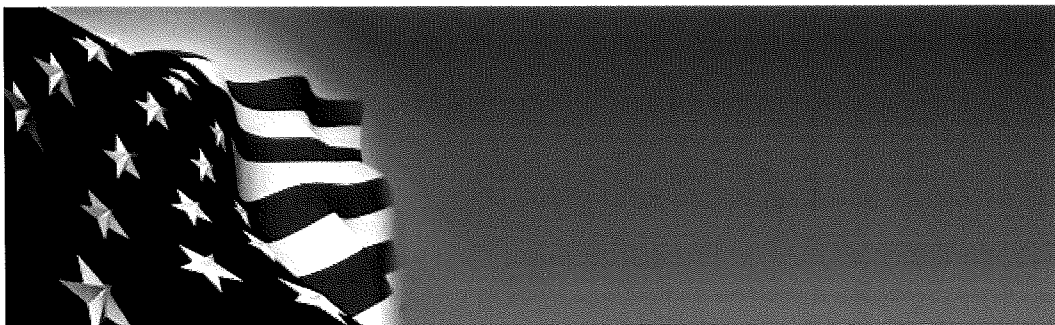


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# CYPEN & CYPEN NEWSLETTER for OCTOBER 2, 2014

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Stephen H. Cypen, Esq., Editor

Never Forget September 11, 2001

and

Always Remember May 2, 2011

**1. FPPTA TRUSTEES SCHOOL:** The Florida Public Pension Trustees Association's Trustee School will take place on October 5 – 8 at the Hyatt Regency Coconut Point, Bonita Springs. A link on FPPTA's web site, [www.fppta.org](http://www.fppta.org), will take you to the Hyatt Regency Coconut Point 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.

**2. TOUGH CHOICES FACE FLORIDA'S GOVERNMENTS:** Public pensions continue to be a significant source of financial stress in many state and local governments. Although news headlines generally focus on a few particularly distressed governments, such as Detroit and Chicago, the challenge of managing pension obligations is widespread, and leading taxpayers and employee groups across the country to look more closely at the financial condition of their own pension plans. Investigating public pension obligations is relatively easy in most states, since there is usually only a handful of statewide plans and relatively few local ones. It is more difficult in Florida because of the large number of locally sponsored pension plans. The Florida Department of Management Services monitors 491 local government plans -- only Illinois and Pennsylvania have more. Beginning in February 2011, Florida State University's LeRoy Collins Institute issued a series of reports highlighting funding and management issues in Florida municipal pension plans. In November 2011, the Institute published a report card that graded 208

defined benefit plans in the state's 100 largest cities. At that time, the Institute found many well-funded plans -- 14% percent received an A grade -- but nearly a third of the plans received Ds or Fs. The new report updates that report card with new information. Financial condition of public pensions should be of concern to plan beneficiaries, employees, taxpayers, local leaders, business leaders and future generations. The report provides information on the financial condition of Florida municipal pensions for most of the past decade (2005-2012). The data reflect information on 320 pension plans from 151 cities. Each plan is given a letter grade based on five measures of the financial condition of public pensions. The entire report is available at <http://collinsinstitute.fsu.edu/sites/collinsinstitute.fsu.edu/files/Tough%20Choices%20Report%20Card%20Update%20SEP%202014.pdf>. Note, the report is only as good as its arbitrary measures and arbitrary weight given too each one.

**3. UNDERSTANDING FLORIDA'S LOCAL PENSION PLANS:** Presented by Florida Public Pension Trustees Association, "Understanding Florida's Local Pension Plans" should be close at hand for every trustee in Florida (and elsewhere). The easy-to-understand primer can be downloaded at [http://www.publicpensioninstitute.org/public/images/PrimerForStateLegislators\\_2014.pdf](http://www.publicpensioninstitute.org/public/images/PrimerForStateLegislators_2014.pdf). There are 411 incorporated cities in the State of Florida, with 334 sponsoring at least one type of retirement plan, either a defined benefit plan or defined contribution account. Florida has 491 local and special district defined benefit retirement plans sponsored by 239 local governments. Many local governments sponsor more than one plan -- separating general employees from firefighters and police officers. These local plans provide guaranteed retirement benefits, as well as death and disability protections to 101,081 active employees and nearly 83,950 retired employees and beneficiaries in the state of Florida. The 491 plans are broken down as follows:

- 160 general employee plans
- 140 police officer plans
- 136 firefighter plans
- 6 police officer and firefighter plans combined
- 41 general employees, police officers and firefighter combined plans
- 6 school board early retirement plans
- 2 other combinations

Among the plan characteristics, 91% offer disability benefits; 89% offer early retirement benefits; and 51% provide for a cost-of-living adjustment for the retirees. Normal retirement benefits are based on a benefit accrual rate, number of years in the average final compensation, age, and years of service. There may be provisions for early retirement, death and disability, and cost-of-living adjustments. Each local government, through negotiations and agreement with the employees' unions, determines the retirement benefits provided to the employees. These benefits are then enacted into law through a local ordinance and administered by the local trustees of the retirement system. Two other facts:

- Pension contributions made by state and local governments account for only **3.7%**

of direct general spending. (Yes, you read that right.)

- The largest portion of pension benefits for public employees, **61%**, comes from the pension fund's investment earnings.

**4. AN INTRODUCTION TO QUALIFICATION AND TAXATION ISSUES FOR GOVERNMENTAL RETIREMENT PLANS:** National Conference on Public Employee Retirement Systems, together with Ice Miller LLP, has published a primer for plan administrators dealing with qualification and taxation issues for governmental retirement plans. Its purpose is to give an overview of the basic qualification requirements and general taxation issues under the Internal Revenue Code, as applicable to governmental plans. The primer is not an exhaustive study of each requirement and is not intended to constitute legal advice on any particular issue. The primer is a brief summary of important topics for consideration by plan administrators:

- Why is qualification under Code § 401(a) so important to a governmental plan?
- Why is qualification of a "governmental plan" so important?
- How does a qualified governmental plan preserve qualified status?
- Why do many governmental plans seek an IRS determination letter?
- What are the advantages to individual members if their governmental plan has a determination letter?

The primer addresses many (but not all) of the applicable Internal Revenue Code provisions, focusing on those issues of greatest concern to plan administrators of defined benefit governmental plans. The bulk of it is organized in code-cite order. Please note that the primer does not discuss governmental defined contribution plans intended to be covered under Code §§ 403(b) or 457, though some of the concepts discussed also apply to those plans. Finally, to the extent that the plan has specific questions regarding its qualified status or its compliance requirements, plan counsel should be consulted. You can access the primer at <http://www.ncpers.org/files/Primer.pdf>.

**5. SPECIAL NEEDS TRUST MAY STAND IN CHILD'S PLACE AS BENEFICIARY TO WHOM SURVIVORS' BENEFITS WERE DUE:** The Supreme Court of New Jersey reviewed whether the disabled son of a retired member of the Police and Firemen's Retirement System may have his survivors' benefit paid into a first-party special needs trust created for him under federal law. The Court held that he may, and reversed the contrary administrative action by the board of trustees. The board's strict view of how to implement the word "child" in the survivors' benefits statute when dealing with the circumstances of a Supplemental Security Income eligible disabled child of a pension system retiree would have forced this class of beneficiary into an untenable situation. The board's determination required a disabled child of a pension system retiree to have to choose between abandoning the survivors' benefit earned by his father and forgoing public assistance programs for his medical needs. That choice is harsh and unwarranted. No legitimate public policy is advanced by the board's interpretation. Both the federal government's SSI and related medical assistance programs, as well as New Jersey's Special Needs statutes, permit use of self-settled special needs trust. The Court rejected as arbitrary, capricious, and unconscionable the board's interpretive

determination that foists on disabled children of pension system retirees, such as the child involved here, was essentially a forfeiture of survivors' benefits. Saccone's son, Anthony, suffers from a severe mental disability and currently receives public assistance in the form of SSI and other programs. However, those forms of public assistance are available only to individuals with incomes below a specified amount. Fearing that Anthony's statutorily directed share of the survivors' benefits would place him over the SSI income cap and thereby disqualify him from receiving public assistance, Saccone wanted to ensure that the pension systems survivors' benefits for Anthony would be paid to the "Anthony J. Saccone Supplemental Benefits Trust." Because assets held within a supplemental benefits trust are not counted as income for the purpose of many public assistance programs, Saccone believed that designating a supplemental benefits or special needs trust as the beneficiary in Anthony's stead would allow Anthony to receive Saccone's death benefits without jeopardizing Anthony's eligibility for public assistance. The Court found that the only thing that had to be determined was whether a first-party special needs trust established for Anthony under federal law may stand in his place of beneficiary to whom survivors' benefits are due under the retirement system. The Court concluded that it may. Two Justices dissented:

This appeal presents a straight-forward question of statutory interpretation. This appeal is not about the good faith of Thomas Saccone, the retired PFRS member. This appeal is not about the wisdom and benefits of an SNT for a disabled, dependent child. Indeed, we have acknowledged the importance of such trusts in any plan for the financial security of a disabled, dependent child and have endeavored to set forth an analytical framework to further such planning when the parents of a disabled, dependent child have divorced. [Citations omitted.]

While I agree with the majority's conclusion that the Board's application of [New Jersey Statute] led to an unfortunate result in this case, the plain language of the statute prohibits a PFRS member from designating the beneficiary of his or her survivors' benefits. The public policy favoring the establishment of SNTs should not supersede the plain language of the statutory provisions which prohibit a retiree from designating a beneficiary other than his spouse or child. Further, the various amendments made to the statute in 1967 evince an unequivocal legislative intent to exclusively limit the survivors' benefit. Therefore, I respectfully dissent and would affirm the Appellate Division judgment. Any changes to the statute which would allow a retiree to designate an SNT as a beneficiary are best left to the Legislature.

Most lawyers know that hard facts make bad law. *Saccone v. Board of Trustees of the Police and Firemen's Retirement System*, Case No. (N.J. September 11, 2014).

**6. ENTITLEMENT REFORM IN THE FUTURE OF PENSIONS:** The Pension Research Council at The Wharton School has issued a new working paper dealing with Entitlement Reform and the Future of Pensions. The United States retirement system is in a state of flux. Large public health programs, notably Medicare and Medicaid, are a cornerstone of American retirement. Unfortunately, these programs are on an unsustainable path due to the aging of the population and prolonged growth in costs for both federal government

and retirees themselves. Social Security's future solvency, while less of a budgetary challenge than major health programs, is also in doubt, with adjustments either to revenue or benefits required to bring the program into long term balance. At the same time, the decades-long transformation of the private, employer-based retirement system is nearly complete, with most private savers working to accumulate liquid assets for retirement rather than credit towards their lifetime pension. All three systems affecting the elderly -- health, Social Security, and employer-based retirement plans -- have not been reformed substantially in decades. Indeed, they have adapted too slowly to fundamental changes in the broader demographic and fiscal landscape. Close to one-third of all adults are scheduled to be on Social Security for one-third of their adult lives, and only a modest percentage of households has private assets at time of retirement near the value of their government health and retirement benefits. As a result, all of the growth in government spending over the next two decades is scheduled to go for Social Security, Medicare and Medicaid, plus interest on the debt. To be clear, the authors believe there are viable and feasible reform options, but agreeing on them requires shifts in both policy priorities and federal law. To this end, they offer a series of policy suggestions that could result in an environment that would better protect the most vulnerable retirees and minimize adverse effects on the middle class and the economy as a whole. PRC WP2014-08 (September 2014).

#### **7. TOTAL HOLDINGS AND INVESTMENTS OF MAJOR PUBLIC PENSION SYSTEMS INCREASED TO OVER \$3.4 TRILLION, REMAINS THE HIGHEST LEVEL SINCE SURVEY BEGAN IN 1968:**

The U.S. Census Bureau has released its quarterly survey of public pensions for the second quarter of 2014. For the 100 largest public employee pension systems in the country, cash and security holdings totaled \$3,365.4 billion for the second quarter of 2014, reaching the highest level since the survey began collecting data in 1968 (The summary is based on the quarterly survey of public pensions, which consists of a panel of the 100 largest state and local government pension systems, as determined by the total cash and security holdings reported in the 2007 census of governments. These 100 systems make up 89.4% of financial activity among such entities, based on that census. Each of the 100 systems represents itself only. The data are not subject to sampling error, but are subject to various non-sampling errors, such as errors of nonresponse and respondent error.) Cash and security holdings had a quarter-to-quarter increase of 4.6%, from \$3,218.2 billion last quarter and a year-to-year increase of 14.3%, from \$2,945.6 billion in the second quarter of 2013. Earnings on investments totaled \$129.4 billion in the second quarter of 2014. Corporate stocks had a quarter-to-quarter increase of 7.4%, from \$1,094.9 billion to \$1,176.0 billion in the second quarter of 2014. Corporate stocks year-to-year increased 15.5% from \$1,018.1 billion in the second quarter of 2013. Corporate stocks composed 35.0% of the total cash and security holdings. Corporate bonds had a quarter-to-quarter increase of 7.1%, from \$346.9 billion to \$371.5 billion in the second quarter of 2014. Corporate bonds year-to-year increased 16.1%, from \$319.9 billion in the second quarter of 2013. Corporate bonds comprised 11.0% of the total cash and security holdings. International securities had a quarter-to-quarter decrease of 2.8% from \$675.2 billion to \$656.5 billion in the second quarter of 2014. International securities year-to-year increased 11.3%, from \$590.0 in the second quarter of 2013. International securities comprised 19.5% of

total cash and security holdings. Federal government securities had a quarter-to-quarter increase of 12.4%, from \$273.9 billion to \$307.8 billion in the second quarter of 2014. Federal government securities year-to-year increased 16.0%, from \$265.4 billion in the second quarter of 2013. Federal government securities equaled 9.1% of the total cash and security holdings. Government contributions had a quarter-to-quarter decrease of 6.8%, from \$25.7 billion to \$24.0 billion in the second quarter of 2014, and a year-to-year increase of 4.8%, from \$22.9 billion in the second quarter of 2013. Employee contributions had a quarter-to-quarter increase of 3.4%, from \$10.9 billion to \$11.3 billion in the second quarter of 2014, and a year-to-year decrease of 1.4%, from \$11.4 billion in the second quarter of 2013.

**8. FLORIDA DOCUMENTARY STAMP TAX APPLIES TO PLAN LOANS:** In a blog, Bryan Cave says if your 401(k) plan maintains a participant loan program, you may discover that you have compliance concerns thanks to a relatively obscure Florida statute. Under its revenue laws, Florida imposes a document tax on loan transactions that are made, signed, executed, issued, or otherwise transacted in the State. (Section 201.08, Florida Statutes, sets the tax at \$0.35 on each \$100 or fraction there of the indebtedness or obligation.) The Florida Department of Revenue has specifically ruled that 401(k) plan loans are subject to the tax. The law further provides that no state court may enforce the provisions of a promissory note if the document tax is not paid. It would be a challenge to sustain a position that the Florida statute is preempted by ERISA. A failure to pay the tax, therefore, could mean that a 401(k) plan is extending loans that are not adequately secured, creating potential for both prohibited transaction issues and plan operational failure issues. The Florida statute arguably reaches not only plan loans extended to participants who are Florida residents but to plans with sponsors resident in Florida or third party administrators resident in Florida. The Florida law does contemplate a process for paying past due taxes. The only good news is that no other state appears to have a similar transactional tax that would apply to plan loans. Caveat: there is no reason to believe that the statute would not apply to DROP loans.

**9. INTERNAL REVENUE SERVICE SETS FISCAL YEAR 2014 MAXIMUM PER DIEM REIMBURSEMENT RATES:** Internal Revenue Service has issued its annual update of special per diem rates for use in substantiating certain business expenses taxpayers incur when traveling away from home in 2014 and 2015 (Notice 2014-57). The notice provides the transportation industry meal and incidental expenses rates, the rate for the incidental-expenses-only deduction and the rates and list of high-cost localities for purposes of the high-low substantiation method. Following are the per diem rates for lodging expenses and meals and incidental expenses, or M&IE, incurred during business travel for Miami-Dade County:

- Season begin date – October 1; Season end date – March 31; Lodging rate -- \$259; M&IE rate -- \$66.
- Season begin date -- April 1; Season end date – May 31; Lodging rate -- \$138; M&IE rate -- \$6.

- Season begin date -- June 1; Season end date -- September 30; Lodging rate -- \$109; M&IE rate -- \$66.

**10. WHAT IT COSTS TO SEE AN NFL FOOTBALL GAME:** The Dallas Cowboys is the most expensive team in the National Football League in terms of costs to fans, according to southflorida.citybizlist.com. This season, fans of the Dallas team will have to pay \$166.70 on average to see them in person. San Francisco 49ers (\$159.50) and New England Patriots (\$157.50) round out the three most expensive teams. Estimates are based on Adult Cost Index, which itself is built on data from surveys of teams. The ACI is the cost for a single fan to purchase an average priced ticket, one beer, one soft drink, one hot dog, and half the cost of parking at the stadium. The average ACI in the NFL this season is \$117.81, up 3.9% from last season (\$113.42). Of the 32 teams in the NFL, 22 have an ACI of at least \$100.00. Miami Dolphins at \$92.91 are number 30 and the Cleveland Browns at \$81.95 are dead last.

**11. INTERESTING FACTS:** The University of Alaska spans four time zones.

**12. TODAY IN HISTORY:** In 1919, President Woodrow Wilson has a stroke, leaving him partially paralyzed.

**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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