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USI CONSULTING GROUP

Market & Legal Update

JUNE 2022 REVIEW

Stay on top of the latest market developments and legal and regulatory updates that may affect your business.

MARKET UPDATE

Markets Post Worst First Half of the Year Since 1970

U.S. equities finished June with steep losses and posted the worst first half year performance since 1970. Even though stocks gained some ground during the final week of the month, they struggled to maintain the positive momentum from bouncing off bear market lows. Persistent inflationary pressures, which have worsened following Russia's invasion of Ukraine and China's zero COVID tolerance lockdowns, have pushed the Federal Reserve further into an aggressive stance as it steps up the pace of interest rate hikes to fight the price pressure. High inflation not experienced since the early 1980s, combined with a more hawkish Fed to contain inflation, could exert downward pressure on economic growth with the probability of a recession increasing according to both economic forecasts and the Federal Reserve Charmain Powell. Accordingly, this uncertainty rattled stock markets in June, pushing the S&P 500 Index into bear market territory with a 20% year to date loss. The Dow Jones Industrial Average was down 6.6% in June and 14.4% during the first 6 months of the year. The tech-heavy Nasdaq Composite posted the largest loss at 29%, as growth stocks have been the worst performers this year. International markets also lost ground, as the MSCI EAFE posted a 19% loss for the first half of the year. In the bond market, the yield on the 10-year Treasury yield moved higher to 3.02% from 2.85% last month.

Market Return Indexes	June 2022	YTD 2022
Dow Jones Industrial Average	-6.6%	-14.4%
S&P 500	-8.3%	-20.0%
NASDAQ (price change)	-8.7%	-29.5%
MSCI Eur. Australasia Far East(EAFE)	-9.3%	-19.6%
MSCI Emerging Markets	-6.6%	-17.6%
Bloomberg High Yield	-6.7%	-14.2%
Bloomberg U.S. Aggregate Bond	-1.6%	-10.4%
Yield Data	**June 2022**	**May 2022**
U.S. 10-Year Treasury Yield	3.02%	2.85%

On June 15th, the Federal Reserve raised rates by 0.75%, marking the largest rate hike in 28 years and following two back-to-back increases in March and May. Investors were expecting a half point hike, but market sentiment changed once the headline consumer price index (CPI) for the month of May was released just days prior to the FOMC meeting. CPI indicated an 8.6% increase in consumer prices from a year ago, which was higher than expected and the highest reading since 1980. The CPI basket is typically broken down into "goods" or transitory inflation and "services" or sticky inflation. The first component, "goods", has been impacted by global supply chain issues while the second, "services", has been pressured by domestic factors, such as wage growth. Services, which includes items like rent, transportation, entertainment, and hospitality, rose 6% in May from a year ago on the heels of higher wages. In terms of employment, The Fed's other mandate, there are almost twice as many job openings as there are unemployed workers, an imbalance that has pushed wages higher and led to stickier overall inflation. This imbalance could potentially peak as Covid fears continue to subside, savings are exhausted, and consumers continue to lose purchasing power due to higher inflation. The Fed is navigating a delicate balancing act, hiking interest rates enough to slow down demand and combat persistently high inflation, but not tightening so much as to send the economy into a recession.

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While policy tightening tends to have a lagged impact on the economy, certain interest rate sensitive sectors are already showing signs of slowing, such as the housing market. Home prices, which have been climbing over the last year, increased at a slightly slower pace of 20.4% in April from 20.6% the previous month, according to the S&P Case-Shiller data. Also, the National Association of Realtors reported that existing home sales fell 3.4% in May representing the lowest level since June of 2020 and the fourth consecutive monthly decline. In addition, mortgage applications are down due to higher rates with the 30-year fixed rate crossing 6% in June. So, although demand continues to outpace supply with limited inventory, higher mortgage rates make housing less affordable. Lastly, another important indicator, the Purchasing Managers' Indices (PMIs), indicated a sharp deceleration in the global economy in June.

As we head into the second half of the year, it is likely that the economy will slow in response to the Fed's objective to curb inflation, which could lower demand as consumers and businesses respond to higher borrowing costs. A significant slowdown could tip the economy into a recession and generate further volatility. Economists that were surveyed by the Wall Street Journal in June indicated a 44% probability of a recession over the next year, up from 18% in January. Historically, the Federal Reserve has had a mixed record of being able to accomplish a "soft landing", a scenario where the Fed raises rates sufficient to curb inflation, yet not to the point of causing a recession. The U.S. has gone into a recession four out of the last six times the Fed has raised interest rates since the 1980s. Indeed, certain sectors of the economy are already showing signs of slowdown and the uncertainty around future economic developments will continue to weigh on the markets.

Questions

If you have any questions regarding the latest market developments, please contact your **USI Consulting Group representative**.

LEGAL UPDATE

IRS Introduces New Pre-Audit Compliance Pilot Program

In June, 2022 the Internal Revenue Service ("IRS") began implementing a new **Pilot Program** that will give retirement plan sponsors, immediately prior to the commencement of a qualified plan audit, a 90-day period to review their retirement plan documents and plan operations and correct certain compliance failures in accordance with the IRS's Employee Plans Compliance Resolution System ("EPCRS") procedures. The intent of the Pilot Program is to allow the plan sponsor the opportunity to identify issues and correct them at a substantially lower cost than if such issues are identified and corrected during the plan audit. At the conclusion of the Pilot Program, the IRS will assess the program's success and determine whether the program should be continued.

Details of the Pilot Program

Under the Pilot Program, the IRS will inform a plan sponsor by letter that their plan has been selected for examination and specify the 90-day period for permissible pre-audit correction. If the plan sponsor does not respond within the 90-day period, the IRS will contact the plan sponsor to schedule the audit.

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During the 90-day review period, plan sponsors will have the opportunity to correct most documentary or operational errors under EPCRS procedures, which were most recently set forth in **Revenue Procedure 2021-30**. Compliance issues that qualify for correction under the EPCRS Self-Correction Program ("SCP") can be corrected without the payment of any IRS sanction, while compliance issues that do not qualify for self-correction can generally be corrected for a nominal IRS fee using the EPCRS Voluntary Correction Program ("VCP") fee schedule, rather than the much more expensive EPCRS Closing Agreement Program ("CAP"). The IRS will require that the plan sponsor (1) correct any errors in accordance with relevant EPCRS correction principles, (2) pay the VCP sanction (if applicable), and (3) update plan procedures to avoid such failures in the future.

At the conclusion of the 90-day period, the IRS will review the plan sponsor's documentation, including any corrections undertaken during the 90-day period, and inform the plan sponsor whether they agree with the plan sponsor's conclusions and proposed corrective actions. The IRS will then either issue a closing letter or perform a limited or full scope audit of the plan, based on the relevant circumstances.

How USICG Can Assist

Plan sponsors who receive a pre-audit letter from the IRS under the Pilot Program should immediately review their plans to identify any documentary or operational compliance issues that could be corrected under the program. USICG and its staff of experienced compliance professionals can assist plan sponsors in the following ways:

- Assist the plan sponsor in compiling the necessary census information and relevant plan related documentation that the IRS will likely request from the plan sponsor in connection with the audit.
- Review such information and documentation (as well as the plan's prior operations) to identify potential plan compliance issues that could be corrected under the IRS Pilot Program prior to the end of the 90-day period, in coordination with the plan sponsor's staff and (other) retirement plan service providers.
- If a documentary or operational compliance issue is identified during a pre-audit review, assist the plan sponsor in determining the optimal (SCP or VCP) correction methodology that can be used to address such issue and documenting such correction for the IRS after implementation.
- Calculate any required corrective contributions and determine any other remedial actions that must be taken in connection with addressing such compliance issues and avoiding such failures in the future.
- If necessary, negotiate with the IRS prior to or during the audit concerning corrective actions, additional required plan contributions, prospective plan design changes, and IRS penalties.

Whether a plan sponsor has been informed of a pending IRS or other governmental audit or not, USICG is always available to help plan sponsors with all retirement plan related compliance matters. Please contact your USICG representative for further information.

Questions

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How USI Consulting Group Can Help

The USI Consulting Group (USICG) team is happy to assist plan sponsors with all retirement plan compliance matters and changes in the market, including those discussed here, to help you mitigate risk and financial impact to your organization.

QUESTIONS?

Contact your USICG representative, visit our **Contact Us** page or reach out to us directly at **information@usicg.com.**

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An index is a measure of value changes in a representative grouping of stocks, bonds, or other securities. Indexes are used primarily for comparative performance measurement and as a gauge of movements in financial markets. You can not invest directly in an index and, for comparative purposes; they do not reflect the effect of the various fees inherent in actual investment vehicles.

The S&P 500 Index is a market value weighted index showing the change in the aggregate market value of 500 U.S. stocks. It is a commonly used measure of stock market total return performance.

The Dow Jones Industrial Average is a price weighted index comprised of 30 actively traded blue chip stocks; primarily industrial companies, but including some service oriented firms.

The NASDAQ Composite Index is a market-value weighted index that measures all domestic and non-U.S. based securities listed on the NASDAQ Stock Market.

Gross Domestic Product (GDP) is the market value of the goods and services produced by labor and property in the U.S. It is comprised of consumer and government purchases, net exports of goods and services, and private domestic investments. The Commerce Department releases figures for GDP on a quarterly basis. Inflation adjusted GDP (or real GDP) is used to measure growth of the U.S. economy.

The MSCI Europe and Australasia, Far East Equity Index (EAFE) is a market capitalization weighted unmanaged index developed by Morgan Stanley Capital International to measure approximately 1,100 securities in 21 major overseas stock markets. It is a commonly used measure for foreign stock market performance.

The Barclays Capital U.S. Aggregate Index covers the U.S. Dollar denominated investment grade, fixed-rate, taxable bond market of SEC-registered securities.

The Barclays Capital U.S. Corporate High Yield Index covers the U.S. Dollar denominated, non-investment grade, fixed income, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's Fitch, and S&P is Ba1/BB+/BB+ or below.

The MSCI Emerging Markets Index (EM) is a free-float-adjusted market-capitalization index developed by Morgan Stanley Capital International. It is designed to measure the equity market performance of 26 emerging market countries.

The 10 Year Treasury Yield is the interest rate the U.S. government pays to borrow money for a 10-year period. In addition to influencing how much the government pays to borrow over this time-frame, the 10-year Treasury Yields also determines how much investors earn by investing in this debt and it is a good indicator of investor sentiment

The higher the yield, the better the economic outlook.

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