



CYPEN & CYPEN
NEWSLETTER
for
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Stephen H. Cypen, Esq., Editor

Never Forget September 11, 2001
and
Always Remember May 2, 2011

1. 2016 RETIREMENT CONFIDENCE SURVEY OF THE STATE AND LOCAL GOVERNMENT WORKFORCE: The *TIAA Institute* and *Center for State and Local Government Excellence* has issued a report entitled “*2016 Retirement Confidence Survey of the State and Local Government Workforce.*” State and local governments employ a significant share of the U.S. workforce -- 14.2 million individuals at the local level and 5.1 million among the states, representing 10% and 4%, respectively, of the

U.S. workforce. Seventy-seven percent of state and local governments hired employees in 2016, which continued an upward trend from 27% in 2013 to 66 percent in 2014 to 73% in 2015. The public sector employs individuals across a broad range of occupations, and the education level of sector workers is relatively high. There are over 3 million public school teachers in the U.S., and approximately 300,000 firefighters and 700,000 police officers are employed by state and local governments. In 2016, 58% of state workers and 52% of local government employees have a bachelor's, advanced or professional degree, compared with 32% of private sector workers. A defining characteristic of public sector employment has traditionally been retirement plan coverage, usually by a defined benefit plan. Ninety-nine percent of full-time state and local government employees have access to an employment-based retirement plan; 93% have access to a DB plan. Eighty-nine percent of full-time public sector employees participate in a plan; 82% participate in a DB plan. The funding of public sector DB plans has been an issue for many states and localities since the 2001 and later 2007-2009 recessions. Among DB plans sponsored by state and local governments, the estimated aggregate ratio of assets to liabilities in fiscal year 2015 was 74% under traditional GASB rules and 72% under the new GASB 67 rules which went into effect in 2014. The Actuarially Determined Employer Contribution was estimated to be 18.6% of payrolls in 2015 and the estimated share of ADEC paid was 91%. Budgetary pressures, evolving workforce demographics and preferences, and longer-term retirement plan cost and benefit trends have led almost all state and many local governments to consider and implement various pension

reforms. The degree of change ranges from adjustments designed to improve long-term funding of existing DB plans (e.g., increases in required worker contributions, decreases in benefit accruals, reductions in cost of living adjustments, and increases in retirement ages) to more fundamental changes that would add a defined contribution plan or DC features to the primary plan structure. The latter could be done by integrating DB and DC plan elements in a hybrid arrangement. Alternatively, a DC plan could replace the DB plan as the primary plan, typically for new hires. Pension reform discussions are motivated by more than the financial condition of public sector DB plans and risk sharing between employers and employees, however. Those discussions also involve the nature of public sector employment, its employment patterns, and employee characteristics and preferences. Virtually all full-time state and local government employees are covered by some form of employment-based retirement plan, with defined benefit pensions being the primary plan for most. With that said, the role of defined contribution plans in the public sector is increasing, most often providing a supplemental savings option, but in some cases serving as the primary retirement plan or part of a hybrid arrangement. As states and localities move on from the residual effects of the 2001 and 2007-2009 recessions, they are adapting to longer-term, structural fiscal challenges. Within this setting, almost all state governments and many local governments have reformed their retirement plans in recent years, often affecting eligibility, benefit levels and sometimes the plan type. Public sector employees are concerned about the status of their employment-based plans, as well as Social Security and Medicare, and even their personal saving and

investing for retirement. As state and local governments continue to focus on pension and retiree healthcare reforms, public sector employees are likely to increase their focus on “reform” of their personal retirement planning and saving. To read the entire report visit: https://www.tiaainstitute.org/public/pdf/2016_retirement_confidence_survey.pdf.

2. FLORIDA COUNTY JUDGE STEVEN LEIFMAN SELECTED ONE OF *GOVERNING*'S PUBLIC OFFICIALS OF THE YEAR: Every year since 1994, *GOVERNING* has honored individual state and local government officials for outstanding accomplishment by naming them Public Officials of the Year. Elected, appointed and career officials from any branch of state or local government are eligible. Our readers are invited to nominate individuals who have had a notable positive impact on their department or agency, community or state. *GOVERNING* annually receives several hundred nominations from individuals in the public and private sectors. In addition, *GOVERNING* staff consults experts and scholars in the field, and also nominates outstanding individuals they encounter in the course of their work. Nominations are evaluated by a selection committee, which, after painstaking research, chooses the winners. This year *GOVERNING* chose County Judge Steven Leifman as one of 2016 Honoree, Public Officials of the Year. In 1973, Steve Leifman was a college student interning for a Florida state senator in Tallahassee. One day, the office received a letter from a constituent claiming that her son was being held at a state psychiatric hospital over the family's objections. Leifman was sent to investigate.

When he arrived at the hospital, staff showed him to the patient's room. There Leifman found the young man shackled to a bed. He was enormously overweight: Hospital staff had been injecting him with Thorazine, an antipsychotic medication that causes weight gain. Thorazine can work as a treatment for psychosis. But the young man strapped to the bed was not psychotic. He was autistic. Leifman was deeply shaken. Then a volunteer took him down to the basement to see where the truly psychotic patients were held. Eventually they reached a metal cage where a guard was hosing feces off several naked men. "It was one of those experiences that you never forget," says Leifman. "The only thing I could think of while I was standing there was, 'We treat animals better in the zoo.'" Florida eventually closed most of its state mental hospitals. But when Leifman, a former public defender, became a county court judge in 1995, he realized where most of the patients had gone -- to jails and prisons. In Miami-Dade County, which has the highest rate of mental illness in the entire nation, one-fifth of all the arrests involved people with mental problems. The Miami-Dade jail was the biggest psychiatric care facility in the state of Florida. Every few months saw incidences in which area law enforcement officers shot and killed someone who was suffering from mental illness. Leifman set out to change this. He developed a "crisis intervention training" program to teach police how to handle people with mental disease. Working with area law enforcement, mental health providers and elected leaders, he created the Criminal Mental Health Project (CMHP), which diverts the mentally ill out of the criminal justice system and into community treatment. In 2004, Leifman and his allies persuaded Miami-Dade County

voters to approve a \$21 million bond issue to convert a shuttered jail into a mental health-care facility. This year, the county and Jackson Memorial Hospital approved another \$20 million for a new state-of-the-art facility, with construction scheduled to start in 2017. In June, Governor Rick Scott signed a law that requires communities across the state to develop CMHP-style models of coordinated care. Many communities now try to keep people with mental illnesses out of the criminal justice system. What makes the Miami model distinctive, The New England Journal of Medicine noted in an article hailing Miami as a national model, is “a comprehensive, coordinated response to what’s recognized as a shared community problem.” Leifman is now working with the American Psychiatric Association Foundation, the National Association of Counties and the Council of State Governments on a new initiative, Stepping Up, which seeks to bring the Miami model to places across the country. “The most exciting part of all of this is that people are recovering; they are getting their lives back,” says the 57-year-old Leifman. “Communities are saving money and improving public safety in the process. It does not get better than that.”

3. TEN YEARS AFTER THE PENSION PROTECTION ACT: EFFECTS ON DB AND DC PLANS: *National Institute on Retirement Security* has

published a new Issue Brief entitled “*10 Years After the Pension Protection Act: Effects on DC and DC Plans.*” The Pension Protection Act of 2006 became law in 2006 with two goals regarding defined benefit pension plans: first, to promote better funding of private sector DB pension plans, and second, to help ensure the solvency of the Pension

Benefit Guarantee Corporation -- the independent government agency that insures private sector DB plans.

The PPA also made several important changes to defined contribution plans. The law clarified the use of automatic enrollment in DC plans and created several safe harbors for employers in order to encourage increased employee participation and to make it easier for employees to manage their own personal retirement accounts. Ten years after the passage of the PPA, the brief analyzes the trends in both DB and DC retirement plans, in order to assess what effects the legislation may have had on these plans. NIRS found that:

- For DB pension plans, an unintended consequence has emerged, in that employers are less and less willing to sponsor these plans and more employers have frozen existing plans.
- Fewer and fewer employees are covered by traditional DB plans, the culmination of a decades-long trend that was accelerated by the PPA's increased funding requirements. The PPA moved to a market basis for funding, which increased both the plans' annual cost and cost volatility.
- Congress has implemented several "stop gap" measures to address pension cost and volatility, but this temporary relief has not been enough to change the behavior of employers, who continue to freeze and terminate their plans.
- DC plans with automatic enrollment have seen some increased participation, but the overall changes are not enough to ensure

adequate retirement security for most workers. Contribution rates are far too low, and perhaps even lower than they would be without auto-enrollment.

- The share of working age households covered by any retirement plan fell from the high mark of 57.6 percent in 2001 to 51.3 percent in 2013.
- Contribution rates tend to be low -- by design -- and perhaps even lower than they would be without auto-enrollment. Even participants who increase their rates over time through auto-escalation features often do not end up saving enough to ensure an adequate retirement income.

Thus, even with the “improved” automatic features of DC plans promoted by the PPA, DB pension plans still offer the best path to retirement security. It is unfortunate that the PPA had the unintended consequence of causing more and more DB plans to freeze or shutter. One solution would be to permanently ease the funding requirements -- rather than continuing with the stop-gap measures that Congress has passed several times since the PPA -- to ensure DB plan sponsors more predictability and less volatility in their funding requirements.

4. STATE PENSION FUND PAID PRIVATE EQUITY FIRMS \$1.5B

OVER FIVE YEARS: The Massachusetts state pension fund paid \$1.5 billion to more than 100 private equity firms over the past five years -- including a \$1 billion share of its profits -- according to data it publicly disclosed for the first time according to the bostonglobe.com. In

exchange for the generous compensation, the pension fund reaped bigger gains from private equity than from any other investment it made: 16.2% annualized returns from 2011 through 2015. That added up to \$4.7 billion for retirees and taxpayers. The five-year net gains dwarfed those in stock index funds, bonds, or hedge funds. The next-closest category was real estate, at 12.6% before subtracting fees, according to a year-end 2015 report by the state's Pension Reserves Investment Management board. Private equity -- the business of buying and reselling companies -- has by far been the best-performing asset class for the \$62 billion pension portfolio over three, five, and 10 years. The disclosure, made in response to a records request by the *Globe*, comes at a time when public pension funds and endowments around the country are under pressure to reduce the fees and profit shares, known as carried interest, they are paying on investments. Michael Trotsky, executive director and chief investment officer of the pension fund, in a memo to the PRIM board about the private equity fees, said he was pleased with the results, but "we continue to work to reduce management fees paid to, and carried interest allocations retained by, our private equity managers." The nation's largest public pension fund, the California Public Employees' Retirement System, a year ago disclosed for the first time that it had paid \$3.4 billion in profit-sharing to private equity firms since 1990, while logging \$24.2 billion in profits. In fiscal year 2015, CalPERS, which invests 9% of its roughly \$300 billion in assets in private equity, paid its private equity managers nearly \$432 million in fees, while posting a return of 8.9%. The Massachusetts fund in 2015 paid \$98 million in management fees to private equity firms such as Boston's Bain Capital

and Thomas H. Lee Partners, according to PRIM. It shared \$197 million in profits, after subtracting fees, while producing a net return of 14.8% -- slightly lower than the five-year average. Unlike CalPERS, Massachusetts' PRIM did not disclose the fees or profit-sharing paid to specific investment firms. Historically, private equity firms have demanded secrecy from investors like the state pension system, as a condition of entry to their funds. Massachusetts law exempts the pension fund from having to respond to certain public information requests, including requests to divulge fees charged by investment managers. Private equity firms typically have charged a 2% annual fee on a pension fund's money, or \$2 on every \$100 invested. The firms invest money in various companies over a few years, and it generally takes five to eight for returns to come to fruition. On top of that, the firms get to keep 20% of any profits they earn for clients, or \$1 out of every \$5. Firms like Bain in the past have commanded even larger sums. But that is changing, both due to pressure from large institutional investors and as private equity enters a cooler period following a hot decade. The demand for lower fees and greater transparency "has been years in the making," said Cesar Estrada, a senior managing director at State Street Corp. and head of private equity services. He said his team is increasingly responding to requests from firms and their clients for more detailed breakdowns of fees and profit-sharing. "Investors are becoming more knowledgeable," he said. CalPERS in its latest report said it shared just 14% of its profits with its private equity managers for the year ended June 30. Massachusetts, by contrast, paid close to the standard 20% to about 120 firms over five years, according to its disclosure. PRIM in 2015 had \$6.8

billion, or about 10% of its total assets, invested in private equity. Trotsky said the fund is working to negotiate “preferential terms” in private equity, such as lower management fees and lower levels of profit-sharing. In addition, the fund is looking to establish a co-investment program, where it could put additional sums into deals with its private equity managers, without paying any fees on those transactions. Hedge funds also use the so-called two-and-20 rule, with a 2% fee paid yearly on the assets invested and 20% of the profits reserved for the manager. The state pension fund said it is saving \$100 million annually since launching the effort.

5. RISING DISCOUNT RATES GIVE CORPORATE PENSION PLANS BIGGEST BUMP IN 12 MONTHS: U.S. corporate pension plans' funded status rose about 3 percentage points in November, driven by falling liabilities, said reports from Wilshire Consulting and Legal & General Investment Management America. According to Wilshire, the aggregate funding ratio for S&P 500 companies with corporate pension plans rose 3.3 percentage points over the month to 80.6% due to a 5.2% drop in liability values, offsetting a 1.2% decrease in asset values. Despite positive U.S. equity returns, asset values fell due to negative returns for most other asset classes during the month. The fall in asset values was more than offset by the fall in liability values resulting from the nearly 40 basis point rise in long corporate bond yields during the month. This is the fifth consecutive month of either flat or rising funded ratios, and this month's increase is the largest in the past 12 months,” said Ned McGuire, vice president and a member of the pension risk solutions

group of Wilshire Consulting. “The post-election, Trump-bounce in corporate funding ratios was driven by a more than 4.5% increase in the Wilshire 5000 Total Market index (for U.S. equities) during the month and rising corporate bond yields, which pushed liability values lower for the fourth consecutive month.” According to LGIMA's monthly Pension Fiscal Fitness Monitor, the funded status of a typical U.S. corporate pension plan with a 60% allocation to global equity and 40% to core fixed income rose 3.4 percentage points to 80.9% in November. Liabilities for the average plan declined 4.6%, due to a 37-basis-point increase in the discount rate. Assets dropped 0.5% over the month.

6. IN MIAMI-DADE, FLORIDA A WOMAN EARNS 87 CENTS FOR EVERY DOLLAR A MAN MAKES:

According to a piece from the miamiherald.com, women consistently earn less than men do in Miami-Dade, with a new study showing wide gaps in a range of occupations, including high-earning positions in architecture, law and management posts in county government itself. In 2014, full-time female workers in Miami-Dade earned 87% of what full-time male workers made, according to the county-funded report by Florida International University. In the local legal field, men earn double what women do, the largest gap among Miami-Dade’s best-paying occupations. In Miami-Dade government itself, the second-largest employer next to the school system, men tend to achieve more financial success as they climb the career ladder. Female supervisors earn an average of about \$73,000, compared to just under \$83,000 for male supervisors -- a 13% gap. “These are structural barriers that exist not only in Miami-Dade County, but throughout the country and

the world,” Miami-Dade Commissioner Daniella Levine Cava, who sponsored the legislation funding the study. “We know, for example, that women often start at lower salaries and then they never catch up.” Titled “The Status of Women in Miami-Dade County,” the \$14,000 report by FIU’s Metropolitan Center lays out the local dimensions of a longstanding, national divide across the country. Nationally, women earn just 79 cents for every dollar made by a man, meaning Miami-Dade’s gender gap is considerably narrower. Researchers point to a string of factors behind the pay gap, including women being more likely to take part-time work and leaving the workforce during childbirth and early years of raising children. But academics also see structural discrimination in many of the elements, including the idea men are exempt from career sacrifices tied to child-raising and discrimination in wages for occupations that tend to employ more women than men. Maria Ilcheva, the FIU researcher who led the study, pointed out there was only one major sector in Miami-Dade where women earn more than men. That is construction, a finding that Ilcheva said surprised her research staff. But with women making up just 7% of Miami-Dade’s construction employees, the pool of earners is small enough to skew the numbers. In sectors where women make up the majority of employees, men still come out ahead on payday. Women make up 53% of employees in Miami-Dade’s finance industry. But the typical man in finance earns \$44,000, compared to \$37,000 for the typical woman, according to the study. Women dominate the industry category that includes both healthcare and education, making up 73% of that workforce. The typical Miami-Dade man in that industry earns \$41,000, and the typical woman

\$30,000. Even in the 10 highest-paid occupations for women in Miami-Dade, men earn more in each category: 40% more in health diagnostics, 34% more in architecture and engineering, and 114% more in legal. Ilcheva said the gender gap also applies when it comes to who owns a Miami-Dade business. Firms owned by men tend to have more employees and more sales than do firms owned by women. She said that suggests help for women-owned businesses could pay dividends for the wage gap. "There is a lot opportunity there," she said. "The majority of employment in Miami-Dade, and across the country, is in small businesses." The report shows women making quicker gains than men on a number of economic fronts in Miami-Dade. The number of women-owned firms in the county grew by 61% between 2007 and 2012, to 187,379. For men-owned firms, growth was 11% to 239,190. Between 2005 and 2014, women in Miami-Dade saw their earnings grow by 18%, compared to 3% for men. FIU's report included an analysis of Miami-Dade's 28,000-person payroll, and found a significant gender gap in paychecks. Men make up 59% of county workers, and tend to make 14% more than female workers. Only 8% of the county's male employee's work in jobs classified as clerical, compared to nearly a third of the county's female employees. The average male supervisor in county government earns \$83,000, compared to \$73,000 for the average female supervisor, according to payroll data from 2016. Women do earn more in some smaller management categories: they make four percent more as assistant division directors and about 1% more as deputy directors. And the best-paid employee in county government is female: County Attorney Abigail Price-Williams earned about \$343,000 in 2015. Ilcheva said the

county payroll data lacks educational information, making it impossible to link gender as the lone factor behind compensation differences. She said that while the study points out detailed differences in county pay among men and women, the results should not be read as revealing gender discrimination. “We are kind of dancing around the issue,” she said. “The finding is there is a gap.”

7. BIG PICTURE VIEW OF DB PLAN INVESTMENTS NEEDED IN

2017: Examining the adequacy of the governance structure, including critical resources and fiduciary risk, should be the first order of business for defined benefit plans entering 2017, as reported by bna.com. In an increasingly complex investment world, “complacency is not an option.” “Governance is about assessing the approach to the oversight of the plan, including the dedication of resources, the frequency of meetings, and the definition of roles and responsibilities; both internally and externally, said an investment leader for Willis Towers Watson. Investments typically are overseen by an investment committee, a number of questions should be asked in evaluating whether the committee as currently comprised and operated is consistent with the goals for the plan. The questions should include:

- whether the committee members have the right skills sets internally to make fully informed investment decisions;
- whether they understand the complexities of pension plan management;
- how often the committee meets and how much decision-making

authority it has; and

- where the committee should seek outside assistance to bridge gaps.

Smart portfolio management includes finding ways to improve the plan's risk and return profile. A diversified portfolio may hedge interest rate risk, while seeking to generate a balanced return profile. As interest rates increase, they reduce plan liabilities, potentially causing plan funding ratios to improve, while a decrease in interest rates has the opposite impact. Interest rates are a key risk driver that the plan must manage and investors should be very thoughtful in managing this risk, even if they believe that rates are going up. Defined benefit plans should also look for ways to keep their costs low through improved implementation. Fees can potentially be saved via renegotiation with managers, by using smart beta approaches in areas where active management has become more limited and expensive, and by streamlining the investment program's operational and administrative aspects. Every dollar saved through improved efficiency is one less required from contributions or portfolio returns. Ways to keep costs low include through economies of scale that the plan sponsor may be able to achieve or access because of its size and partnerships to get preferential fee arrangements from investment managers. Defined benefit plans should consider all these changes in the context of what is likely to continue to be a low-return environment. Willis Towers Watson believes that the market will offer low returns over the intermediate to long term, and are concerned that valuations in U.S. and foreign stock markets are above average and

higher than warranted based on global growth expectations and amount of central bank debt.

8. INTEREST RATES REMAIN THE SAME FOR THE FIRST

QUARTER OF 2017: The Internal Revenue Service has announced that interest rates will remain the same for the calendar quarter beginning January 1, 2017. The rates will be:

- 4% for overpayments (3% in the case of a corporation);
- 1.5% for the portion of a corporate overpayment exceeding \$10,000;
- 4% percent for underpayments; and
- 6% percent for large corporate underpayments.

Under the Internal Revenue Code, the rate of interest is determined on a quarterly basis. For taxpayers other than corporations, the overpayment and underpayment rate is the federal short-term rate plus 3 percentage points. Generally, in the case of a corporation, the underpayment rate is the federal short-term rate plus 3 percentage points and the overpayment rate is the federal short-term rate plus 2 percentage points. The rate for large corporate underpayments is the federal short-term rate plus 5 percentage points. The rate on the portion of a corporate overpayment of tax exceeding \$10,000 for a taxable period is the federal short-term rate plus one-half (0.5) of a percentage point. The interest rates just announced are computed from the federal short-term rate determined during October 2016 to take effect November 1, 2016, based on daily compounding. IR-2016-159 (December 5, 2016).

9. FLORIDA MAN KEPT COLLECTING DEAD BROTHER'S PENSION CHECKS FOR 7 YEARS:

A Florida man was sentenced to six months in jail and five years' probation on Friday after authorities said he had been collecting his dead brother's pension checks for seven years. Martin Petschauer died on July 9, 2008 in Queens, New York, but his brother, Robert, 71, kept collecting his pension checks for \$180,000, as reported by palmbeachpost.com. Robert, who lives in Florida, kept collecting the checks until October 2015 when officials learned that Martin, who worked as an auditor in New York, had died years ago. Officials said Robert phoned the state pension call center and posed as his brother, saying "I am alive and I want my pension." "A very astute woman with the pension system called back and asked to speak with Martin Petschauer and gets this guy who says, 'I am his brother. He is not home right now,'" said Deputy Comptroller of Investigations Nelson Sheingold. "Obviously, we had done some research and we had the actual obituary. When that was raised, the call ended very abruptly." Robert was brought to New York where he was recently sentenced and signed a judgement to have the \$180,000 sent to the state.

10. FUN WITH WORDS: When she saw her first strands of grey hair she thought she would dye.

11. PARAPROSDOKIAN: Ever stop to think and forget to start again?

12. TODAY IN HISTORY: In 1902, Oliver Wendell Holmes Jr. became

Associate Justice on Supreme Court.

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.

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