

NICSA NEWS

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Sizing up 2011 at NICSA



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This time of year is always a busy one for us—with the NICSA Annual Conference right around the corner. Scheduled for February 13-16, at the Doral Golf Resort in Miami, Florida, the 29th Annual NICSA Conference promises to be an important industry event. The theme, Sizing up the Future, captures the spirit of our industry—as firms measure current conditions, calibrate their position and calculate the algorithm for future success.

The conference will focus on the trends in fund industry, including changes in regulation, and how they affect operations and technology. Regulation and compliance will be a key element of the conversation this year. We'll discuss how the impending Dodd-Frank financial reform legislation and 12b-2 might impact the future, as well as look at issues around the implementation of already enacted legislation such as cost basis reporting, AML travel rules and FATCA.

Keynote speakers will include: **F. William McNabb III**, chairman and CEO of **Vanguard**; **George C.W. Gatch**, chief executive officer, **JP Morgan Asset Management Americas**; **Shlomo Benartzi**, professor and co-chair of the **Behavioral Decision-Making Group**, **UCLA Anderson School of Management**, and

chief behavioral economist, **Allianz Global Investors**; and author, Internet entrepreneur and technology expert **Scott Klososky**. **CNBC's Tyler Mathisen** returns to host our signature panel, Face the Membership, and **SourceMedia** editorial director **Tom Steinert-Threlkeld** will again moderate our CIO panel.

The 29th Annual Conference would not have been possible without the hard work of our dedicated volunteers. We want to thank Annual Conference Committee chairs **Lee Kowarski** of **kasina** and **Michael McNeill** of **Putnam Investments** who worked with exhibits co-chair **Lynette Turner** of **BNY Mellon Asset Servicing** and the Technology Committee, chaired by **Barbara Buchner** of **BNY Mellon Asset Servicing**, **Lisa-Marie Fitch** of **State Street Corporation** and **Sam Perone** of **Bank of America / Merrill Lynch**, to plan this year's event.

New for 2011 is a full day of pre-conference networking with a Sunday morning golf tournament on two of Doral's championship courses, followed by the barbeque lunch at the 19th hole. We end the day with the opening reception in our exhibit hall.

The conference does not fall on President's Day weekend this year, making travel planning easier and cost effective. We are very excited about the 2011 program and hope you will join us and be part of the important conversations in Miami.

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NICSA

Retirement Saving by Default

By Theresa Hamacher, CFA, President, NICSA

Retirement income security has been a key focus at recent **NICSA** conferences. Panels discussed trends in the design of 401(k) and other defined contribution plans at all three regional meetings this fall: at the East Coast meeting in Boston, the Midwest meeting in Chicago and the West Coast meeting in San Francisco.

The conversation will be continued at NICSA 29th Annual Conference & Expo on February 13-16, with a keynote address on the post-retirement crisis by leading behavioral finance economist, **Shlomo Benartzi** of **UCLA**, and a panel on how the industry can help clients retire in style.

It's an extremely important discussion, because the United States is facing the prospect of a large retirement savings shortfall. Without a change in course, many retirees will discover that they don't have enough money to support the lifestyle that they had hoped for—throughout a retirement that is likely to last

longer than expected, given the continuing increase in average life expectancy.

The shortfall is the result of decisions affecting both asset allocation and savings rates. On the asset allocation front, many retirement plan participants have had difficulty matching their risk-reward profile of their investments with their time horizons. For example, some take too little risk early in their working lives, placing a large portion of their retirement assets in low-risk money market funds—just at the time when they have the lengthy time horizon that would enable them to ride out the ups and downs of the stocks—and benefit from their higher long-term returns. Conversely, other plan participants may invest the bulk of their portfolio in stocks, leaving them a high degree of exposure to swings in the market—a good thing when the market is rising, but potentially catastrophic when the market

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declines, especially for participants near retirement age. Many near-retirees who had stock-heavy portfolios during the credit crisis found that they had to continue working well beyond their expected retirement date.

At the same time, many plan participants simply don't save enough to allow them to meet their retirement goals. Some workers don't enroll in their company's 401(k) plan at all and lose the benefits of tax-deferred saving and of their employer's matching contributions, equal to 2% of salary in the average 401(k) plan. (All statistics from the **Profit Sharing/401k Council of America's 53rd Annual Survey of Profit Sharing and 401(k) Plans**.) Other participants contribute only a small percent of their salary to the account—maybe just enough to earn the matching contribution. For those who are late getting started with their retirement savings, contributions at that minimum level won't be sufficient to fund a retirement that

now lasts an average of 18 years.

Fortunately, the work of behavioral finance economists shows that there's a simple way to address these problems—by making greater use of default options in plan design. (See the box on page 2 for an introduction to this relatively new field of study.) When a default option is in place, workers are automatically signed up for certain plan features—and only have to take action if they decide that particular feature does not make sense for them and want to opt out. The use of three different types of default options has skyrocketed since the **Pension Protection Act of 2006** specifically sanctioned them:

- **Default investment.** In 2009, 57% of all defined contribution plans used a target date fund as a default investment option. That means that salary deductions are automatically directed into an appropriate target date fund unless a participant instructs otherwise. Since the asset allocation of target date funds is designed to be age appropriate, this default option helps

ensure that the risk level in participants' portfolios matches their time horizon.

- **Automatic enrollment.** At 38% of firms new employees are now automatically enrolled in the retirement plan when they become eligible—most often with a 3% contribution rate.

- **Automatic increase in contribution rate.** Over half of plans now automatically increase a participant's contribution rate over time, sometimes by directing salary increases into the retirement plan rather than into a paycheck—an approach that has been dubbed a SMarT plan (for "Save More Tomorrow") by **Richard H. Thaler** and **Shlomo Benartzi**, two of its early proponents. At a plan that they studied, implementing an automatic escalator increased the average savings rate from 3.5% to 13.6% in less than four years.

Is an automatic escalator in your plan's future? Come hear Shlomo Benartzi at the **NICSA Annual Conference** in Miami to learn more about both the theory and practice of default options.

Efficiency Studies

Is the stock market rational or irrational? Or maybe both? Advocates of the Efficient Market Hypothesis argue that the market is a smoothly functioning machine, while behavioral finance economists contend that it's only as efficient as the imperfect human beings that invest in it.

For an overview of these competing views of the market, we've included two excerpts from *The Fund Industry: How Your Money is Managed*, by **Robert Pozen**, chairman emeritus of **MFS**, and **Theresa Hamacher**, president of **NICSA**. The book, an update of the definitive text on the fund business, will be published by **Wiley** in January 2011.

Acting Efficiently

Planning to spend Saturday night looking for a good stock pick? One group of economists—the advocates of the Efficient Market Hypothesis—suggests that you may as well go to the movies instead, since the search for undervalued stocks is just so much wasted effort. They argue that so many people are spending so much time researching possible investments that the market for any widely traded security is incredibly efficient. By that they mean that the price of a security already reflects everything that's publicly known about its earnings prospects.

They explain that their research shows that stock prices move in a random walk, in which tomorrow's change in price—up or down—has no predictable connection to today's price. For

example, if Windy Corner stock is selling for \$40 per share today, tomorrow it's just as likely to sell for \$41 as it is to sell for \$39. That's because today's price of \$40 incorporates all the public information about Windy Corner as a company and as a stock. As a result, any change in Windy Corner's stock price can only result from the release of new information, and investors can't tell in advance whether this new information will be positive or negative. In other words, to the disappointment of those trying to find a better deal in the market, the efficient market advocates suggest that there's no such thing as an undervalued security.

Financial Myth Busters

Researchers studying behavioral finance are the myth busters of the economics world. Their work is based on the premise that people don't always act rationally. While that may seem obvious, the assumption is a radical departure from previous work in the field. Classical economic theories—including the Efficient Market Hypothesis—are based on the idea that individuals always advance their financial best interest.

Behavioral finance research rejects that notion and demonstrates how people act in predictably self-defeating ways. Their studies have shown, for example, that investors are more reluctant to sell losing investments than winning ones, even if selling losing investments would help them reduce their income tax bill. They offer explanations for why stocks tend to go up on sunny days, down after the home team has lost in soccer's World Cup tournament.

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Upcoming Events

January 13
East Coast Regional Meeting
Hyatt Regency Boston
Boston

February 13-16
29th Annual Conference & Expo
Doral Golf Resort & Spa, A Marriott Resort
Miami

April 21
West Coast Regional Meeting
Offices of American Funds
Los Angeles

April 2011
East Coast Regional Meeting
New York

May 2011
Investment Operations Seminar
Boston

October 2011
General Membership Meeting
Boston

Webinars
December 8
Rule 206(4)-5: Pay to Play Rules

January 26
AML Regulatory Changes Impacting Mutual Funds: Insights Regarding the Travel Rule

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PRESIDENT'S LETTER

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The Fund Industry: How Your Money is Managed

I am so pleased to announce the publication of *The Fund Industry: How Your Money is Managed* (Wiley Financial Press, 2011), which I had the privilege of authoring with Robert Pozen, chairman emeritus of MFS. I truly believe that everyone working with mutual funds needs to read this book! It is the most in-depth and up-to-date guide to navigating the mutual fund industry around, written in an accessible style with many examples and charts.

The Fund Industry: How Your Money is Managed details how mutual funds are marketed, regulated, and invested in stocks and bonds. The book also describes the critical factors needed to choose a specific fund for your investment or retirement plan, including what to look for when reading prospectuses, shareholder reports and third-party reviews. In addition, the book:

- Discusses the spread of mutual funds to Asia, Europe, and Latin America
- Compares mutual funds to other investment vehicles such as hedge funds and ETFs
- Shows how to sort mutual funds by categories and subcategories based on security type and investment objective.

The Fund Industry: How Your Money is Managed will be available in February 2011 and can be pre-ordered now at many online bookstores, including Amazon, Barnes and Noble and Borders as well as through Wiley and NICSA. This

book is the perfect training tool—for an employee, a department or an entire organization. For a limited time, NICSA is offering deeply discounted member rates for individual and bulk orders. Watch your e-mail for information about how to get the book at the best price available.

2011 TA Compliance Guide

Another great resource for the industry, the *NICSA Transfer Agent Compliance Guide* has been newly revised for 2011 and will be available in March. To make the guide even easier to use, we've added a new section outlining all the changes made, along with an index.

You'll find updates on AML for the travel rule, Blue Sky rules, privacy regulations, Sarbanes-Oxley, SAS-70, lost/stolen/recovered certificate reporting, transaction processing requirements, signature validation program requirements, suspension of redemptions rules and transfer rules. In addition, we've included a high-level overview of cost basis regulations. You'll also find sections detailing everything you need to know about: 529 plans, privacy, lost shareholders, ACH, signature guarantees, IRAs, tax, administrative matters, and transfer agent transaction processing.

This comprehensive reference guide will be available in print, in electronic form and through site licensing agreement.

At this busy time of year, we hope you'll share our enthusiasm and excitement for what 2011 has in store. Thank you for supporting NICSA and best wishes to you and yours for a truly wonderful holiday season.

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ment and, more importantly, why out-of-favor stocks with low price-to-earnings ratios consistently do better than average. In an efficient market, stock prices would be affected only by new information and would not follow predictable patterns like these.

So, there is hope for active managers. By identifying these patterns of irrationality, they have a chance of

finding undervalued investments.

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