



CYPEN & CYPEN
NEWSLETTER
for
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Never Forget September 11, 2001

and

Always Remember May 2, 2011

1. NASRA ON TOTAL PENSION PLAN INVESTMENT RETURN

ASSUMPTIONS: National Association of State Retirement

Administrators has issued a brief on public pension plans investment return assumptions. Some critics of current public pension investment return assumption levels say that current low interest rates and volatile investment markets require public pension funds to take on excessive

investment risk to achieve their assumption. Because investment earnings account for a majority of revenue for a typical public pension fund, the accuracy of the assumption has a major effect on the plan's finances and actuarial funding level. An investment return assumption that is set too low will overstate liabilities and costs, causing current taxpayers to be overcharged and future taxpayers to be undercharged. A rate set too high will understate liabilities, undercharging current taxpayers, at the expense of future taxpayers. An assumption that is significantly wrong in either direction will cause a misallocation of resources and unfairly distribute costs among generations of taxpayers. Although public pension funds, like other investors, experienced sub-par returns in the 2008-09 decline in global equity markets, and in 2015, median public pension fund returns over a longer period exceed the assumed rates used by most plans. Specifically, the median annualized investment return for the 25-year period ended December 31, 2015, exceeds the average assumption of 7.62%. Public retirement systems typically follow guidelines set forth by the Actuarial Standards Board to set and review their actuarial assumptions, including the expected rate of investment return. Most systems review their actuarial assumptions regularly, pursuant to state or local statute or system policy. Actuarial Standards of Practice No. 27 (ASOP 27) prescribes the considerations actuaries should make in setting an investment return assumption. As described in ASOP 27, the process for establishing and reviewing the investment return assumption involves consideration of various financial, economic, and market factors, and is based on a very long term view, typically 30 to 50 years. A primary objective for using a long term

approach in setting public pensions' return assumption is to promote stability and predictability of cost to ensure intergenerational equity among taxpayers. The investment return assumption used by public pension plans typically contains two components: inflation and the real rate of return. The sum of these is the nominal return rate, which is the rate that is most often used and cited. The inflation assumption typically is applied also to other actuarial assumptions, such as the assumed level of wage growth and, depending on the plan's benefit structure, assumed rates of cost-of-living adjustments. The second component of the investment return assumption is the real rate of return, which is the return on investment after adjusting for inflation. The real rate of return is intended to reflect the return produced as a result of the risk taken in investing the assets. Achieving a return approximately commensurate with the inflation rate normally is attainable by investing in securities, such as US Treasury bonds, that are considered to be risk free, that pay a guaranteed rate of return that is absolutely risk free. Achieving a return higher than the risk free rate requires taking some investment risk; for public pension funds, this risk takes the form of investments in public and private equities, real estate, and other asset classes. The average real rate of return among plans in the Public Fund Survey has risen since FY 01, from approximately 4.25% to 4.60%. This has occurred as a result of some plans that have reduced their inflation assumption without changing their nominal investment return assumption; or reductions in inflation assumptions by an amount greater than they have reduced their nominal assumption; or both. Unlike public pension plans, corporate plans are required by federal regulations to make

contributions on the basis of current interest rates. This method results in plan costs that are volatile and uncertain, often changing dramatically from one year to the next. This volatility is due in part to fluctuations in interest rates and has been identified as a leading factor in the decision among corporations to abandon their pension plans. By focusing on the long term and relying on a stable investment return assumption, public plans experience less volatility of costs. Since 1985, public pension funds have accrued an estimated \$6.7 trillion in revenue, of which \$4.3 trillion, or 64%, is estimated to have come from investment earnings. Employer contributions account for \$1.6 trillion, or 25% of the total, and employee contributions total \$755 billion, or 11%. Public retirement systems operate over long timeframes and manage assets for participants whose involvement with the plan can last more than half a century. Consider the case of a newly-hired public school teacher who is 30 years old. If this pension plan participant elects to make a career out of teaching school, he may work for 35 years, to age 65, and live another 25 years, to age 90. This teacher's pension plan will receive contributions for the first 35 years and then pay out benefits for another 25 years. During the entire 60-year period, the plan is investing assets on behalf of this participant. To emphasize the long term nature of the investment return assumption, for a typical career employee, more than one-half of the investment income earned on assets accumulated to pay benefits is received after the employee retires. The investment return assumption is established through a process that considers factors such as economic and financial criteria; the plan's liabilities; and the plan's asset allocation, which reflects the plan's capital market assumptions,

risk tolerance, and projected cash flows. Standards for setting an investment return assumption, established and maintained by professional actuaries, recommend that actuaries consider a range of specified factors, including current and projected interest rates and rates of inflation; historic and projected returns for individual asset classes; and historic returns of the fund itself. The investment return assumption reflects a value within the projected range. Many public pension plans have reduced their return assumption in recent years. Among the 127 plans measured, more than one-half have reduced their investment return assumption since fiscal year 2008. The average return assumption is 7.62%. Over the last 25 years, a period that has included three economic recessions and four years when median public pension fund investment returns were negative, public pension funds have exceeded their assumed rates of investment return. Changes in economic and financial conditions are causing many public plans to reconsider their investment return assumption. Such a consideration must include a range of financial and economic factors while remaining consistent with the long timeframe under which plans operate.

2. ARIZONA FACES COMPLICATED PUBLIC PENSION SITUATION:

Governing recognizes that Illinois's and New Jersey's public pensions may be in worse shape, but Arizona takes a backseat to no one when it comes to pension intrigue. A case before the state's Supreme Court highlights that intrigue, as well as some of the basic decisions state and local governments face while they grapple with the sustainability of their retirement systems. In 2011, Arizona enacted reforms to its Public

Safety Personnel Retirement System, which at the time also included the Elected Officials Retirement Plan. The changes required increased contributions and reduced benefits. A 2014 state Supreme Court ruling restored retiree COLAs. Now a case brought by two active judges, challenging the increased employee contributions, has made its way to Arizona's Supreme Court after a lower court ruled that the state must refund the increased contributions. While the judges' case is before the Supreme Court, that is not exactly who will be hearing it. Four out of the five justices recused themselves because they would benefit from any refund. The fifth was appointed after the EORP was closed to new members, so he will be part of a special five-judge panel who will hear the case. And since the EORP was part of the PSPRS, the panel's ruling will also affect police and firefighters. The quagmire is further complicated by a voter-approved 1998 state constitutional amendment saying that public retirement benefits shall not be diminished or impaired, a provision not unique among the states, and was a basis of the lower court's ruling. EORP was shut down because it was expensive. Bargaining parties might consider higher salaries rather than higher pension benefits, but, in any event, if pensions are offered, both employees and taxpayers had better be prepared to pay for them. So, what else is new?

3. GOOD NEWS FOR ACTORS' PENSION PLAN: It is Oscar time. While some actors are choosing which designer they will be wearing on the red carpet in nervous anticipation of the final rip of those famous envelopes, all actors and producers were awarded the good news of

their pension fund's high rating by the Society of Actuaries. Pionline.com reports that the Screen Actors Guild-Producers Pension & Health Plans, was 84% funded, with \$3.5 billion in assets against accumulated benefit liabilities of \$4.2 billion, thus, putting the plan in the green zone, using the IRS's red-yellow-green zone system. The pension plan continues to carry a funding ratio greater than 80%, with assets between \$3 billion and \$3.5 billion. The SAG Producers pension fund might be ready for its close up with its funding ratio about average for all multiemployer plans, but television is outshining Hollywood in this regard. The \$2.3 billion AFTRA Health & Retirement Funds, the New York-based union pension fund for television and radio workers was 90% funded.

4. MAXIMIZE YOUR SOCIAL SECURITY BENEFITS: An extensive article from Bond Schoeneck & King warns "*April, 2016 Law Change Prompts Immediate Review.*" The Social Security old age system is a simple concept with some very complex rules. It is a near-universal arrangement, covering working Americans and their families, which provides retirement benefits for life. The basic rules require a minimum of 40 quarters of coverage -- essentially 10 years of paying into the system as an employee or self-employed person. Benefits are based on your highest 35 year average of covered earnings, which determines a "primary insurance amount" or "PIA." The PIA is payable at your "full retirement age" or "FRA," which was once age 65. For individuals born in years 1943 through 1954, FRA is age 66, and it increases to age 67 for anyone born in 1960 or thereafter. The Social Security system has been the subject of debate and political opinion. Undoubtedly, the

system will be changed in years to come. Nonetheless, it is a relatively vast and stable system that is likely to endure over time. This article is based on current Social Security laws as well as the changes adopted in late 2015, which go into effect on May 1, 2016. The article contains the following subheadings:

- Basic Rules
- Options for Married Couples
- "File and Suspend" Tactic
- Further notes to the "file and suspend" strategy
- "File and Restrict" Tactic
- Where To Go From Here

Read the entire article at: <http://www.bsk.com/media-center/3375-employee-benefits-maximize-your-social-security-benefits-2-16>.

5. WORKERS' COMP HEART PRESUMPTION DECISION

REVERSED AND REMANDED...AGAIN: A workers' compensation case recurred before the Florida First District Court of Appeal.

Previously, the Employer challenged the JCC's determination that it had not defeated the presumption of occupational causation to which the parties agreed claimant, a law enforcement officer, was entitled under Section 112.18(1)(a), Florida Statutes. In the first appeal, the appellate court agreed that the JCC ignored or overlooked parts of the medical opinion testimony when he concluded that claimant's slow accessory pathway was not a congenital condition. The court reversed and remanded to the JCC for consideration of the medical evidence in its

entirety. On remand, no new evidence was submitted. The parties were afforded the opportunity to direct the JCC to those portions of the doctors' depositions that they believed supported their respective positions regarding claimant's entitlement to benefits. The JCC reversed his previous conclusion that the slow accessory pathway was not a congenital condition. The JCC noted that it was the employer's burden to prove a non-occupational cause of the supra ventricular tachycardia by competent evidence. He found that a non-occupational underlying medical condition, the slow pathway-AV node, was the root of the ultimate SVT, which had a trigger of unspecified etiology. Because the SVT would not have occurred but for the existence of the congenital slow pathway, the JCC concluded that the SVT must also be found to be a product of the underlying congenital, non-occupational condition. Accordingly, the JCC found claimant's claim not compensable. Unfortunately, the JCC made no findings regarding whether or not any potential trigger or triggers for the SVT were occupational; rather, he erroneously concluded that, because the underlying slow accessory pathway was congenital (non-occupational), so too was the trigger. Based on the foregoing, the court again reversed and remanded for further proceedings, this time indicating the parties may include reopening of the medical evidence to address the trigger issue. *Mitchell v. Miami Dade County a/k/a/ MDPD (INTERCOASTAL)* 41 Fla. L. Weekly D454 (Fla. 1st DCA February 23, 2016).

6. CITIZENS HAVE NO FIRST AMENDMENT RIGHT TO FILM

POLICE: Citizens do not have a First Amendment right to film police

officers, absent a challenge to their conduct, a federal judge has ruled in a case of first impression. According to *The Legal Intelligencer*, U.S. District Judge Mark Kearney of the Eastern District of Pennsylvania issued his ruling in two consolidated cases filed against the city of Philadelphia by citizens whose cellphones were confiscated after they either photographed police activity or were barred from filming police activity. Neither plaintiff was filming the police conduct because of any criticism or challenge to what was happening. One thought the conduct was an interesting scene and would make for a good picture. The other was a legal observer trained to observe police. The citizens urged the Court to find, for the first time, photographing police without any challenge or criticism is expressive conduct protected by the First Amendment. While the court instinctively understand the citizens' argument, particularly with rapidly developing instant image sharing technology, the court found no basis to craft a new First Amendment right based solely on observing and recording without expressive conduct and, consistent with the teachings of the Supreme Court and the court of appeals, declined to do so. The Judge was not addressing whether the police's conduct in either of the plaintiffs' cases violated their Fourth Amendment rights, which the Judge said was up to a jury to determine. He was also not ruling on whether a First Amendment right to film police exists when the conduct was being challenged. While courts applying the Fourth Amendment have long held police may not seize phones or arrest citizens without probable cause and cannot use excessive force, the case only asks to study one snapshot in time through the lens of the First Amendment only: whether photographing or

filming police on our portable devices without challenging police is expressive conduct protected by the First Amendment.

7. COULD SOCIAL SECURITY STATEMENT DO MORE?: A new blog from Center from Retirement Research at Boston College informs that two out of three working Americans grade their retirement readiness at no better than a “C.” So, how about using the Social Security Statement that lands in their mailboxes, grabbing their attention, to spur them to action? The statement is already valued by millions of Americans. A survey by the U.S. Social Security Administration found that people who received statements were dramatically more knowledgeable about their basic pension benefits than people who had already retired when SSA started mailing them out in the mid-1990s. Social Security is the nation’s most important source of retirement income, and the information in the statements is essential to most workers’ retirement planning. Mailed out before every fifth birthday -- 25, 30, 35, *etc.* -- and annually at age 60, the statement provides estimates of each worker’s future benefits at three different claiming ages: 62, when they have access to their smallest monthly benefit; the “full retirement age”; and 70, when workers receive their highest monthly benefit. It clearly lays out how much workers can increase their monthly retirement income by delaying when they start collecting their benefits. (In lieu of paper statements, people who sign up online can check their benefits anytime and will receive an email every year when their updated statement becomes available): <https://faq.ssa.gov/link/portal/34011/34019/Article/3709/How-can-I-get-a-Social-Security-Statement-that-shows-a-record-of-my->

[earnings-and-an-estimate-of-my-future-benefits](#). New evidence is emerging that workers are moving in the right direction, with more of them delaying the age at which they claim their benefits. But the statement does not get credit for driving these decisions. Reasons for these delays include employers shifting away from traditional pensions. Controlling for this and other influences on retirement timing, one study found that the mailed statements had no impact on when workers claimed their benefits. Further, too many people apparently are not reading the statements coming in the mail. Nearly one-third of workers who were less than two years away from signing up for their benefits were unable to estimate how much they would receive, even though they had been receiving yearly statements for a decade. For the majority who do read them, though, it is reassuring to get a statement in the mail. But this is a false sense of security, if workers do not actually act on what it tells them.

8. HOW DO NON-FINANCIAL FACTORS AFFECT RETIREMENT DECISIONS?: The introduction to a new issue brief from Center for Retirement Research at Boston College says that financial factors clearly influence retirement decisions, as everyone would like to have sufficient income when leaving the workforce. But numerous studies find that such factors are only a small part of the story. Non-financial considerations clearly contribute to the decision to retire. The brief reviews studies to determine how two types of non-financial factors affect retirement decisions: the worker's on-the-job experience and the allure of retirement activities. The discussion proceeds as follows. The

first section presents evidence that a positive work experience is a critical component in decisions of workers ages 65 and over to remain in the labor force. The second section identifies job characteristics that either incline workers to retire or to remain on the job. The third section examines how personal objectives affect work/retirement decisions. The final section concludes that non-financial benefits seem far more important than non-financial costs -- both in keeping some workers in the labor force and drawing others into retirement. Given the importance of the decision to workers' financial well-being, it is important that they also understand and carefully weigh the financial implications in deciding when to exit the labor force. Few workers, however, are equipped even to estimate the financial implications. This inability raises the prospect of many workers being pulled out of the labor force too early to gain a financially secure retirement. February 2016, Number 16-3.

9. INSTITUTIONAL INVESTORS STILL FAIL TO PUT TO BRAKES ON AMERICA'S 100 MOST OVERPAID CEOs:

Leading mutual funds and pension funds so far have taken little action to curb the extraordinary misallocation of assets represented by the excessive compensation of America's top 100 overpaid CEOs, according to a new report from *As You Sow*. The report identifies Calamos, Steward, TCW Wadell & Reed, BlackRock and Vanguard as among the 10 mutual fund families most likely to rubberstamp excessive compensation for CEOs. Titled *The 100 Most Overpaid CEOs: Are Fund Managers Asleep at the Wheel?*, and available online at www.asyousow.org/ceopay, the report

cites David Zaslav/Discovery Communications Inc., Leslie Moonves/CBS Corporation, Steve Eells and Marty Moran/Chipotle Mexican Grill Inc., Satya Nadella/Microsoft Corporation, and Jeffrey Leiden/Vertex Pharmaceuticals Inc., as being among the most overpaid CEOs in America. Of the top 25 most overpaid CEOs in the *As You Sow* list, eleven made the list for the second year in a row. The report concludes: CEO compensation as it is currently structured does not work: rather than incentivize sustainable growth, it increases disproportionately by every measure, and receives no consequences. Too often it rewards deals above development and risk rather than return on invested capital. The Economic Policy Institute notes that over the period of 1978 to 2013, the inflation-adjusted pay of a typical worker grew by about 0.4% a year (a total of 10% over 35 years) while the pay of a typical CEO grew almost a hundredfold. CEO pay grew an astounding 997% over the past 36 years, greatly outpacing the S&P 500, which has grown only 504% in this time period. The 100 most overpaid CEOs deserve more scrutiny than they are getting today from mutual funds and pension funds. Now is the time for shareholders, particularly those with fiduciary responsibilities, to become more engaged in their analysis of executive pay and those who award these packages. The report puts the focus where it belongs, on the institutional investors and board members who are responsible for pay packages that distort incentives and pay too much for too little. Everyone wants to be properly compensated for the work they do; it is part of the American dream and bedrock of the capitalist system. However, the process which determines CEO pay is broken. The good

news is that there are ways to curb excessive CEO pay before it becomes a more inexorable problem, and responsible investors are leading the way in providing reasonable solutions. Other key findings are

- The most overpaid CEOs represent an extraordinary misallocation of assets. Seventeen CEOs with compensation at least \$20 million more in compensation in 2014 than they would have garnered if their pay had been aligned with performance. For example, Discovery awarded its CEO an astonishing \$156 million in compensation. If existing pay packages bore a simple linear relationship to performance, that pay would have been roughly \$14 million -- resulting in \$142 million in excess pay.
- The company that ranked first for poor CEO pay practices last year, Nabors Industries, has seen such a decline in market capitalization that it was removed from the S&P 500. Of the 100 companies in the 2015 list, there are 66 that are repeats from last year.
- Pension funds are making some progress on opposing high CEO pay. One of the funds with the greatest change was CalPERS, which last year opposed just 30% of the overpaid CEO pay package, and this year increased that opposition level to 47% of the overall CEO pay packages, an increase of more than 50% its opposition.
- Mutual funds are far more likely to rubberstamp high CEO pay than are pension funds. Of the largest mutual funds, American

and Schwab approved 65% of these packages, while Blackrock supported 97% of them. Some funds seem routinely to rubber stamp management pay practices, enabling the worst offenders, and failing in their fiduciary duty.

- Socially responsible investing mutual funds were more likely to vote against excessive pay packages. Eleven SRI mutual funds were surveyed. Of these, one mutual fund, Green Century, failed to cast a vote either for or against any of the 40 say-on-pay resolutions that they voted on, instead abstaining on all.
- Directors play a key role in encouraging excessive CEO compensation. There are 21 directors who serve on two or more of the boards highlighted. Three directors serve on three such boards. Retired Johnson & Johnson CEO William Weldon serves on the boards of CVS, Exxon Mobil, and JP Morgan -- all three companies ranked in this study. Retired Exxon CEO Ray Arani serves on the compensation committee of Wynn Resorts. It may be that such CEOs who were extraordinarily well-paid for their tenure are even less inclined to constrain current pay, even if best practices have changed.

10. WHAT OCCASIONAL INCREASES CAN DO FOR RETIREMENT

SAVINGS?: Fidelity urges people to start saving as early as possible, and if they can, increase savings each year, according to plansponsor.com. Fidelity recommends participants save 15% toward retirement, including their pre-tax deferrals and any contributions their employers make. Last year, Fidelity examined the benefit of increasing

401(k) or 403(b) savings by just 1% for people ages 25 to 55. Each age saw additional estimated monthly retirement income, especially the 25-year-old. This year Fidelity took the analysis a step further, studying three increase scenarios to demonstrate the power of establishing ongoing savings rituals when young. First, a 25-year-old earning \$40,000 who increases his deferral this year by 1% could receive additional income in retirement of \$190 per month. Fidelity recognizes that Millennials will have a lot of expenses during their working lives, such as saving for a home, paying off student debt or unexpected health care costs. With this in mind, Fidelity studied the benefit of increasing savings by 1% every five years for a total increase of 5% over 25 years. Those who adopt this pattern could receive \$690 more in monthly retirement income. The impact is even greater if a 25-year-old begins a savings ritual where they increase their deferral by 1% annually for a total of 12 increases. Under this scenario, he could receive \$1,930 per month in extra retirement income.

11. NOTE TO SELF: POSTING MY BEACH VACATION PHOTOS ON FACEBOOK DURING FMLA LEAVE MAY NOT BE SUCH A GOOD

IDEA: If you love a good social media FMLA smack down as does [fmlainsights.com](http://www.fmlainsights.com), you will enjoy it even more when the employer handles the situation in textbook fashion. The current installment offers both, while also providing a road map for employers when investigating suspected FMLA abuse. Read the story of Rodney at <http://www.fmlainsights.com/note-to-self-posting-my-beach-vacation-photos-on-facebook-during-fmla-leave-is-not-a-good-idea/>.

12. SO YOU THINK YOU KNOW EVERYTHING: Tigers have striped skin, not just striped fur.

13. TODAY IN HISTORY: In 1862, paper currency (greenbacks) introduced in U.S. by President Abraham Lincoln.

14. 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.

15. 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>.

16. REMEMBER, YOU CAN NEVER OUTLIVE YOUR DEFINED RETIREMENT BENEFIT.