



## **Headline Hazards - Don't Forget the Small Print!**

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"The Devil is in the details" - German proverb

As advisers, all of us may have varying opinions about the short-term and longer-term effectiveness of the Federal government's very active recent intervention efforts to assist credit markets, bank liquidity and general financial system consumer confidence. Nonetheless, there shouldn't be any disputes about the importance of advisers understanding *all* of these programs' key facts versus the headlines' impressions on how these programs work to deliver accurate, advantageous advice to your clients. The headlines and the three to six bullet point summaries in the CNBC bottom banner or in news web site headline summaries are definitely not complete enough to draw fully accurate conclusions. More importantly, the headlines on their own can be very misleading.

This week's announcement of the infusion of up to \$250 billion of new capital into U.S. controlled banks by the government joins a myriad of other Treasury, FDIC and Federal Reserve announcements of new programs coming out almost weekly since mid-September. The very first news headlines I saw on the newest upcoming infusion of bank capital was a news alert in my email that roughly read something like "U.S. to partly nationalize nine largest banks." Well, I think it is fair to say a program that is ostensibly voluntary (banks can decide by November 14th to participate or not) and involves the issuance of senior non-voting preferred stock at levels that can't exceed \$25 billion or 3% of any given issuing institution's risk-adjusted assets, isn't really the same as an even partial "nationalization." Also, the issuing bank can buy back the preferred stock after three years - the government's money doesn't have to be part of even their long run capital structure, although the government does get some warrants to buy some common stock, but is far from a controlling interest.

The specific new Treasury department actions that prompted this email related to some very misleading media headlines that were used, as the government desired, to calm investors on September 19, 2008 and to stave off a redemption run that started that week on non-government securities money market funds. With several major brokerage firms teetering, and the Reserve Fund "breaking the buck," suddenly that little footnote on your brokerage statements next to your money market balance that said "not FDIC insured," seemed to mean a lot more.



The Treasury department said to themselves, something like, "We have to fix that, or no one will be able to roll over their commercial paper, regardless of their credit quality." A reasonable concern.

So the headline rolls across the CNBC screen: "Treasury to insure all money market account balances," "Whew!" goes the money market fund managers and the holders of those types of funds. That hole in the credit market is plugged, now on to the next crisis. The commentators note the Treasury insurance program is only for a year. Your clients still breathe easier. All is good on at least the money market fund side, right?

A couple of weeks later, and the market starts its rapid decline, and finally a few of your clients, despite your advice to the contrary, literally can't sleep any more, and one of them says, "Liquidate half of all my equity funds, leave it in my account, and we can put the money back to work when I think we've gotten near a new bottom, but right now I just can't risk any more of my capital." Or, take another client who was thinking of moving cash in their brokerage money market account into CDs but doesn't because of the Treasury money market insurance announcement. That same client notices the odd yield relationships of municipal money market funds with seven day yields of 4.6% compared to 2.1% for taxable money markets, and instructs you to switch her \$75,000 to the muni money market fund, since the Treasury has insured that fund too, correct? You double check your client's brokerage firm announcement that they are participating in the Treasury insurance program on all their funds - so that part seems fine. Funny, that the first headline on this announcement, I mean that very first one on CNBC, not the revised one later that day, didn't mention money market funds had to sign up and pay some premiums to be in the Treasury's insurance program.

If, while attempting to calm clients with phone calls during the most volatile down days in the market, you only relied on the initial news headlines, before the details were published on the Treasury website on September 29, 2008, and before in the quiet of the evening you'd actually read those details when released, you could have missed seeing that there was a big problem in those clients instructions to you.

It turns out that only the total shares in a client's money market fund **as of the close of business on September 19, 2008**, (if that fund joined the insurance program by the October 8, 2008 deadline) had *any insurance*. The first client example cited above had \$100,000 in a money market fund on September 19, 2008, and sometime in the middle of the first week in October sold half of his equity positions for \$500,000 and let that money sit in the money fund for now. By leaving \$600,000 in the money market fund, he should know he only had Treasury insurance protection on his money market assets on the first 100,000



shares - the ones in the account on September 19, 2008. So much for money markets being backed by the government!

Possibly worse, if you didn't alert the client in the second example that **by switching her \$75,000 to a municipal money market fund, that client now has zero Treasury insurance protection**, even if the municipal money market fund the client switched to is in the same fund family. If these funds had "broken the buck" imagine how the clients and you would feel about what happened with money thought to be insured!

Now there is an announcement that all FDIC insured checking accounts will have unlimited balance protection through 2009. I will say, most of the headlines on that announcement I saw did insert the important qualifier, "non-interest bearing" deposit accounts only have the higher coverage, and pointed out the FDIC was trying to slow corporate deposit account withdrawals. But in this case, the FDIC emphasized that point in their original announcement.

Bottom line: a lot of new government programs intended to help your clients regain faith in major and minor depository and credit granting institutions are coming at us right and left. In terms of specific impacts, advisors need to go past the headlines and think through the ramifications once ALL the details of a program are digested. In the example above, in which the client moved money into a municipal money market fund, if the safety of principal is the dominant concern of the client versus the higher yield, the client can put money back into the original money market fund, and be protected up to the full \$75,000 they had in that fund on September 19, 2008.

Below are links to the Treasury department's details on the money market fund program. Some of the key points not obvious in the headlines I've seen were:

- Only money market funds with an end of day NAV on September 19, 2008 above \$0.995/share were eligible for the program.
- The program is voluntary and carries a 1 to 1.5 basis point insurance premium cost to the participating fund - *you need to verify your client's money market fund is participating.*
- The clients *cannot get Treasury protection on increases to their money market balances after September 19, 2008*, including any reinvested interest. By moving money around into different money market funds, clients could jeopardize any insurance protection.



- If your money market fund "breaks the buck," the Treasury protection is calculated this way: They compare the shares you held in the money market fund the day the NAV fell below \$1.00 to the shares you held on September 19, 2008. The lesser of those two share amounts are multiplied by the difference in the \$1.00 NAV and actual NAV, and the result is the amount of your insurance benefit. The remainder of the money you get back is at the liquidating below \$1.00 NAV from the fund company, not the Treasury.
- The insurance program isn't really for one year; it is only for the three months ending December 19, 2008, and at that time the Secretary of the Treasury can extend the program for up to another nine months or terminate the program. If he chooses to extend the program, each fund is responsible for signing up for the program again, and paying another insurance premium to receive the protection. So you should mark you're your calendars to watch for Treasury announcements on that date.

Take time to get past the headlines, into the facts, and then translate those facts into meaningful advice for your clients - that is the future of financial advising.

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