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Economic Commentary

Recent geopolitical events have created a great deal of angst among most. The claims of responsibility for the Paris attacks and the Russian airliner bombing by ISIS have many questioning the extent of the chaos and the scalable potential for its expansion. The mass migration of Syrian refugees is reaching astronomical levels, and the human suffering is unbearable to watch. As Americans, we want to know who is at fault, what is the solution and when will this condition be fixed. Unfortunately, the answers are not simple and, therefore, the solution will not be readily at hand. Let's start with the creation of ISIS.

Several months ago we referenced the death of the Islamic prophet Mohammed in 632 as the beginning of a rift in the Muslim religion. The split was about who would succeed Mohammed, which eventually led to war in an attempt to force the succession solution. Most religious wars, or all wars, are about power and control. While there are many nuances within the reasons for the internal conflict within Islam at the time, the two major differences were that the Sunni faction believe in the power of the Caliph as the supreme authority of interpreting the word of Allah, and therefore the teachings of the Quran, while the Shiite or Shi'a place divine authority in the Imams of the religion.

Globally there are approximately 2.5 billion Muslims, and approximately 90% are Sunni. From a global perspective you can pretty much surmise that Shi'a feel that they are in the minority and perhaps oppressed. Geographical situation does, however, come into play. Shi'a is the majority in Iraq and Iran — Sunni dominate in all other Islamic countries in the middle east.

Sunni purists, some would argue extremists, believe that Shi'a are apostates or defectors of Islam and, therefore, infidels who must be eliminated to form a pure Islam. Interpretations of supreme authorities and, therefore, "acceptable belief practices" have persisted throughout history in many religions, and have been responsible for man's inhumanity to man for thousands of years. Some have waged power struggles and wars because of fervently held beliefs, while others were simply in the battle for control, power and the ability to subjugate. The emergence of ISIS in the early 2000s was due to several factors, one of which was the opportunity for Sunni

Commentary, continued

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dominance and control in Islam.

Atrocities and sectarian and even tribal violence between Sunni and Shi'a within the middle east has a rich and constant history; however, for the most part it was controlled by strong oppressive dictators who had a bigger hammer than those waging the sectarian strife. Saddam Hussein was born Sunni and while most of his government leaders were Sunni he was equally brutal to all dissenters. To be certain, the Shi'a majority was shut out of the governing process and threatened by the Sunni minority, but the common fear was Saddam and his regime rather than occasional Sunni-Shi'a conflict. The same could be said for Syria and Libya.

Power changes create voids or vacuums. The question is not *if* those vacuums will be filled, but *by whom*. The overthrow of Saddam in Iraq, the war in Afghanistan against Al Qaida and the Taliban, as well as the infamous Arab Spring that resulted in Muammar Gaddafi's demise, launched the perfect opportunity for voids to be filled by religious zealots as well as those seeking simple and brutal power. The process of filling those voids was the creation of ISIS.

We have cautioned before that countries with great military forces are rarely great at nation building. Power voids require combinations of strong security and even stronger efforts at nation building. While the security efforts can be accomplished with strategies, tactics, equipment and forceful execution, nation building is more difficult and requires listening, negotiating, empowering, legitimizing and creating opportunities for tomorrow to be better than it was today. Absent of hope and security, the average citizens in countries with power voids have limited power to control their own destiny.

When the transitional government in Iraq was formed, the Shi'a majority understandably shut out their oppressors and the Sunni and sectarian violence increased. We were slow to force a more collaborative and inclusive government and the US received the reputation of being a Shi'a ally and protector and, therefore, a roadblock to the Sunni extremists who viewed us as aiding the apostates or those getting in the way of a pure Islam.

Putin's loyalty to Assad in Syria, and the Russian military's bombing of ISIS groups in Syria, earned Russia the same reputation as the US. The ISIS paradigm is simple — you are either with us or you are an infidel who deserves death — and, thus, over 340 innocent people suffered the consequences of a suicide bomb being detonated on a Russian airliner. Similarly, over 120 innocent people were gunned down on a Friday evening in Paris due to the French participation in a coalition of forces trying to address the Syrian civil war and attending refugee crisis.

The definition of terrorism comes from the French word *terrorisme*, originally meaning “state of terror,” which in turn derives from the

Latin verb *terrere* meaning to frighten. While terrorism is an action, it is historically a political strategy used by both right and left wing political parties, nationalist groups, religious groups, revolutionaries and governments.

I am absolutely certain that the British loyalists and troops residing in America would have accused the American revolutionaries of committing acts of terror. The results of the acts of terror and revolutionary battles resulted in negotiations, peace, compacts, treaties, trade agreements and partnerships. Make no mistake, I am not comparing ISIS with revolutionaries fighting for independence and democracy — they want neither. The acts of terror they commit are not a strategy of negotiation and compromise but rather a strategy that spreads fear, intimidation, confusion, abandonment and capitulation.

Unlike those revolutionaries in a country who have been disempowered, disenfranchised and abused by their own government, ISIS does not have a negotiable end other than genocide and sectarian cleansing that allows them the power of religious, economic, political and social structure over all of Islam. The leaders of ISIS have not been elected but rather self-appointed. Their financial resources are gained by theft and conscription, and their abuse of human rights is legendary. What then are the rest of the world's options?

The first step is to understand the historical context of the condition we find ourselves in. A lesson we will learn repeatedly if we do not learn from it as we move to the future. All of the modern civilized world, as well as developing and emerging countries, have a common vested interest in reducing terror and corrupt human rights abuses by extremist groups that seek to subjugate others. ISIS's success to date is precisely due to the lack of a cohesive global strategy to eliminate its opportunities to exist in any scalable form. How can this be done?

Leaders of countries must recognize that the Syrian refugee problem is destabilizing a major portion of the globe, and that destabilization is disruptive as well as, potentially, structurally destructive to some fragile economies. Simultaneously, these leaders must know as well as voice the knowledge that this refugee problem is not the fault of the refugees, but rather by a pitiful United Nations response to genocide and sectarian cleansing. Unfortunately, we have experienced the same in Serbia, Bosnia, North Africa and too many other countries to mention.

If there were safe zones for Syrians to gather, they wouldn't need to seek shelter outside of their country. If Assad knew that he could not play one country against the other, but was indeed uniformly and unequivocally boxed in by all, the real negotiation to heal Syria could begin.

While we know that 90 % of all Muslims are Sunni we also know that only

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a small portion of Sunni support the effort to eliminate Shi’a. Efforts must be made to support non-extremist voices in their criticism and opposition to ISIS. They must know they have the support of the rest of the world, and that they are not less safe for doing so.

We must give those who live in fear and intimidation of ISIS an alternative that is attractive enough that they will turn away from the extremists who torture and terrorize. When people live in hopelessness, despair and hunger and when they have no alternative for a better tomorrow, terrorists have fertile ground. It is human nature to want the best for their offspring not the worst. This is true in every corner of the world. If the United Nation member countries wanted to end the despotic reach of ISIS, it could do so rapidly by putting aside ridiculous petty differences and focusing on providing actionable hope for those in ISIS’s grasp. Currently, ISIS enjoys the awareness that they fight the weak and unarmed who are desperately poor and without hope. What would occur if collectively the United Nations put a unified effort on the ground and in the air that included the many, not just a few, member nations that truly signaled simply “no more” to ISIS, and in doing so created safe zones that could be reconstructed where economies could return, schools could be built and hope restored out of the desperation that currently exists.

Simultaneously, technology and intelligence sharing must grow to levels not imagined before. More and better must be the benchmark. Terror exists when terrorists have opportunity. The balance between information collection in free and democratic societies must always be in the conversation, yet those who lost their lives or loved ones in Paris or on the Russian airliner or in 9/11 or Kenya or too many other places to name would have wanted more, not less, information for authorities to combat terrorists planning attacks.

We have all heard the phrase “doing the same thing over and over and expecting different results is the definition of insanity.” The consequences of combining benign neglect and ineffective solutions are great, both in human and economic cost. Throughout our history, and in too many instances where as a globe we have remained silent in the face of despotic extremists, it has never worked out. The solution can’t be viewed through a left or right, east or west, democratic, socialist, communist, Islamic, Jewish or Christian lens. The results of doing nothing will impact all of the above.

For those readers who might be thinking this has been a little preachy, I apologize and suggest you might have caught me on a bad day. When you have as much gray hair and laps around the sun as I have sometimes you lose your tolerance for stupidity in global affairs. It just might have been one of those days. ☑

Focus For Impact

As you already know, each year we survey our entire team as part of our strategic planning process. The objective is to get everyone's thoughts on the future of our company and identify ways to improve. The first question we ask them is "As a Greenleaf Trust employee, what are you most pleased with?" And each year, the three most common words used in their answers are "clients", "culture", and "team." A more thorough review of their answers reveals that they value collaborating with their teammates on meaningful work that benefits our clients in a unique work environment. This is good. So, the next question we ask them is how do we make sure you can continue to do this? Their answer is typical of someone who enjoys being a part of a high performance culture. They want to be held accountable for achieving goals that are important to them.

In 2012, members of our Client Centric Teams (CCT) started the "Focus For Impact" quarterly goal platform as a way for them to ensure that they would be successful in making an impact each quarter in areas where they identify a need. They developed the platform to focus their efforts on five key areas: client care, collaboration, continuous improvement, personal development, and purposeful growth. Important components of the platform are as follows:

1. Each teammate gets to choose their own goals with the input of their leader at quarterly coaching sessions, so we know that the goals will be personally meaningful/important (much more so than something leaders merely dictate to them).
2. When teammates write down their goals, they become real, psychological commitments as it is human nature to avoid saying one thing and doing another (cognitive dissonance).
3. Since the goals are aligned with principal accountabilities and tied to their compensation, when leaders follow-up each quarter in coaching sessions, the organization emphasizes the importance of each person's opinions (goal setting) and contribution (impactful outcomes).

Successful goal setting also involves the ability to measure outcomes, which is done during each person's quarterly coaching session with their leader. And, over the course of a year the outcomes are definitely measurable. Considering five goals per CCT member (40) each quarter, the collective benefit of their success is 800 impactful outcomes achieved on purpose each year!

I am extremely proud of our team and what they have been able to accomplish. The Focus For Impact program embodies our culture, engages our team, and benefits our clients. Equally important is that this type of formal plan and process involving accountability enhances repeatability of success and keeps clients, culture, and team top of mind for everyone. ☑



*Michael F. Odar, CFA
President*

"... each year we survey our entire team... to get everyone's thoughts on the future of our company and identify ways to improve."



Thomas I. Meyers, Esq., CTFP
Vice President
Trust Relationship Officer

“It was once thought that, in the absence of a request for information, the trustee ordinarily had no duty to provide information, except as part of an accounting.”

The Trustee’s Duty to Inform and Report to Beneficiaries

The duty to keep the beneficiaries of a trust informed can be traced back to an 1818 decision of the English Court of Chancery. This duty of notification was adopted by leading treatises, both English and American, and continues as the duty to inform in the major treatises we use today.

The trustee is under a duty to trust beneficiaries to give them complete and accurate information as to the nature and amount of the trust property, and to permit them to inspect the subject matter of the trust and the accounts and other documents relating to the trust.

It was once thought that, in the absence of a request for information, the trustee ordinarily had no duty to provide information, except as part of an accounting. It is now quite clear, however, that the trustee has a standing duty to keep the beneficiaries reasonably informed about the administration of the trust – the trustee has a duty to provide the beneficiaries with such information as is reasonably necessary to protect their interests.

When the trust is in favor of successive beneficiaries, both the beneficiaries who are currently entitled to receive income and/or principal *as well as beneficiaries who have a future interest* are entitled to this information, whether the interest is vested or contingent – all beneficiaries are entitled to such information as is reasonably necessary to enable them to enforce their rights or to obtain relief for a breach of trust. Because only the beneficiaries have the right and power to enforce the trust and to require the trustee to carry out the trust for the sole benefit of the beneficiaries, the trustee’s denial of the beneficiaries’ right to information consists of a breach of trust.

Litigation against trustees is increasing, making it important that trustees identify and manage all aspects of their fiduciary risk – including risk that either arises directly or is affected by the trustee’s disclosure obligations.

Michigan’s law governing the trustee’s duty to inform and report to beneficiaries, adopted from the Uniform Trust Code, can be found in MCL 700.7814, which provides, in part:

Section 7814:

- 1) A trustee shall keep the qualified trust beneficiaries reasonably informed about the administration of the trust and of the material facts necessary for them to protect their interests. Unless unreasonable under the circumstances, a trustee shall promptly respond to a trust beneficiary’s request for information related to the administration of the trust.
- 2) A trustee shall, upon the reasonable request of a trust beneficiary, promptly furnish to the trust beneficiary a copy of the terms of the trust that describe or affect the trust beneficiary’s interest and relevant

information about the trust property.

- 3) A trustee shall send to the distributees or permissible distributees of trust income or principal, and to other qualified or nonqualified trust beneficiaries who request it, at least annually and at the termination of the trust, a report of the trust property, liabilities, receipts, and disbursements, including the source and amount of the trustee's compensation, a listing of the trust property and, if feasible, their respective market values.

MCL 700.7814(5) provides that a trust beneficiary may waive the right to a trustee's report or other information otherwise required to be furnished under this section. A trust beneficiary, with respect to future reports and other information, may also withdraw a waiver previously given.

MCL 700.7103 defines "qualified beneficiary" as follows:

Section 7103(g):

"Qualified trust beneficiary" means a trust beneficiary to whom one or more of the following apply on the date the trust beneficiary's qualification is determined:

- i) The trust beneficiary is a distributee or permissible distributee of trust income or principal.
- ii) The trust beneficiary would be a distributee or permissible distributee of trust income or principal if the interests of the distributees under the trust described in subparagraph (i) terminated on that date without causing the trust to terminate.
- iii) The trust beneficiary would be a distributee or permissible distributee of trust income or principal if the trust terminated on that date.

It is important to note that Michigan law does not give the settlor of a trust the power to direct the non-disclosure of a trust to a qualified beneficiary. Hence, Michigan does not tolerate "silent trusts." And while Michigan law sets forth default rules, some of which a trust document can override, MCL 700.7105 states that some provisions in the Michigan Trust Code cannot be superseded by the trust document. Specifically, MCL 700.7105(2)(i) provides that:

"the duty...to provide beneficiaries with the terms of the trust and information about the trust's property, and to notify qualified trust beneficiaries of an irrevocable trust of the existence of the trust and the identity of the trustee" cannot be overridden by a trust document.

In conclusion, Michigan law has strict and clear requirements that mandate trustees to inform and report to *all* qualified beneficiaries of a trust, both current beneficiaries and future beneficiaries. 

"... Michigan law has strict and clear requirements that mandate trustees to inform and report to *all* qualified beneficiaries of a trust..."



Michelle M. Gray
Participant Services Coordinator

“...retirement savers almost never see a long-term improvement in their financial situation by choosing to take a loan [from their 401(k)].”

Why You Might Want To Reconsider That 401(k) Loan

For many 401(k) participants, taking a loan from their 401(k) plan might sound like a good idea. After all, the interest rates are typically lower than a traditional personal loan, they pay themselves back principal and interest and, assuming they remain employed with the participating employer throughout the term of their loan and satisfy the loan terms, there are no early withdrawal fees or taxes owed. Although it might sound like a good idea, retirement savers almost never see a long-term improvement in their financial situation by choosing to take a loan.

Of the approximately 87% of plans that offer loans, it's estimated that between 10-17% of 401(k) participants choose to take a loan from their plan. The younger generation, or those farther away from retirement, tends to be more loan-happy than their older counterparts. For example, 17% of Millennials (those born between the early 1980s and the early 2000s) have taken a loan from their employer-sponsored retirement plan while only 13% of the Generation Xers (those born between the early 1960s and the early 1980s) and only 10% of the Baby Boomers (those born between the years 1946 and 1964) have taken a loan from their employer-sponsored retirement plan.

Part of what makes taking loans harmful for the long-term is that those who take one loan are likely to take at least one more in the future. While 50% of 401(k) borrowers take just one loan, the other 50% borrow multiple times. In addition, research shows that when a plan sponsor permits multiple rather than only one loan, each individual loan tends to be smaller, but the probability of plan borrowing nearly doubles, and the aggregate amount borrowed rises by 16%. Researchers contend that this suggests employees perceive that easier loan access is actually an encouragement to borrow.

It's also been found that borrowers tend to save less on average over time after their first loan. For example, 25% of borrowers reduced their savings rate within five years of taking a loan, generating \$180 to \$690 less per month in anticipated annuitized retirement income. Even more troubling, 15% of those who take a loan go on to stop saving altogether within a fairly short period of time.

Given the above, how can plan administrators help their employees avoid falling prey to the pitfalls of borrowing money from their 401(k) plans? One way is to modify your plan design. Plans are not required to offer loans, so you

could eliminate the loan feature altogether. Or, if you choose to offer loans in your plan, allowing a participant only one loan at a time and/or incorporating a waiting period between loans can help discourage chronic borrowers from taking additional loans. You could also restrict loans to hardship reasons only, which means a participant could only take a loan

for designated hardship reasons and would be required to provide proof of their hardship prior to the loan being approved. Lastly, we encourage plan administrators to have participants to call the Greenleaf Trust participant call center to discuss the potential pitfalls of taking a loan with a call center representative. ☑

Developing Long-Term Return Expectations – What to do When You Don't Have Biff's Sports Almanac

In the 1989 film “Back to the Future Part II”, antagonist Biff Tannen takes a sports almanac in 2015 and travels back in time to 1955 where he gives the almanac to his younger self. Armed with this information, Biff becomes extremely wealthy by betting on sports in the ensuing years. At Greenleaf, we do not practice time travel, do not have any almanacs from the future, and regard ourselves as long-term investors rather than bettors. Though we do not know the future, we do our best to estimate what market returns will be over the coming years. In this article, I will discuss the importance of capital market assumptions and describe at a high level how we go about the process of forming our estimates. In a future article, we will dig deeper into our capital market assumptions and how they are reflected in our portfolios.

Return expectations are important for a couple of reasons. First, they help our Wealth Management Advisors determine what asset allocation is appropriate for our clients to meet their financial goals. Second, they help us determine our mix of investments for a given level of risk. For example, if expected returns from international equities are much higher than those of US equities, we may establish an overweight position in international equities while reducing our position in US equities.

When developing expected returns we utilize a combination of theory,



*Daniel C. Haines, CFA
Fixed Income Analyst*

“Though we do not know the future, we do our best to estimate what market returns will be over the coming years.”

history and current market conditions. For both US equities and US bonds, we will look at the historical returns, drivers, and take a quick peek into the future at expected future returns.

Equities

Since 1926, US large cap equities have returned around 10% annually (6.9% above inflation). The drivers for equity returns include the dividend yield, the change in valuation and earnings growth. During this period, dividends contributed 3.9% per year, valuation change contributed 0.8% per year and earnings growth contributed 5.1% per year (2.1% above inflation).

Source	Annual Return Contribution (1926-2014)
Dividend Yield	3.9%
Change in P/E	0.8%
Earnings Growth	5.1%
Total Nominal Return	10.0%
Inflation	2.9%
Total Real Return	6.9%

Note: Returns are geometric averages; sources: Robert Shiller, Ibbotson Associates

	January 1926	October 2015	Average
Dividend Yield	4.8%	2.05%	3.85%
P/E (TTM)	10.1	21.8	16.8

“Since 1926, US large cap equities have returned around 10% annually (6.9% above inflation).”

Examining each driver, we see the following:

- Dividend yields are lower than they have been over this period and thus our expected returns from this driver are lower.
- Valuation multiples have expanded and are now at the higher end of their historical range. Many expect these valuations to contract and it is thus possible that they will detract from returns going forward, as opposed to being a positive contributor to returns as they have in the past.
- Earnings growth depends on revenue growth, changes in margins and changes in share count. For the purposes of this article, we will assume that real earnings growth will be similar to historical levels.

Based on low dividend yields, high valuations and average earnings growth, we expect that US large cap equity returns will be lower than they’ve been historically.

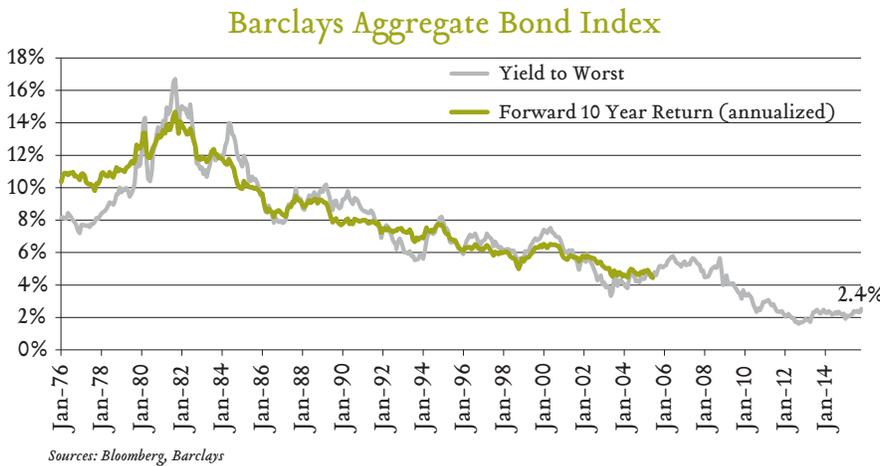
Bonds

Since 1926, long-term government bonds have returned 5.67% (2.7% above inflation). Treasury bond returns depend on interest income and changes in price due to changes in interest rates. Over the long-term, the majority of their return has been generated by interest income.

Source	Annual Return Contribution (1926-2014)
Interest Income	5.2%
Capital Appreciation	0.4%
Total Nominal Return	5.7%
Inflation	2.9%
Total Real Return	2.7%

Note: Returns are geometric averages; sources: Robert Shiller, Ibbotson Associates

However, we invest in more than just US government debt at Greenleaf Trust, and a more appropriate index to examine is the Barclays Aggregate Bond Index. This index includes bonds with credit risk that have yields above Treasury yields. When doing an in-depth forecast we consider our expectations for interest rates including the level and shape of the yield curve, credit spreads and the likelihood of default. However, when building return expectations for bonds, the starting yield is a very useful measure. The chart below shows the yield on the Barclays Aggregate Bond Index and the subsequent return for the next 10 years. As you can see below, the starting yield level of the index has shown a high correlation to forward 10 year returns. Currently, the yield on the index is 2.4%, which suggests that returns over the next decade are expected to be lower than they have been historically.



“Without the ability to travel back to the future, it is impossible to say exactly how markets will perform. However, the indicators mentioned in this article give us a better idea.”

Summary

After decades of strong returns it is worth stepping back to consider what we should expect markets to return over the coming 10–20 years. Without the ability to travel back to the future, it is impossible to say exactly how markets will perform. However, the indicators mentioned in this article give us a better idea. Based on the observations above, we expect US equity and fixed income returns will be lower than they have been historically both on a nominal and real basis. In a future article we will give a more in-depth explanation of our capital market assumptions and how they impact our portfolios. ☑

Stock Market Pulse

Index	Total Return Since		P/E Multiples	11/30/2015
	11/30/2015	12/31/2014		
S&P 1500	480.78	2.95%	S&P 1500	18.0x
DJIA	17,719.92	0.06%	DJIA	15.3x
NASDAQ.....	5,108.66	9.05%	NASDAQ.....	21.2x
S&P 500.....	2,080.41	3.01%	S&P 500.....	17.8x
S&P 400	1,461.81	2.08%	S&P 400	19.5x
S&P 600	706.75	2.95%	S&P 600	20.2x
NYSE Composite	10,409.58	-3.96%		
Dow Jones Utilities.....	563.13	-5.70%		
Barclays Aggregate Bond.....	108.81	0.68%		

Key Rates

Fed Funds Rate	0% to 0.25%
Tbill 90 Days.....	0.18%
T Bond 30 Yr.....	2.99%
Prime Rate	3.25%

Current Valuations

Index	Aggregate	P/E	Div. Yield
S&P 1500	480.78	18.0x	2.06%
S&P 500.....	2,080.41	17.8x	2.12%
DJIA	17,719.92	15.3x	2.42%
Dow Jones Utilities.....	563.13	NA	3.66%

Spread Between 30 Year Government Yields and Market Dividend Yields: 0.93%

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