

THE SHERIDAN ROAD MAP

The Best Route to Financial Success



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Welcome to the Sheridan Road Map! Your source of monthly insight into the financial world. Sheridan Road provides a one stop financial solution for middle-market companies, their executives and employees. We are the premier provider of Corporate Advisory, Corporate Retirement Advisory, and Wealth Management Services, by providing holistic and independent advice to our corporate and individual clients. The Sheridan Road Map will provide insight into both historical and topical issues, a calendar of upcoming events, industry news and analysis, and a "Friends of Sheridan Road" section which often spotlights a new company that may be of service to our clients. "Let us help you navigate your Financial Road!" Visit us at www.sheridanroad.com.

BY THE NUMBERS

1. A Year to Forget- 10/9/08 marks the 1-year anniversary of the S&P 500's all-time closing high of 1,565. The low close for the index over the past year took place on 10/3/08 when the S&P 500 dropped to 1,099, off 29.8% from its peak.

2. From Top to Bottom- In the 9 bear markets for the S&P 500 since 1957 (not counting the current downturn), the average decline from the stock index's peak close to its bear market low close was 31.5%. The average length of time from the stock index's peak close to its bear market low close was 12.3 months.

3. Bad Month- The S&P 500 lost 8.9% (total return) in 9/08, its worst monthly performance since the stock index fell 10.9% in 9/02. The 2000-02 bear market lasted 30¹/₂ months and suffered through a 49% drop but the bear market ended 9 days after the September 2002 double-digit loss.

4. October History- Since 1990, October has been the best performing month for the S&P 500, up +2.2% (total return) on average. Six of the last seven Octobers have been up.

5. A Long Bull Market- The best performing bull market for the S&P 500 in the previous 75 years lasted 9¹/₂ years. From a low on 10/11/90 to a high on 3/24/00, the S&P 500 gained +417%.

6. Bearish Bonds- As nervous investors sold stocks and bought bonds last month, the yield on the 10-year Treasury note fell to 3.41% on 9/15/08 (i.e., price up, yield down), a yield drop of 0.61% since the beginning of the year. As the bond market came to grips with the immense size of the bailout measures proposed by the US government in the last month, concerns about the nation's rising debt level have pushed prices down and yields up to 3.83% as of 9/30/08.

7. RTC History- The eventual cost to taxpayers of the Resolution Trust Corporation (RTC ran from 1989-95) was \$120-140 billion, more than 70% less than the original \$500 billion cost estimate. The RTC was created to sell real estate assets from failed savings and loans.

8. Dubious Record- The government will release its budget deficit results from September, bringing a close to fiscal year 2008. It is anticipated that the final deficit number for the year will reflect a \$389 billion deficit, the 2nd largest annual total ever, trailing only the country's \$413 billion deficit from fiscal year 2004. Merrill Lynch economists are projecting a \$900 billion deficit for fiscal year 2009 and an \$825 billion deficit for fiscal year 2010. Fiscal year 2009 began last Wednesday.

9. They Will Regret It- 31% of current American workers have done no planning or saved any money for retirement.

10. Health Insurance- The average employee who purchases medical insurance through his/her employer will pay an estimated \$319 per month in calendar year 2009 for both their health insurance premium and for any out-of-pocket expenses. The projected 2009 cost is a +8.9% increase over the costs from calendar year 2008.

11. No Retirement at 65- 33% of American men ages 65-69 are currently employed for pay and 72% of the 33% are employed on a full-time basis.

Sources: 1-6, BTN Research; 7, NY Times, Denver Post; 8, Financial Times; 9, Principal Financial; 10, Hewitt Associates; 11, PlanSponsor.com, Congressional Research Service

THE NOT-SO-DISTANT FINANCIAL DYSTOPIA

In Michael Panzner's revised and updated book, *Financial Armageddon: Protect Your Future From Economic Collapse*, Panzner argues that America—and the world—are facing an all-out financial catastrophe; it's on the horizon—just beyond the “orgy of borrowing and extravagance,” an under-funded retirement system, a scary over-the-counter derivatives market and empty government guarantees.

From Registered Rep's June 1, 2008 interview:

Registered Rep: In your book, you say the world is now a riskier place, that the modern financial system has made it riskier—and not less so, as has been advertised.

Michael Panzner: Yes, financial markets are riskier, but it's also part of a broader attitude: People assuming they can [take more risk] and worry about it less.

RR: We've seen it in spades with the credit market debacle.

Panzner: Yes. We're clearly seeing the unraveling, the deleveraging process, taking place now. When I was writing the book, investors were in peak euphoria, and people thought there was no limit to the amount of leverage they could have. Clearly that attitude's changed, and I think those attitudes will become even more entrenched as time goes by. But it was at every level of the financial community—you know, investment banks, commercial banks, etc. Everybody was operating under the assumption that they could take on tremendous amounts of borrowed money and capitalize on that without paying the piper in any form.

And you also have the same thing going on at the consumer level. American households are stretched in terms of the size of their outstanding debt. Many will have trouble meeting those obligations going forward. And then you throw in the government side of things. Look at the extent of both the published obligations, such as government debt, and also the government's retirement-related obligations. Some argue that retirement obligations aren't quite the same thing as a Treasury bond, but I'll be anxious to see what happens with all those people who are older and nearing retirement when the government says, “We can't afford your Social Security, and we can't afford your Medicare.”

RR: Are you saying the United States is bankrupt—too many future obligations—but no one's willing to admit it yet?

Panzner: I think people are starting to recognize it. In fact there was a very interesting commentary in the Federal Reserve Bank of St. Louis Review, published in the July/Aug. 2006 issue, written by Larry Kotlikoff, an economics professor, saying the United States is bankrupt. At the time the article came out, I think most people would have thought of the article as an abstract hypothesis and not a reality. I think more and more

people are coming around to the idea that, yes, we're talking bankruptcy in a literal sense. We may have to worry about that. And I think that's been a dramatic change.

RR: Why are Treasuries not being sold off then? There are always some doom-and-gloom commentators predicting the worst.

Panzner: Others have written books that predicted hard times ahead, probably in every decade. In many cases they were proved wrong. I think the difference this time around is that there are so many bearish ducks lined up in a row. You've got enormous leverage in the financial system, in terms of the derivatives market, which, as we've seen in recent months, is turning out to be almost a black hole of losses bleeding Wall Street and Main Street dry. Then you have the fact that the first Baby Boomer signed up for Social Security. That's the demographic tsunami that people have been warned about: the graying of America. In fact, it's a big problem in many countries.

And you also have this issue with the currency: The dollar has lost its place as the world's reserve currency. I think there are clear signs that the United States' role, its long-term role as an empire, is losing steam. Historically, that's what happens: Empires come and go.

So you put that all together, you put all these sort of imbalances and problems and obligations—this whole general idea of living beyond your means—and I think we're at a moment in time where we are going to see a dramatic change in the outlook for this country.

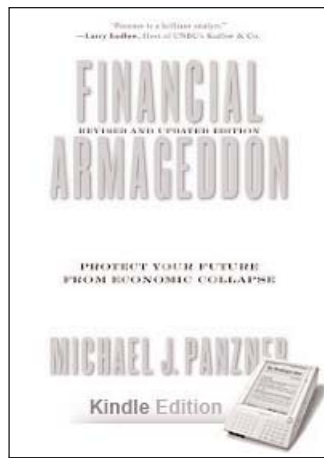
RR: Well, where's everybody else? Why aren't there more people saying what you're saying?

Panzner: It's very interesting. A year ago, many people—especially in the mainstream—had the impression that I was ‘out there.’ But now, a year later, my book *Financial Armageddon* isn't as crazy as it sounded a year ago. All of a sudden you see articles about the stuff I was talking about—derivatives and leverage—in mainstream publications. So, yeah, I was a bit ahead of my time, and I like to think that it's because I put the big picture together.

RR: What were some of the signs that led you to this bearish opinion?

Panzner: The number that really stuck in my mind was total debt, which is really the collection of total public and private debt. Mind you, that statistic doesn't include things like Medicare, Medicaid or Social Security, but outstanding debt—which includes the public and private sector. That number was something on the order of 300% of GDP. That was a few years ago. Total debt now is about 350% of GDP. The last time we saw those kinds of numbers was during the Great Depression.

And then I started to do some more digging, and I saw



NEW EMPLOYEE BENEFIT: FINANCIAL ADVISER

Recently, on the advice of her financial planner, Jeri Allan rebalanced her 401(k) portfolio, slashing in half her big allocation in large-company equities, which was heavy in IBM stock. Who paid for this advice? Her employer, IBM.

Ms. Allan, a 24-year veteran of IBM Corp., has been receiving monthly 90-minute sessions with a financial expert, as part of IBM's Money Smart program launched last year. The program aims to help employees with planning for retirement, managing their investment portfolios and other money matters.

Such counseling would have cost her between \$100 and \$300 an hour with an adviser, according to figures from Garrett Planning Network, an association of fee-only planners.

The program is one of a number of efforts employers are rolling out to offer more-comprehensive financial advice to workers. Previously, most companies had done little more than distribute informational brochures and post tips and tools on their Web sites. In recent years, prompted by a broad-based shift from pensions to defined-contribution plans such as 401(k)s, many employers have been providing workers with access to personalized services. The newest offerings are a free employee benefit and include one-on-one counseling and in-depth seminars provided by contracted professional advisory firms.

Employers say that most workers don't have the time or expertise necessary to comprehend their financial options. "If you're going to offer employees choices in your health-care and retirement offerings, then you have some obligation to give them an education to make those choices," says John Berisford, senior vice president of human resources at Pepsi Bottling Group, which offers a similar program to IBM's.

But some legal and human-resources experts caution that workers should be careful about availing themselves of services provided through their employer. It's easy to have a false sense of security because any investment can go sour. In the past, many companies have been reluctant to offer financial guidance to their employees—for fear workers could sue if the results were poor. A 2006 change in pension law offered employers some protection from liability, so workers' chances of getting redress from their employer if they're dissatisfied are now slim.

Employers say that the support they're providing is strictly instructive and doesn't involve sales pitches or give advisers free rein over workers' assets. Such restrictions are typically outlined in the contracts signed between employers and advisory firms. The pension law requires that employers thoroughly vet advisory firms to ensure that they're qualified to provide support that best serves workers' interests.

Employees, some of whom may never have had one-on-one financial counseling before, may be unaware of what they can ask. Others may press an adviser to offer deeper insights, or give information about products other than what the program is designed to provide.

Randall MacDonald, senior vice president, human resources at IBM, says the company completed a rigorous evaluation before selecting Ayco Co., a division of Goldman Sachs.

No-nos include making product recommendations and advising on specific mutual funds, stocks or other investments, says Ayco's Meg Keyes, senior vice president for financial-related services. The advisers will, however, go over the pros and cons of particular types of funds or stock sectors and provide a list of funds that the firm analyzes.

IBM employees have been placing about 4,500 calls a month to Ayco's counselors. Employees' spouses are also welcome to call, and consultations last an average of 30 minutes.

Pepsi Bottling Group's program, called Healthy Money, is in partnership with PricewaterhouseCoopers LLP and has been rolled out over the past 20 months for the beverage company's 28,000-person U.S. work force. Some 600 employees have participated in

confidential phone counseling and roughly 8,000 have attended in-depth workshops on everything from controlling credit-card debt to saving for college tuition.

Barbara Naughton, a senior accounts-receivable manager at Pepsi Bottling, attended a personal-finance seminar held in March. What she learned about financial moves as you near retirement prompted Ms. Naughton, 58, to rearrange her retirement portfolio, she says. She was also inspired to pay off her credit-card debt with savings to avoid interest fees. As a result, she now expects to meet her goal of retiring comfortably around age 65.

IBM and Pepsi Bottling Group's programs are among the most customized. The financial experts running them are versed in the specific financial-related benefits that each employer provides, such as 401(k) investments, life-insurance plans and other savings vehicles. IBM's program is expected to cost around \$50 million the first five years, says Mr. MacDonald.

Other large employers, like Microsoft Corp., Caterpillar Inc. and Convergys Corp., say they have added more sophisticated financial-education benefits in recent years. Meanwhile, many midsize and small businesses have been doing the same.

Companies say that in addition to helping retain workers, an advanced financial-education program can benefit the bottom line. "You typically have a highly productive, satisfied employee [because] you've eliminated an enormous stress from their life," says Mr. MacDonald.



NEW STANDARDS, NEW SCRUTINY FOR 401(K) PLAN AUDITS THIS YEAR



Do you remember the first time you met your spouse's parents? They wanted to know everything about you. There was a barrage of questions as they closely examined your past and assessed your prospects for the future. Well, you're likely to find yourself in a similar situation this summer, but now the interrogator will be your 401(k) plan auditor. That's because new, stricter audit standards, known as the "risk assessment standards," now apply

to all audits. For calendar year 2007 401(k) plans, this will be the first audit under the new standards. The new audit will be quite a departure from previous years. Never before have so many new questions, documentation, and evaluations been required. The bottom line: your audit will take longer and demand more of your time.

You can blame the tougher standards on Enron and its ilk. The American Institute of CPA's (AICPA) tightened standards in the aftermath of widespread corporate accounting fraud in the early part of this decade. The new standards extend to all audits, including audits of employee benefit plans.

Plan sponsors are generally required to file an employee benefit plan audit if the plan has 100 or more participants, under the Employee Retirement Income Security Act of 1974 (ERISA). The audit is submitted as part of the plan's annual return/report (Form 5500) to the Employee Benefit Security Administration (EBSA) of the U.S. Department of Labor. If the audit is incomplete or substandard, you, the plan sponsor—not your auditor—bear the fiduciary responsibility and liability, including personal penalties. Deficient audits are surprisingly common and are found in approximately one-third of the one million audits filed each year, according to EBSA. Therefore, you should be more diligent than ever in managing the plan audit process. That starts by knowing what to expect.

What's Different This Year

The new risk assessment standards require the auditor to assess the likelihood that the plan sponsor would make a material misstatement on the plan's financial statements, either because of weak internal controls or unauthorized transactions. Simply put, the auditor is now looking at the business, not just the books. For example, a cash-strapped company may have difficulty depositing employee contributions on time. Therefore, auditors are obligated to gain an understanding of the plan sponsor's business and its operating environment, including:

- External factors, such as competitive environment as well as supplier and customer relationships
- The nature of the entity's business, including its operations, ownership, and governance
- The entity's objectives, strategies and related business risks
- Measurement and review of the entity's financial performance
- The design of internal control procedures and whether these procedures have been implemented and are operating effectively

As you can guess, more time will be spent making inquiries of management and employees, reviewing processes, and detailing transactions during the course of the audit. Management should expect auditors to ask detailed questions concerning internal controls, requesting copies of documentation showing that controls discussed have been truly implemented, and observing or walking through controls to determine if they are operating effectively. The auditor will observe controls that cannot be verified merely by inspecting documentation. Auditors also must evaluate management's attitudes towards the importance of internal controls and its impact on timely and accurate financial reporting.

Custom-Designed Audits for Each Plan Sponsor

All of this work occurs before the actual audit begins, because each audit now must be tailor-made to focus on areas judged to contain the highest risk. In the past, auditors had the option of using a "default" audit to the maximum level of control risk. This is no longer an option. The auditor is obligated to design a customized audit whose nature, timing, and extent will depend on what risks the auditor uncovers during the risk-assessment phase of the engagement. Based upon the high-risk areas identified, the auditor will develop further audit procedures that are designed to reduce the risk of material misstatement to an acceptable low level. The auditor will examine that plan transactions and asset balances are presented in accordance with generally accepted accounting principles.

In addition, the AICPA now details what your auditor should do to sufficiently document audit procedures—a process that had not been explicitly defined previously. Poor audit documentation is one of the most common reasons that audits are found deficient by EBSA, and now the work papers must be more explicit than ever. SAS 103, Audit Documentation, requires that the audit documentation be sufficiently detailed to give experienced auditors a clear understanding of the work performed, the evidence obtained, and the conclusions reached. This standard clarifies that verbal explanations do not, by themselves, provide sufficient support for the auditor's work. Auditors will have to spend extra time fully describing the procedures they perform and how the information supports their conclusions. In addition, plan sponsors may need to provide more documentation to be included in the auditor's files.

NEW STANDARDS *(continued from page 4)*

SAS 103 also states that auditors can prepare their reports but cannot date them until they have sufficient, appropriate evidence to support the opinion. Sometimes this evidence may not be ready for months. Consequently, the auditor will have to update the audit report to include subsequent events testing up through the report date. This additional audit work will be factored in audit fees.

Better Communication Counts

The Department of Labor is not the only entity that will get more detailed reports. Now your auditor is charged with clearly communicating a number of things to the people in charge of the plan's governance. Specifically, SAS 114, The Auditor's Communication With Those Charged with Governance, details what auditors should communicate with those charged with governance, such as a plan trustee, pension committee, or audit committee, who will bear responsibility for the audit. At the start of the audit, the auditor must provide an overview of the timing and scope of the audit. At the conclusion of the audit, the auditor should communicate significant audit findings to those charged with governance. Comments may be along the line of difficulties encountered in the audit application of accounting principles, noteworthy client estimates made, and other important matters.

Another standard, SAS 112, Communicating Internal Control Related Matters Identified in an Audit, became effective for Plan Year 2006. It requires the auditor to communicate in writing an assessment of your plan's internal controls on an annual basis. The SAS 112 letter outlines certain deficiencies or weaknesses in your plan's internal controls, called control deficiencies. A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. (Note: SAS 112 does not require your auditor to search for control deficiencies, but rather to evaluate them if they have been identified.)

SAS 112 stipulates that identified deficiencies must be communicated every year in which the deficiencies existed, even if your auditor had previously communicated them to you. These communications are private communications between you and your auditor. However, if the Department of Labor is performing a compliance audit on your plan, they may request to see any such communication from your auditor.

By Jan Altman, Greg Auteri, Michael Friedman, Vincent Gaudiuso, Ken Perlman, and Dominic Rovano • Defined Contribution Insights, July/August 2008

NOT-SO-DISTANT FINANCIAL DYSTOPIA *(continued from page 2)*

debt payments as a percentage of income statistics at record levels. Then I got my mind around the extent of the real estate boom. Clearly, there were a lot of people who were saying there's no bubble there—in the Fed, in the mainstream media, among the economics fraternity. But it had all the hallmarks of a bubble. So what do you get? What causes a bubble? To a great extent it has to do with debt. It has to do with people's willingness to borrow much more than they can afford because they just believe that the price of the asset will keep going up forever. In my mind, the inflation of the housing bubble and this level of debt—which has not been seen for 80 years or so—just struck me as a sort of wakeup call.

RR: What should financial advisors do? What should they be doing for their retail clients?

Panzner: As Will Rogers said: "Don't talk to me about return on capital, talk to me about return of capital." And I think that's the kind of mindset that you need to focus on. A lot of people are going to be looking and saying, "Well, I can't earn enough yield, or I can't get enough in capital gains," and, in the end, have real problems getting their money back because they've invested in something or invested with an organization that really had many more risks built in than they thought. It's a time to think defensively.

I think this is where equity investors are making a huge mistake: Everyone still thinks this is a garden-variety environment. But when you had crises in the past, you wanted to buy the dip because there were always buying opportunities. When you have had companies taking big write-downs, you want to buy because that's a signal of the beginning of the end. But few investors are putting the write-downs in the broader context that you have this huge housing bubble collapsing and there's no bottom in sight.

So I can tell you for sure that if the housing market has five years more downside left, there's going to be a lot more write-downs, a lot more pain and a lot more financial institutions going belly-up. Therefore people are not thinking about this in terms of the broader economic fundamentals; they're just doing knee-jerk trades based on what's happened during the Greenspan bubble era.

By David A. Geraciotti • Registered Rep., June 1, 2008



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