chief Investment Officer and Head of Nuveen Solutions; and John Miller, who leads the municipals fixed-income strategic direction and investments perspectives for Nuveen. Their edited comments follow.



“In our annual 10 predictions for the year, we said we believe that 2019 will be choppy and frustrating, but that there won’t be a recession.”

Robert Doll, Chief Equity Strategist and Senior Portfolio Manager, Nuveen Solutions

INCSS: ***Wearing your hat as manager of the Nuveen Equity Market Neutral Fund, what factors are informing your choices this year?***

Robert Doll: Unlike most of the other equity categories, this is an absolute-return portfolio, so it’s the differential between our longs and shorts that provides the return. We hold about 100 stocks long and about 100 short, and the longs tend to be stocks that are relatively cheap, and the shorts tend to be relatively expensive. If we get the mix right more often than not, then we win. Since we believe the U.S. economy will do relatively better than other economies, and since our benchmark is the Russell 1000 Index, which is composed of U.S. companies, the long positions in our portfolio tend to be those companies that are domestically oriented while the shorts tend to have more international exposure.

INCSS: ***Putting on your hat as chief equity strategist, what do you see overall for the market in 2019?***

RD: In our annual 10 predictions for the year, we said we believe that 2019 will be choppy and frustrating but that there won’t be a recession. The economy overall is OK; it’s not great, but it’s good enough. The U.S. economy is slowing from about 3% growth to around 2%, but not every company is growing at that rate, and some companies are struggling with deteriorating margins, cost pressures and finding workers. There will be some good news coming from markets, but we will need a lot more good news for the market to go noticeably higher.

INCSS: ***Frank, you’re responsible for your firm’s multi-asset platform as part of the Nuveen Solutions group that you head, which also manages the TIAA-CREF Lifecycle target-date funds. Tell us what your group is doing and your forecast for the year.***

Frank van Etten: We see more volatility coming this year, but that doesn’t necessarily mean a negative market environment. As managers of a series of target-date funds, however, we have to look at things differently. We’re not aiming to beat a benchmark, and we have to put this year’s performance in perspective and consider not only the short-term and long-term outlooks for markets but also the long-term outlook of investors who may be in our funds for 40 years or more.

Our investors want to retire successfully, and our allocation decisions have a lot to do with making that happen. We believe that top-down decisions have a great impact on achieving the desired results, and our allocation decisions have to be right across asset classes, geographic areas, sectors, market capitalization and styles. Only by taking all those into consideration can we get the kind of diversification our investors need.

Continued on page S12

“Our investors want to retire successfully, and our allocation decisions have a lot to do with making that happen.”

Frank van Etten, Chief Investment Officer, Nuveen Solutions

SEVEN-TIME AWARD WINNER TIAA ON 2019: VOLATILE

Continued from page S11

INCSS: ***Tell us about the process you use to make allocation decisions for your target-date funds.***

FVE: The process starts with the glide path, which guides lots of decisions. We have a "through" glide path, as opposed to a "to retirement" glide path, and we're currently working on extending the glide path further to reflect greater longevity and because many participants stay in our funds after they leave work.

Although our focus is the long term, we have shorter-term views as well, and we adjust the portfolios accordingly. Because we expect more volatility and slower growth, it's appropriate that we go into sectors that are less volatile and into styles that are less sensitive to this stage of the market cycle. For that reason, we are now taking less risk in high yield and bank loans, for instance, and diversifying into other areas.

INCSS: ***What form does that diversification take?***

FVE: We're fortunate that we can benefit from TIAA's long-term strength in direct real estate. Currently, our target-date mutual funds are the only ones that have direct real estate in their portfolios, and while that was hard to accomplish technically, we absolutely love having it in the portfolio. Clearly, there are some times when real estate is more valuable than other times, but real estate provides diversification and can be a different source of growth, stability and even some inflation protection. Direct real estate constitutes roughly 5% of our portfolios generally, but it has had a real impact. It was the best-performing sector in our funds last year.

INCSS: ***Municipal bonds and other fixed-income investments play an important role in mixed-assets management at TIAA Investments. John, where do you see interest rates and the fixed-income market going this year?***

John Miller: While we're seeing the U.S. economy take a slower growth trajectory, we're not really seeing any signs that lead to a recession. We're migrating down to our potential growth rate of about 2% to 2.5% from an above-potential growth rate of about 3.5% last year, which created inflation fears and worries about overstimulation.

We're also observing slowdowns in the eurozone and Asia, and in China in particular. That means that the U.S. economy is outperforming advanced economies around the world, even if it is slowing itself. It also translates into a strong dollar and commodity prices pulling back, keeping inflation in check — and keeping the Fed from having to increase rates rapidly or dramatically. That has been helpful this year.

Corporate high yield has been the biggest beneficiary of this changed environment. The market sold off sharply in December on the theory that the Fed would overtighten. But now that the Fed has said it would take a more wait-and-see approach, high-yield spreads have tightened in what was probably the biggest snapback rally of all markets.

INCSS: ***What about municipal bonds?***

JM: Due to taxes, supply and demand dynamics and other factors that are different in different parts of the yield curve, municipal bonds don't necessarily move in sync with interest rates and other fixed-income classes. For one, the total amount of bonds that are called or mature each year are around $420 billion to $440 billion, compared with gross new-issue supply of about $338 billion. That means the market shrank by about $100 billion last year, which helped stabilize performance, and which is unlike the Treasury and corporate markets, where there is a lot more paper to digest.

> "This year, we've seen increased demand from retail investors, which likely is a result of the change in the tax law. The new law increased the effective tax rate on higher-income residents of states with income taxes, who now have limits on how much of those taxes they can deduct."
>
> **John Miller, municipals fixed-income strategic direction and investments perspectives, Nuveen**

This year, we've seen increased demand from retail investors, which likely is a result of the change in the tax law. The new law increased the effective tax rate on higher-income residents of states with income taxes, who now have limits on how much of those taxes they can deduct. This has raised demand for tax-free municipals.

As far as risk as concerned, the muni market with its more than 55,000 issuers is the most diverse, heterogeneous and fragmented of all asset classes. So, as difficult as it is to characterize the market broadly, the overall macro environment for municipals generally has been a tailwind, and we've seen more upgrades than downgrades. Any defaults we expect are more idiosyncratic in nature than symptomatic of broad problems. ■

How Thrivent helps investors 'be wise with money' through its mixed-asset funds

Expect interest rates to rise gradually, but no recession is in the cards

After three consecutive years as Lipper's Overall Fund Family winner among small firms, Thrivent Mutual Funds this year took top honors in the small-firm mixed-assets category. *InvestmentNews* Content Strategy Studio recently spoke with David Royal, President and Chief Investment Officer of Thrivent Asset Management, about the firm's approach to managing mixed assets and its outlook for 2019.

INCSS: ***You've described your mixed-asset funds as Thrivent's flagship products. Tell us why, and give us an overview of the funds and how they are managed.***

David Royal: Mixed assets are especially meaningful for us at Thrivent, which started as a fraternal benevolent society. Our overall mission is to help people be wise with money, and our mixed-asset funds are central to that mission, particularly in serving moderate-income investors. We have risk-based asset allocation funds that range from moderately conservative to aggressive, and three funds more focused on income, with zero, 30% and 50% equity exposure.

The way we think about mixed assets is shaped by who we are and our mission. We have 22 equity and 17 fixed-income analysts, which is a large number for a firm our size, and everything starts with bottom-up research. On the fixed-income side, we are credit driven and don't make duration bets.

In addition to our fundamental research, we have two big quantitative groups and another dedicated team of quant analysts that does nothing but work on asset allocation. We have a senior team of committee members that make decisions that are largely driven by quant factors. The majority of our alpha comes from bottom-up stock and credit selection.

INCSS: *What do you see currently?*

DR: As we look at the world right now, we see most things as kind of average, with assets fairly valued. We're not making big bets by asset class. Probably the biggest question mark we see is in international equities. Right now, U.S. market cap is at a 40-year high relative to total world market cap. At some point, that has to reverse. That makes European equities potentially attractive, but European fundamentals are currently awful, especially in German manufacturing. In fact, except for Brexit, the U.K. is stronger than the rest of Europe. We think it's probably a little too early to overweight foreign developed markets, and we're more optimistic on emerging markets, where we are modest buyers.

In the U.S., we don't see a recession coming in 2019. The weak retail sales we saw for December were probably an anomaly, and the risk in housing is low. In the past, market declines without a drop in corporate earnings — like the decline we saw this past December — haven't signaled a recession. We think the first quarter will probably be the weakest in terms of earnings growth, which should be in the high single digits for the year. We expect labor will squeeze margins a little. But this is not what an earnings recession looks like.

China is a wild card because it's so hard to get data. They're putting a lot of stimulus into the system, so I wouldn't be surprised to see China turn around. One of the best ways to see how China is doing is to look at Europe, which exports much more to China than we do. We think that much of the weakness in Germany in fact, is due to weakness in China that goes unreported in the official statistics.

> "One of the best ways to see how China is doing is to look at Europe, which exports much more to China than we do. We think that much of the weakness in Germany, in fact, is due to weakness in China that goes unreported in the official statistics."
>
> **David Royal, President & CIO, Thrivent Mutual Funds**

INCSS: *What about fixed income?*

DR: For 2019, we think rates will gradually rise. We have no bets on duration now. And we see rates being range-bound between 2.60% and 3.10% on the 10-year Treasury. Unless we see signs of inflation, we don't think rates will go much higher than 3%. We feel good about corporate credit generally, but if there is one area to watch, it's in the low triple-B range. If we were to have a bit of a slowdown, I'd worry most about that and question if I were getting paid enough for the risk. ■

$100M AMOUNT IN DEFAMATION LAWSUIT ADVISER ED BUTOWSKY FILED AGAINST CHARLES SCHWAB & CO., WHICH IS NOW HEADED TO ARBITRATION

Make room for next-generation advisers

GUESTBLOG
JONI YOUNGWIRTH

Recently, I read an article in the Harvard Business Review ("What Happens to Younger Workers When Older Workers Don't Retire") that got me thinking. It focused on the world of symphony orchestras, where many principal oboists are eschewing retirement. As a result, younger players are giving up, changing careers or lingering as a result of "slot constraints."

Sound familiar? It's something I see playing out in our industry as well.

If you find yourself struggling with the transition to retirement, or even thinking about it, these ideas may help you establish a plan, stick to it and make room for the next generation.

> **KEY POINTS**
> - Some advisers delay retirement past dates agreed to with the next generation, who is waiting to take over.
> - Advisers should set a date to exit and create a plan.
> - Concerns about decreased mental capacity should be checked out.

Set a date. Some tenured advisers hire less-seasoned advisers with the intention of retiring in a few years. But, inevitably, the tenured adviser decides to work a couple more years, and then a couple more, and so on. The young adviser burns out, stuck in a holding pattern. To avoid this, start by putting your retirement date in writing — and sticking to it.

Create a retirement plan. Try writing up a formal plan. You might include the extent of your work in retirement, relationships to be fostered, health and wellness factors, and passions you'd like to pursue.

Put it into practice. Once you have a general plan, put it into practice! Try making a list of things you've never gotten around to, and just start doing them.

Establish a firmwide "turnover date." As firms transition from solos to ensembles, the importance of addressing retirement age becomes increasingly important. Develop a turnover-date policy that applies to everyone, whether age 40, 50 or 60.

Get a mental health checkup. Accountability for spotting decreased capacity among clients is becoming critical. But we also need to be mindful of spotting it among ourselves. A periodic mental health checkup will help protect you, your firm and your clients.

Shift into a lower gear. For those not ready to stop working cold turkey, try downsizing to a limited number of clients, reducing compensation commensurately.

Explore the possibilities. Delayed retirement among advisers is something that many of us don't want to talk about. But I think it's time to have these conversations.

Joni Youngwirth is managing principal of practice management at Commonwealth Financial Network.

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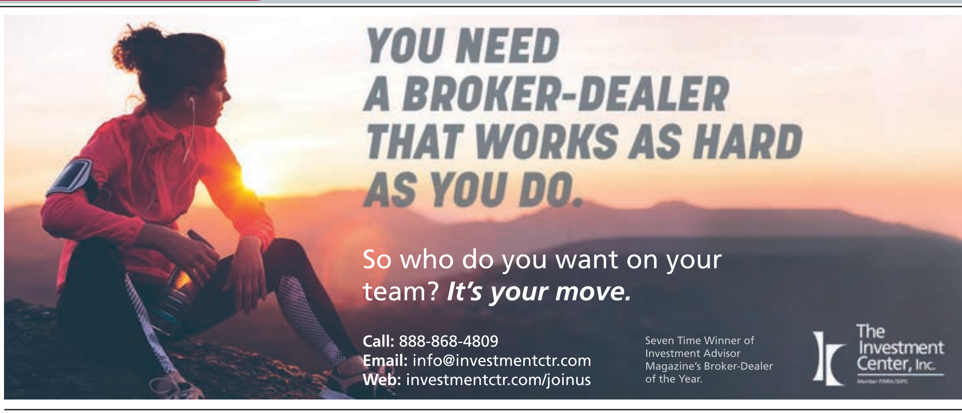

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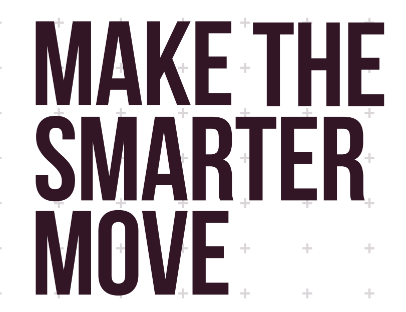


A farewell note to inspire the future of advice

BY ROBERT J. MOORE

Editor's note: The following is an edited version of a letter written by Robert J. Moore as he steps down for health reasons as Cetera Financial Group's CEO later this month.

DEAR VALUED members of the wealth management profession,

At the outset, let me express my sincere gratitude for the privilege to work alongside so many committed and talented individuals, whose collective efforts make a positive difference in the lives of millions of Americans, who want, need and deserve access to trusted advice and assistance in achieving financial well-being.

Second only to the role of the family physician, the role of the financial adviser is of utmost importance in assisting clients with navigating the complexity and uncertainty that we all face in planning for our financial future.

In addition, thousands of dedicated financial advisers serve their communities, nation and the world in countless acts of true charity and philanthropy. One of the most fulfilling aspects of working in this profession is seeing firsthand literally thousands of examples of the good works and best interests of clients delivered with a sense of dedication and humility that often goes unnoticed or unappreciated.

As I now prepare to move into the next chapter of my journey, I wanted to provide some reflection and introspection for a profession I have come to love, a purpose for which I am passionate and a challenge to those who follow.

Although there have been many changes and advances made across the profession, the pace and form of those changes have lagged the broader economic landscape and are in need of greater transformation at a more rapid rate than has been the case historically.

All facets of the client, adviser and provider experience are ripe for innovation and disruption. I have come to refer to this as the Advice-Centric Experience (ACE). At the core, the ACE is orientated towards a fundamental change in the way we engage with one another, liberated by technology and elevated by those who empathize with the roles of each participant. We stand at the dawn of delivering an experience that delights clients, supercharges advisers, streamlines providers and comforts regulators in a manner that allows for harmonizing and securing the best interests of clients we serve.

It is a vision for our profession that places relationships over transactions, solutions over individual products and outcomes over confusing comparisons with complex benchmarks. This is the time to collectively harness the energy and capabilities within the profession to focus on delivering financial well-being as the standard for our collective success. At the heart of this endeavor is a voluntary commitment to enhance transparency, reduce conflict, improve efficiency, and lower costs to preserve the value found in the advice given and the relationships built.

The primary barrier I perceive from my years of active involvement is the overemphasis on short-term performance and a startling level of inertia toward the status quo. Rather than recognizing the sheer abundance of growth opportunities, there is a preoccupation with moving deck chairs in the name of market share. Many of the competitive behaviors of late reflect a small-mindedness and lack of civility that are undermining the honorable nature of the profession and impeding progress.

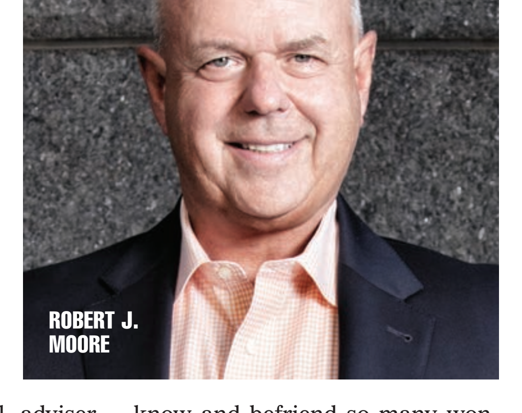
The challenge, therefore, to current leaders is to tap into the latent potential that resides within each person and unlock the energy that desires change and is able to transform the nature of our relationships into the reality of a comprehensive Advice-Centric Experience.

As I take this next step to focus on my health, I am keenly aware that my financial adviser will be a key member of my support team, and I will benefit from their wise counsel. This is an extremely personal example of the difference you make in the lives of so many.

It has been a distinct honor to know and befriend so many wonderful people who have enriched my life and for whom I shall always be grateful.

My sincere regards and best wishes,

RJ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CETERA PAY

CONTINUED FROM PAGE 2

niades said. "This is our chance to create a path for advisers who want to monetize that aspect of the engagement with clients."

Cetera will begin supporting fee-for-service with a small pilot group of advisers to collect feedback and make adjustments before offering it to all the roughly 8,000 advisers in Cetera's network. How advisers set and implement fee-based services is up to them, Mr. Antoniades said, and Cetera will not require advisers to offer it.

Cetera already supports a variety of business models for broker-dealers and registered investment advisers. Adding support for the fee-for-service model is part of Cetera's focus on what it calls an "advice-centric experience."

FEE COMPRESSION

While advisers accustomed to making a living by collecting commissions or charging an AUM may balk at the idea of collecting Netflix-style subscriptions, Mr. Antoniades believes charging for advice and financial planning will be increasingly necessary for advisers to withstand ongoing fee compression.

"Advisers are going to have to figure out ways to engage with more clients and to institute different pricing models," he said.

Charging fees for individual services doesn't have to replace commissions or AUM fees, Mr. Antoniades said. It can simply be an additional model to reach more clients, especially young investors, he explained.

Mr. Kitces of the XY Planning Network has been a proponent of the fee-for-service model for years, and said Cetera's adoption is the biggest indicator yet of a broader trend across the industry.

"Forward-looking broker-dealers are realizing that the whole industry is shifting away from product distribution and shifting to providing actual [financial] advice," Mr. Kitces said. "That's frankly a huge challenge for B-Ds. Legally, the reason a B-D exists is to facilitate product distribution."

This same challenge is driving change at other firms. For example, Commonwealth announced plans for an RIA division, and Wells Fargo is partnering with TradePMR to launch an RIA model.

But Cetera is the first large broker-dealer to "break ranks" and embrace the fee-for-service model, Mr. Kitces said.

LIMITED CUSTOMER POOL

The AUM model isn't going anywhere, but it limits the number of investors an adviser can work with, he said. Only a fraction of U.S. households have enough investible assets to make the AUM model worthwhile, and most of the assets are in 401(k) accounts an adviser doesn't manage. Then you have people that would rather manage their own finances than delegate it to an adviser.

> **"THE WHOLE INDUSTRY IS SHIFTING AWAY FROM PRODUCT DISTRIBUTION."**
>
> MICHAEL KITCES, CO-FOUNDER XY PLANNING NETWORK

The opportunity with introducing a fee-for-service model is not to compete for clients who can be served by the AUM model, but to make the adviser relevant to clients who can't or don't want to be.

"From an industry perspective, this is why I'm so bullish on fee-for-service," Mr. Kitces said.

AUTOMATING SYSTEMS

According to Mr. Antoniades, hundreds of Cetera advisers already charge for advice or financial planning, but are stuck using manual systems and collecting checks. Partnering with AdvicePay will help digitize and automate that, as well as encourage other advisers to offer financial planning services.

Some advisers will never make the transition, he said, but firms that can't support advisers who do will find themselves left behind.

"Our job is to create a platform that is capable of facilitating that transition for advisers who want to make that journey," Mr. Antoniades said. "We want to be ahead of the curve."

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UBS pursuit of rich Americans builds

BLOOMBERG NEWS

UBS GROUP PROMOTED 96 employees to the level of managing director in the Americas as it seeks to gain more rich clients and expand in the region.

The Swiss bank elevated 60 financial advisers and 36 Americas staff, according to Tom Naratil, co-president of UBS Global Wealth Management and president of UBS in the Americas, who posted lists of the promoted employees on LinkedIn.

UBS plans to expand by targeting billionaires, managing the complex fortunes of large families and boosting lending.

BIGGEST WEALTH MANAGER

The bank is the world's biggest wealth manager, with $2.26 trillion of assets under management, but its American wealth operations are smaller than rivals Bank of America Corp. and Morgan Stanley.

The division has an "extremely ambitious" plan to boost pretax profits by 10% to 15% over the next three years, Mr. Naratil said in a December interview.

TOM NARATIL

"We continue to strategically invest in the Americas as a key area of growth" Mr. Naratil said in a statement. "Our advisers are the most productive in the industry and these promotions are in recognition of their accomplishments."

FINANCIAL TARGETS

In October, UBS Group CEO Sergio Ermotti took a bolder set of financial targets to investors, pledging to drive wealth management profit higher and place the U.S at the center of a growth strategy that includes boosting lending to high- and ultra-high-net-worth clients.

MERRILL MARKET

CONTINUED FROM PAGE 2

rival firm, who asked not to be identified, said he recently lost a client to Merrill Lynch, in part because Bank of America is shaving half a percent from the client's mortgage to win a bigger share of the client's business.

"It's hard to compete," the adviser said.

Merrill Lynch is testing interest rate reductions for both new and existing assets in seven states: California, Connecticut, Florida, New Jersey, New York, Oregon and Washington.

Clients need to have at least $500,000 in deposits or investments to qualify for the half a percent mortgage reduction. New or existing clients with a minimum $250,000 in deposits or investments with the firm before a mortgage loan closes can receive an interest rate reduction between 0.125% to 0.250%, based on the level of new assets. The firm also is offering various reductions in closing costs and lender origination fees.

"Our strategy is geared toward deepening relationships and rewarding clients for doing more with us," said Merrill Lynch spokesman Matt Card.

As this column noted last month, Merrill Lynch is embracing the practice of cross-selling, which some in the financial advice industry regard with disdain.

Since the start of last year, Merrill Lynch has been paying its nearly 15,000 advisers extra for reeling in new households and getting clients to sign up for banking services like loans and deposit accounts.

> **0.5%**
> PERCENTAGE POINT OFF A BofA MORTGAGE FOR SOME CLIENTS

Meanwhile, many advisers abhor the notion of cross-selling. The business practice, particularly linked to sales targets, creates conflicts in a client relationship already fraught with conflicts.

Of course, Merrill Lynch is not alone among its competitors that want advisers to grab a bigger share of the client's wallet.

MORGAN STANLEY

For example, Morgan Stanley last year introduced a pay plan that goosed brokers and financial advisers to use a new, integrated wealth management platform to grab some of the roughly $2 trillion in assets its clients currently hold outside the firm.

Compensation drives behavior, as *InvestmentNews* industry columnist and headhunter Danny Sarch recently noted.

Advisers and investors need to keep a tally on the internal expenses charged at Merrill Lynch or any competitor when a client thinks about changing his or her broker-dealer while chasing what is being pitched as a discount.

A client may be offered a discount on a product like a mortgage, such as Merrill Lynch is currently offering. But the internal expenses of funds used in wrap accounts or managed money programs at the new firm could be higher, eroding or eating into what appears to be overall reduced costs for the consumer.

The question is, will Merrill Lynch's most productive advisers embrace cross-selling or be turned off by the firm tying it to their pay? The firm obviously loves the opportunity, but will the most senior bulls in the thundering herd share that love?

If Merrill Lynch sees an increase in experienced advisers leaving the firm in 2019, it may get the answer.

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VANGUARD TDF

CONTINUED FROM PAGE 3

fund fees are among the industry's lowest, at a cost of 0.09% on an asset-weighted basis for its Vanguard Institutional Target Retirement funds, tied with SSgA's Target Retirement funds, according to Sway data. Only Charles Schwab's Target Index funds are cheaper, at 0.08%. By comparison, the cheapest actively managed target-date mutual fund costs 0.51%, for TIAA-CREF's Lifecycle funds.

Also working against active funds right now is the fact that they performed worse last year, on an asset-weighted basis, than index TDFs, even though the stock market was down — an environment in which active managers are thought to show more relative value.

Passive TDFs returned an average -6.18% in 2018, compared with -6.56% for active funds, according to Sway. The S&P 500 was down 6.2% last year.

Passive TDFs now have better one-, three- and five-year asset-weighted returns than active TDFs, a reversal from a year ago. Those statistics could accelerate the flow of TDF assets from active to passive funds, Mr. Brown said.

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Millennial women take back seat in own finances

BLOOMBERG NEWS

MARIELLE SCHURIG spoke to a group of women at a wellness event at Lululemon Athletica Inc.'s store in New York's Flatiron district, after they'd sweated it out in a yoga and circuit-training class. Following her remarks, attendees lined up to talk to her about their finances.

The women told Ms. Schurig, 31, an account vice president at UBS Financial Services Inc., that they let their spouses or partners decide on money matters. Despite investing hours in self-care, many of the self-proclaimed feminists admitted that they had taken a back seat in their own financial affairs.

That's not uncommon: 59% of women age 20 to 34 defer investing and financial planning to spouses, according to a survey by UBS Group released last Wednesday. The Swiss bank found younger women are more likely than earlier generations to give such leeway to their partners.

"I was really surprised to see that," Ms. Schurig said in an interview at UBS' office in New York. "You see women fighting for equal rights and equal opportunities, for respect in the workplace and at home. There's all these women running for political office. We continue talking about breaking glass ceilings. But once we make the money and get those positions, what are we doing with it?"

UBS Global Wealth Management polled 3,652 women globally with a minimum of $250,000 in investible assets. Millennial women cite other responsibilities as being more urgent than investing and financial planning, according to the study. And younger women often don't include financial health as a factor in their well-being, said Ms. Schurig, a regular at SoulCycle.

"Women will spend a lot of time researching the best skin care, makeup product — they're not sitting down and examining their financial life," she said. "It'll be hard for us to be fully equal with men if we're not on the same financial page as them."

DAY-TO-DAY MONEY MATTERS

The study found that women are overwhelmingly involved in day-to-day money matters, with 80% paying bills and 85% regularly managing expenses. Yet all around the world, that engagement doesn't extend to longer-term finances.

"Women tend to take care of the daily bills, the budgets, and not the long-term planning," Kathleen Entwistle, 53, a private wealth adviser at UBS Financial Services who's been in the industry for 18 years, said at a presentation in New York. "It feels overwhelming to them. The idea isn't: Are men or women better? It's the dynamics of the way we've been taught, brought up, and the way we think about these things."

About 82% of women of all ages told UBS that they thought men know more about investing and financial planning.

In a separate S&P Global Inc. survey of almost 10,000 Americans, only 26% of U.S. women said they make investments.

Wendy Holmes, 47, a private wealth adviser at UBS Financial Services, said she hopes the latest findings will jolt more women into action. One of her clients, a single mother, had a memorable reaction to last year's survey.

"She said it was a serious wake-up call, and she wanted to be more engaged and to understand how she was investing," Ms. Holmes said.

RISK-AVERSE

CONTINUED FROM PAGE 4

the past 10 years through March 5, the S&P 500 Index posted an average annualized gain of 17.06%. Over the same period, the Bloomberg Barclays US Aggregate Bond Index had an average annualized return of 3.67%.

PERFORMANCE DISPARITY

That kind of extreme performance disparity is often what gives financial advisers fits when clients insist the stock market is too risky.

"I would suggest the No. 1 way to live on 5% of the investor's assets, without the risk of outliving those assets, is a variable annuity with a guaranteed income rider," said Tim Holsworth, president of AHP Financial Services.

"I see no future in a 100% bond portfolio, unless the distribution rate is in the 2% or 3% range," he added.

Thomas McCarthy, senior financial planner at McCarthy & Cox, said it is virtually impossible for most retirees to finance retirement without some exposure to the equity markets, which is why he often resorts to annuity products that tie up client assets and structured notes that expose investors to issuer risk.

"If someone is really conservative, they better have really low lifestyle expectations," he said.

While advisers typically reduce their clients' allocation to equities as they enter retirement, removing the growth potential of equities entirely can present challenges.

"You don't really outlive your money, but you can be forced to change your lifestyle if you don't have enough money," said Ashley Folkes, senior vice president at Moors & Cabot.

Mr. Folkes said he often sees clients who have worked with advisers on bank platforms who are so risk-averse they are reluctant to stray beyond five-year certificates of deposit.

For some clients, he said the answer is structured products that keep investors exposed to the equity markets but offer downside protection.

The trade-off for that downside protection is limited upside, which can also hurt long-term performance goals.

17%
AVERAGE ANNUALIZED GAIN IN S&P 500 OVER LAST DECADE

Mr. Folkes said his preferred method of dealing with ultra-conservative clients is a simple bucket strategy that divides the portfolio into near-term, mid-term and long-term sub portfolios.

The near-term bucket, he said, might be all cash and cash-equivalent investments that can cover living expenses for up to three years.

MID-TERM BUCKET

The mid-term bucket might have a three- to seven-year allocation objective, which will include some equity market exposure and is designed to replenish the near-term bucket.

The long-term bucket is where the riskier growth strategies are employed.

The key, according to Mr. Folkes is that the client is only focused on the certainty of what's in the near-term bucket.

Nate Creviston, wealth management analyst at Capital Advisors, is also a fan of bucket strategies for clients who don't want to think about stock market volatility.

"There are things that can be done, but you can't go to 100% bonds because any growth will be eroded by inflation," he said. "Even with our most risk-averse clients, we still need to have some allocation to stocks. The simple math with today's yields in the fixed-income space would see a retiree's money have a negative real return if they only invested in bonds."

Ed Butowsky, managing director at Chapwood Capital Investment Management, said unless the client has an oversized retirement portfolio, it will be difficult to finance 25 years of retirement on a bond portfolio yielding 3%.

"If the client is that scared of the stock market, you have to just go to fixed income and then continue to educate the client," he said. "You have to have things in your portfolio that grow."

Put another way, Harold Evensky, chairman of Evensky & Katz/Foldes Financial, said, "Unless you have enough money that you can bury it in your backyard, you need to be invested."

"Too often, people confuse certainty and safety," he added. "It may be safe to sit in bonds but the only thing certain is you won't have enough money once you adjust for inflation and taxes. The risk of being invested in a diversified portfolio over a long period of time is very small."

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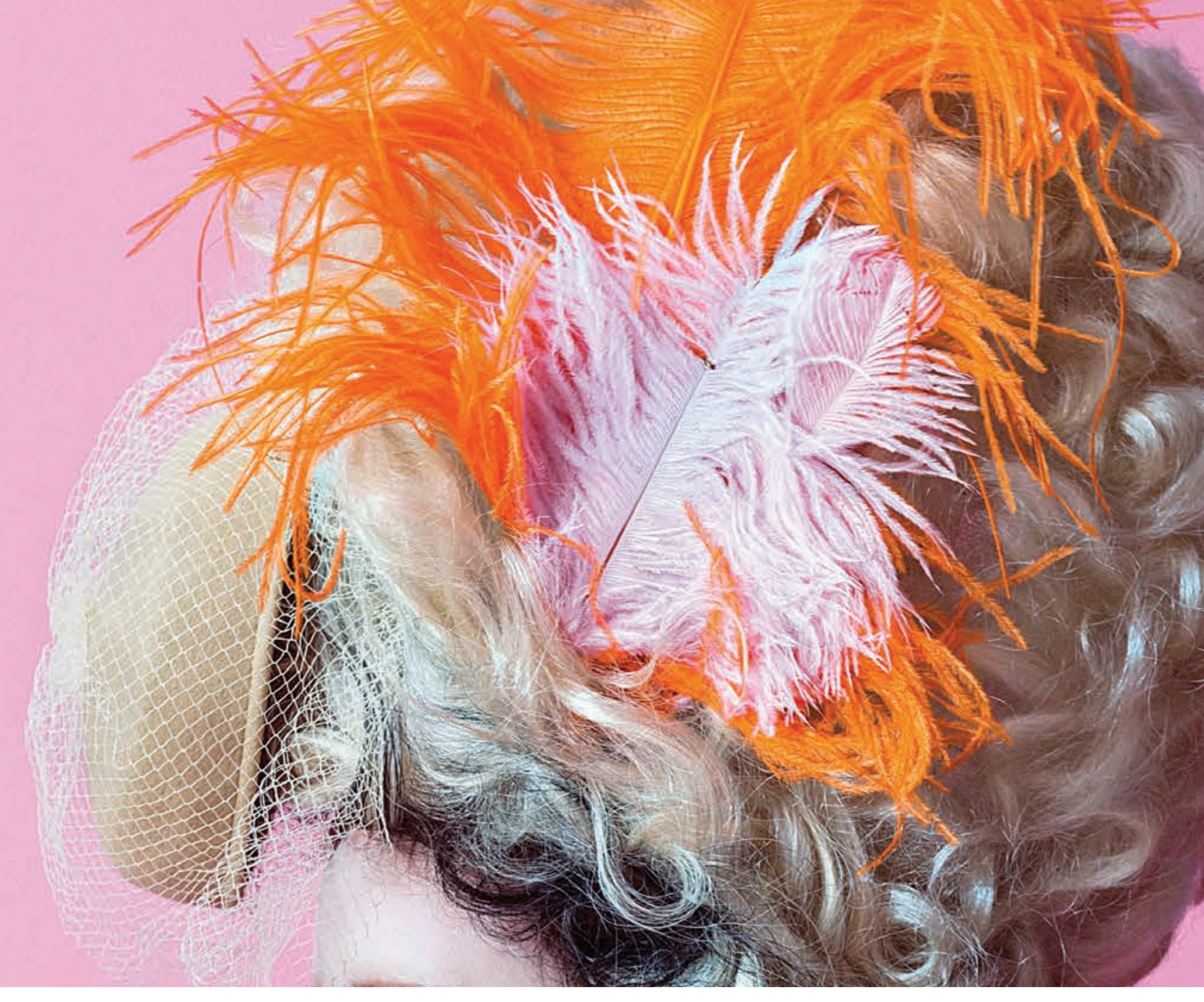

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