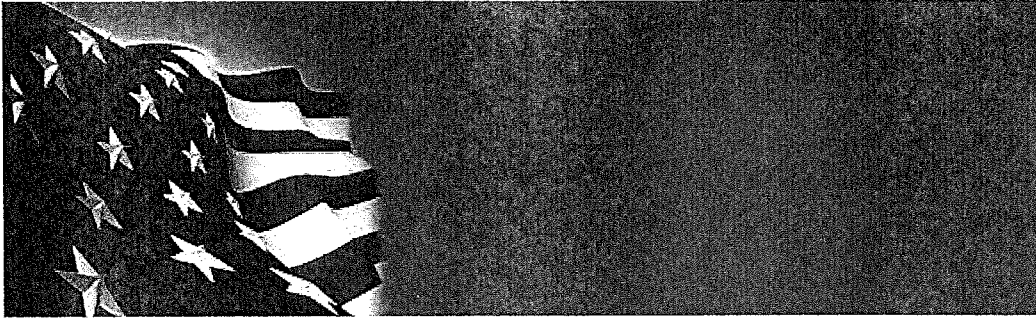


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CYPEN & CYPEN NEWSLETTER

for

JUNE 5, 2014

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Stephen H. Cypen, Esq., Editor

Never Forget September 11, 2001

and

Always Remember May 2, 2011

1. QUANTITATIVE MEASURES FOR EVALUATING SOCIAL SECURITY REFORM PROPOSALS: A new issue brief from the American Academy of Actuaries addresses recent reports of the Social Security Board of Trustees' estimate that the program's trust funds will be exhausted in approximately 25 years unless changes are made to the program. Various reforms have been proposed, including combinations that increase payroll taxes, raise retirement age, lower benefits or allocate payroll taxes to individually owned accounts. Advocates of various reforms all claim that their proposals would solve Social Security's financial problems, while continuing to meet participants' financial needs in retirement. In face of these competing claims, a set of guidelines of quantitative measures is needed for evaluating Social Security reform proposals. The issue brief describes a number of measures that can provide useful quantitative analysis of reform proposals. The issue brief explains how these measures can be used together to obtain a clearer picture of the relative advantages and disadvantages of proposals for bringing long-term financial soundness to Social Security. Because Social Security is such a large system, changes in the program are likely to have macroeconomic effects, causing considerable debate among diverse stakeholders. The goal of establishing a quantitative framework is to promote consistent analysis of such proposals and to ensure proper comparability of proposals over the broad timeframes and range of provisions covered. Based on the analyses done for past Social Security legislative proposals, the issue brief recommends the use of a standard set of measurement tools that would clearly and objectively present financial effects of Social Security reform proposals. While some of

these measurement tools may not be appropriate for every reform alternative and may need to be adapted to a specific proposal, a balanced and clear analysis is important. In general, two types of measurement standards can be applied to Social Security reform proposals. Measures of actuarial viability show whether income to the Social Security system would be sufficient to support payment of projected benefits and other expenses. Measures of distributional impact show how well the system would meet the financial needs and expectations of participants. An example of the quantitative measurements considered and potential format for comparing potential proposals is included at the end of the brief. The following are some key points:

- Many have offered Social Security reform proposals to keep the program financially sound before its trust fund becomes exhausted in approximately 25 years.
- Consistent quantitative measures allow for a better comparison of Social Security reform proposals. These measures fall in two broad categories: actuarial viability and distributional impact.
- Actuarial viability measures show whether a proposal could provide sufficient income to the Social Security system to support projected benefits and expenses. These measures include Social Security's Long-Term Adequacy, Long-Term Solvency, Sustainable Solvency, and Need for Large Scale General Revenue Participation.
- Distributional impact measures show well how a proposal could meet the financial needs and expectations of participants; these measures include Replacement Ratios, Purchasing Power at Older Ages, and Money's Worth Comparisons.
- Quantitative measures do not "favor" one proposal over another; rather, these measures provide an objective platform for assessing Social Security reform proposals.

2. FREEZING DEFINED BENEFIT PLANS: Groom Law Group has authored a *Practical Law Practice Note* that provides a basic overview of implications of freezing a defined benefit plan under the Employee Retirement Income Security Act of 1974 and Internal Revenue Code, and explains some of the issues that can arise after the plan is frozen. In the current economic climate more companies are freezing their defined benefit plans. Such a step used to be a rare event that usually involved only financially-strapped companies. However, even profitable companies have joined the chorus of those announcing freezes. The general cause seems to be that U.S. companies are reacting to stiff competition overseas and at home from companies that do not sponsor defined benefit plans. Many pension plan freezes are also in response to companies' growing concern that defined benefit plans have become more costly. Freezing a defined benefit plan may help to reduce a plan sponsor's long-term cost and volatility of its financial obligations. However, once a pension plan is frozen, the plan sponsor and the frozen pension plan's fiduciaries retain important ongoing obligations and duties under both ERISA and the Internal Revenue Code. Failure to comply with these obligations and duties could have significant adverse consequences on the plan sponsor, plan fiduciaries, plan participants and their beneficiaries. Therefore, when considering a plan freeze, a plan sponsor should carefully analyze its long-term strategies for management and disposition of the frozen plan to avoid significant liability exposure in the future. The note explains six categories:

- Some common reasons for choosing to freeze a defined benefit plan;
- The difference between freezing and terminating a defined benefit plan;
- Types of plan freezes;
- The various implications of a plan freeze;
- The process of freezing a defined benefit plan; and
- Long-term strategies for frozen defined benefit plans.

Because of space limitations, we will deal with only one of the listed subjects – types of plan freezes:

- A plan can be closed to new entrants while those participants already in the plan continue to accrue benefits (commonly called a “soft freeze”).
- A plan can stop benefit accruals for all participants, but allow benefits to increase with growth in participants' wages (also sometimes called a “soft freeze”).
- A plan can stop benefit accruals for some, but not all, participants based on age, tenure or job classification (commonly called a “partial freeze”).
- A plan can stop service accruals for all participants and all participants stop earning benefits. Assets remain in the plan and are paid out when participants retire or leave, but participants' benefits do not grow with additional years of service (commonly called a “hard freeze”).
- A plan can also be frozen using a combination of the foregoing methods.

Certain restrictions apply when an employer freezes its defined benefit plan including anti-cutback rules in prohibition against certain retroactive changes. Read the entire excellent piece at http://www.groom.com/media/publication/733_Freezing_Defined_Benefit_Plans_2014.pdf.

3. TENNESSEE LAW WILL REQUIRE FULL PENSION CONTRIBUTIONS BY LOCAL GOVERNMENTS: The Governor of Tennessee has signed legislation that will require some local governments in the state to increase contributions to their pension funds. Effective immediately for contributions beginning after July 1, 2014, the Public Employee Defined Benefit Financial Security Act of 2014 requires local governments to contribute 100% of the actuarially determined annual required contribution that incorporates both the normal cost of benefits and the amortization of the pension plan's unfunded accrued liability. The act affects local government pension funds that do not participate in the \$40 billion Tennessee Consolidated Retirement System, which already requires such funding. Local governments can work toward the 100% contribution requirement over six years, but local governments that would experience financial hardship can work with the State Treasury Department if they cannot reach 100% in that time frame. Among local government pension funds that do not belong to TCRS is the \$1.9 billion Memphis City Retirement System. The new law is cited as a primary reason for the Memphis mayor's recommendation to close the defined benefit plan, which last contributed just 20.4% of the annual required contribution. With over \$2.5 billion in liabilities, the fund has a 72.6% funding ratio. This story appeared in *Pensions & Investments*.

4. MARDEN REFOCUSSES THE LENS: Susan Marden, Florida Public Pension Trustees

Association Public Relations Consultant, writes there is something inherently ugly about claims by private sector workers that government employees should not “get more” than they, themselves, receive in retirement benefits. At the core of the matter, taxpayers seem to have been led to feel especially resentful of the lifetime guarantee that public employees receive. They have been encouraged to feel angry their hard earned dollars might finance a more secure retirement for public employees who work for them. But is there not something fundamentally wrong with that attitude? Such a view presumes that public workers should be somehow less valued and at the same time more grateful for their compensation. It presumes their salaries, benefits, their very jobs are a gift given at the beneficence of public whim, and which can be taken away as easily as bestowed. In reality, public workers are a highly skilled, highly educated workforce, saddled with the prodigious responsibilities of maintaining and operating our civic functions and government services -- from public schools, to judicial courts, from maintaining roads and infrastructure, to public safety. They are no more or less worthy of their paycheck or their benefits than those in the private sector. In fact, there are some very practical reasons why private sector workers have been losing their (guaranteed) defined benefit pensions over the past 40 years, and those reasons have nothing whatsoever to do with comparisons between public and private sector workers, their skill set, what services they perform, or what they are compensated. It is not about the value of the workers, it is about the viability of pension plans as they now are governed. Beginning with passage of Employee Retirement Income Security Act of 1974, and through the Pension Protection Act of 2006, Congress passed a series of laws intended to be consumer protections, but which had the unintended consequence of making pension funding very unattractive to private sector employers. The reason for this series of laws and regulations is that too many corporations had been failing adequately to fund their pension plans, were using the funds for other expenses and were lacking in transparency about where the funds were invested. (It was not all that long ago that General Motors was being basically kept afloat by the over funding of its pension plans. Some may remember the-then chairman’s famous quote that “GM is a pension plan running an automobile company.”) But the laws intended to protect these workers were enacted through complex regulations that are difficult to adhere to (not to mention expensive). American businesses have been pulling back from the old school pension system ever since. Pension plan coverage among all private industry workers was down to 35% in the early 1990s; by 2011, that coverage stood at only 18%. But the new rules were at very least a challenge, especially to small businesses with limited financial resources. Today, private sector pension plans are required to be 100% funded, funding shortfalls must be amortized over just 7 years (down from 30), and employers must average over just 2 years the interest rates used to calculate assets and liabilities (down from 4-5 years). The public sector has had unparalleled stability in terms of staffing, projected costs, contributions. Its larger and more diverse labor force enables public systems to better pool risk and average returns over a very long investment horizon. Recent statistics showed among **private sector** establishments with fewer than 50 workers, just 8% offered a defined benefit pension plan. In contrast, among establishments with 500 or more workers, 48% offered such a plan. This statistic reinforces the notion that a large and diverse labor pool makes financing a DB plan vastly more supportable. Cost efficiencies are significantly more achievable for larger businesses and especially for public sector systems.

5. SOCIAL SECURITY GOVERNMENT PENSION OFFSET: Social Security spousal benefits were established in the 1930s to help support wives who are financially dependent on their husbands. It has since become more common for both spouses in a couple to work, with the result that, in more cases, both members of a couple are entitled to Social Security or other government pensions based on their own work records. Social Security does not provide both a full retired worker and a full spousal benefit to the same individual. Two provisions are designed to reduce Social Security spousal benefits of individuals who are not financially dependent on their spouses because they receive benefits based on their own work records. These are

- the “dual entitlement” rule, which applies to spouses who qualify for both (a) Social Security spousal benefits based on their spouses’ work histories in Social Security-covered employment and (b) their own Social Security retired-or disabled-worker benefits, based on their own work histories in Social Security covered employment; and
- the Government Pension Offset, which applies to spouses who qualify for both (a) Social Security spousal benefits based on their spouses’ work histories in Social Security-covered employment and (b) their own government pensions, based on their own work in government employment that was not covered by Social Security.

The GPO reduces Social Security spousal or widow’s benefits by two-thirds of the pension from non-covered government employment. The GPO does not reduce the benefits of the spouse who was covered by Social Security. Opponents contend that the GPO is imprecise and can be unfair. Defenders argue it is the best method currently available for preserving the spousal benefit’s original intent of supporting financially dependent spouses and also for eliminating an unfair advantage for spouses working in non-Social Security-covered employment compared with spouses working in Social Security covered jobs (who are subject to the dual entitlement rule). (The GPO should not be confused with the Windfall Elimination Provision, which reduces Social Security benefits that a person receives as a worker if he also has a government pension based on work that was not covered by Social Security. (See C & C Newsletter for March 13, 2014, Item 2). Congressional Research Service 7-5700 RI32453 (April 23, 2014).

6. IMPROVING RETIREMENT READINESS FOR STATE AND LOCAL GOVERNMENT EMPLOYEES: The International Foundation for Retirement Education has prepared a white paper for The National Association of Government Defined Contribution Administrators. Here are a few of the many survey statistics that provide evidence that American workers are on the verge of a retirement crisis:

- 57% of workers report that the total value of their households’ savings and investments, excluding the value of their primary homes and any defined benefit plans, is less than \$25,000.
- Only 13% of workers indicate they are very confident they will have enough money to live comfortably in retirement.
- A typical working-age household has only \$3,000 in retirement account assets; a

typical near-retirement household has only \$12,000.

- Among elderly Social Security beneficiaries, 23% of married couples and about 46% of unmarried persons rely on Social Security for 90% or more of their income.
- More than three-quarters of plan sponsors agree the days of not working in retirement are gone for their participants, with 55% saying they are not confident their participants are saving enough.

Public sector employers have started to adjust their retirement plan benefits offerings, and shift more of the risk of saving and investing for retirement to their employees. The combination of changing benefits, retirees living longer and increases in medical expenses mean that public sector employers are facing a significant challenge to ensure employees recognize their new retirement readiness responsibilities. Lessons from the same shift within the private sector over the past several decades tell us that, without help, most public sector employees will not be able clearly to understand their new personal risks and make informed retirement planning decisions. Therefore, public sector employees retiring in the future will be in jeopardy of not having adequate resources, and many may ultimately become somewhat dependent on their former employers in the form of social assistance. While public sector employers need to continue to use benefit packages as a way to attract and retain skilled workers, they must also find a balance in their communications to inform employees that without personal savings or other income sources, these benefits will likely not be sufficient to meet all of their future retirement income needs. Public employers and retirement plan providers can help plan participants accept their new retirement planning risks and responsibilities by:

- Offering personal retirement assessment tools that measure retirement readiness on a holistic basis – meaning looking not only at an employee's wealth and financial needs component, but also the employees' health and happiness preparedness.
- Expanding education programs to address various retirement planning needs (not just investing decisions) related to public plan differences, gender, ethnicity and generation.
- Encouraging participation in voluntary savings plans by using best practices plan features that simplify decision making, reduce costs and offer outcome-based income projections.

Although there is not a one-size-fits all solution, a commitment to a retirement readiness evaluation program combined with ongoing education programs and enhanced savings plan design features will create a strong foundation for positively impacting needed changes in public sector plan participant behavior. Amen.

7. JUDGE AND PUBLIC DEFENDER REALLY DUKE IT OUT: Mynews13.com reports that chaos in a Brevard County courtroom, between a judge and a public defender, got so heated they came to blows. The public defender's office likens what happened to an episode of *Jerry Springer*. Tension was building in Judge John Murphy's courtroom between him and public defender Andrew Weinstock. After the judge challenged Weinstock to a fight, both men went into the hallway, where a ruckus could be heard. According to the lawyer, the judge grabbed him by the collar and began punching him in

his head. Apparently Weinstock never threw any punches of his own, and was just trying to defend himself. (Apparently, he also a private defender.) Seconds after the brouhaha was over, the courtroom crowd (naturally) broke into applause. The lawyer was not seriously hurt, does not want to pursue criminal charges and is currently taking a couple days off. However, he has been reassigned, and will not be in the same courtroom as Judge Murphy again. (How about the same ring?) The Florida Judicial Qualifications Commission, which oversees judges, will no doubt conduct a full investigation. Meanwhile, Judge Murphy will be taking a leave of absence, and will be undergoing anger management classes. (Grrrrr.)

8. FIVE WAYS PRIVATIZATION IS FLEECING AMERICAN TAXPAYERS: *Salon* says that government outsourcing goes horribly wrong more often than not. The following are a few representative horror stories. For decades, we have been subjected to constant propaganda that government is inefficient, bureaucratic and expensive. We are told that the answer is to privatize or outsource government functions to private businesses, and they will do things more efficiently, and everyone comes out ahead. As a result, we have experienced years of privatization of government functions. So, how has this wave of privatization worked out? Has privatization saved taxpayers money and improved services to citizens? The simple answer: of course not. If a company can make a profit doing something the government had been doing, it means that we are losing out one way or another. It is simple math. And the result of falling for the privatization scam is that taxpayers have been fleeced, services to citizens have been cut way back and communities have been made poorer. But the companies that convinced governments to hand over public functions have gotten rich off of the deal. Surprised? Consider the following:

- **Chicago Parking Meters.** The mother of all privatization horror stories concerns Chicago's parking meters. In 2008 the city financialized its parking meter revenue stream, leasing rights for 75 years to collect from parking meters to a consortium led by Morgan Stanley. Right away parking meter rates went up fourfold and meters stopped working. The city's residents were unhappy, but there was nothing they could do about it. Obviously, Morgan Stanley was more interested in making money than giving Chicago the best deal it could. An investigation showed that the city was shortchanged by at least \$974 million. Later, it turns out the consortium may realize a profit of almost \$10 billion, after paying Chicago only \$1.15 billion.
- **Toll Roads.** Some states are considering privatizing their roads with public-private partnerships. The deal is that private companies maintain the roads, and in exchange can charge a toll and make a profit. How is this one going? In 2006, Indiana privatized I-80 for \$3.8 billion, giving a 75-year lease. (Sideline: Goldman Sachs earned \$20 million just for brokering the deal.) Since then, tolls have doubled, and it is going to get worse. The leaseholders can raise the toll annually. Colorado's 99-year lease of its Northwest Highway has met a similar fate.
- **Prisons for Profit.** Imagine a system where someone makes a profit if more and more people are put in prison: a perverse incentive. What could be worse than getting a profit to get people put in jail? Since the private companies want profits, rehabilitation becomes a cost. Thus, companies push for government policies that

put more people into prison for more crimes and for longer sentences. But the worst part of prison privatization is companies saving on costs by cutting back on staff, food quality and everything else. Investigations in 21 states unveil a startling pattern of murder, riots and sexual assault at private prisons nationwide. Nine major riots have erupted since 2000. At least 25 inmates died amid claims of mistreatment, inadequate medical care or in riots. At Florida's state run prisons in the same 12-year period: no major damage or injuries from riots; no closures over squalor; and no Justice Department investigations over human rights.

- **Cost Overruns.** Cost overruns are a common scam when governments outsource to private companies. In 2008, New York City decided to save money by contracting out its payroll system. The original estimate to develop the system was \$68 million. Somehow, the cost ballooned to \$700 million, and the system still did not work! The "good news" -- the contractor has agreed to pay the city \$500 million under a deferred prosecution agreement to resolve claims that it conspired to defraud the city. Three company employees were sentenced to 20 years each for their roles in the theft and fraud. (Are they in a private prison?)
- **Any Government Outsourcing Anything.** If you examine the claim that private companies are always more efficient than government, the argument starts to fall apart. Just how are companies more efficient? The first way is supposed to be cost-savings. But how do companies save money. There are two ways: reduce what they pay employees/suppliers and cut back on the amount or quality of service. People who are employed by the city to perform tasks are laid off, and things are turned over to the company. Typically, the company will hire people at as close to minimum wage as possible, and likely with no benefits. It will employ fewer managers, and pay them less. It will cut back on maintenance of the fleet, and it will try to cut back on the service. Does this situation actually save government money? If people with okay public employee jobs are replaced by lower paid workers, the community is poorer in the aggregate. More people will need public safety net services. There will be foreclosures, tax revenues will drop because of lower pay, but also because poorer people cannot spend as much in stores. Sales taxes drop as stores face fewer customers able to get by. The next time someone tells you private companies are always more efficient than government, tell them that the facts are against them, it has been tried and just has not worked. (Or just give them the Bronx cheer.)

9. SIX WAYS TO INSURE EMPLOYEES TAKE VACATION THIS SUMMER:

Ebn.benefitnews.com says that despite time away from work being a key ingredient to work-life balance, many Americans do not take full advantage of their paid vacation benefits. Fifty-nine percent of respondents to a recent survey said they left at least one paid time off day unused at the end of last year, while 35% of them left five days or more. Here are ways benefits professionals say can help end America's vacation deprivation:

- **Let Gandhi be your guide.** Like Gandhi inspires, be the change you want to see. Set a good example and take all of your own vacation.
- **Reward with vacation days.** Offer additional vacation days as a reward for outstanding performance, innovation and solutions to challenges.
- **Make it mandatory.** If feasible, stipulate that all employees must take their allotted

vacation every year.

- **Use it or lose it.** If you are uncomfortable with mandatory policies or it is not feasible for your workplace, use-it-or-lose-it is another approach. Or, eliminate or limit the ability for employees to cash out vacation days.
- **Make the business case.** Make the business case for adopting a more liberal vacation policy. It is no coincidence that most of the companies on Fortune's 100 Best Companies to Work for list not only have generous perks, but also post impressive business results.
- **Offer voluntary options.** Offer vacation options (excluding airfare), such as hotels, cruises, destination packages and all-inclusive resorts as a payroll-deducted voluntary benefit.

10. FPPTA 30TH ANNUAL CONFERENCE: The Florida Public Pension Trustees Association's 30th Annual Conference will take place on June 29 – July 2, 2014 at the Hilton Bonnet Creek, Orlando. A link on FPPTA's web site, www.fppta.org, will take you to the Hilton Bonnet Creek site to make your room reservations. You may access information and updates about the Conference at FPPTA's website. All police officer and firefighter plan participants, board of trustee members, plan sponsors and anyone interested in the administration and operation of the Chapters 175 and 185 pension plans should take advantage of this Conference.

11. WHY TEACHERS DRINK: Q. Name the four seasons? A. Salt, pepper, mustard and vinegar.

12. TODAY IN HISTORY: In 1988, 1st Children's Miracle Network Telethon raises \$590,000.

13. KEEP THOSE CARDS AND LETTERS COMING: Several readers regularly supply us with suggestions or tips for newsletter items. Please feel free to send us or point us to matters you think would be of interest to our readers. Subject to editorial discretion, we may print them. Rest assured that we will not publish any names as referring sources.

14. PLEASE SHARE OUR NEWSLETTER: Our newsletter readership is not limited to the number of people who choose to enter a free subscription. Many pension board administrators provide hard copies in their meeting agenda. Other administrators forward the newsletter electronically to trustees. In any event, please tell those you feel may be interested that they can subscribe to their own free copy of the newsletter at <http://www.cypen.com/subscribe.htm>.

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