



**CYPEN & CYPEN**  
**NEWSLETTER**  
**for**  
**NOVEMBER 17, 2016**

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Never Forget September 11, 2001

and

Always Remember May 2, 2011

**1. CORPORATE PENSION FUNDED STATUS IMPROVED BY \$28 BILLION IN OCTOBER:** The funded status of the 100 largest corporate defined benefit pension plans improved by \$28 billion during October as measured by the Milliman 100 Pension Funding Index. October's funded status boost was the largest of 2016. The deficit fell

to \$410 billion due to interest rate gains experienced during October. As of October 31, the funded ratio increased to 77.3%, up from 76.3% at the end of September. The market value of assets declined by \$17 billion as a result of October's investment loss of 0.84%. The Milliman 100 PFI asset value decreased to \$1.393 trillion at the end of October from \$1.410 trillion at the end of September. By comparison, the 2016 Milliman Pension Funding Study reported that the monthly median expected investment return during 2015 was 0.58% (7.2% annualized). The projected benefit obligation, or pension liabilities, decreased to \$1.803 trillion at the end of October from \$1.848 trillion at the end of September. The change resulted from an increase of 19 basis points in the monthly discount rate to 3.61% for October, from 3.42% for September. Discount rates had reached a record low in August and have climbed 29 basis points since then to help boost funded status. Over the last 12 months (November 2015 – October 2016), the cumulative asset return for these pensions has been 4.44% and the Milliman 100 PFI funded status deficit has deteriorated by \$116 billion. The rise in the funded status deficit over the past 12 months is due to a combination of decreases in discount rates, on the order of 55 basis points, and lower-than-expected investment returns. The funded ratio of the Milliman 100 companies has decreased over the past 12 months to 77.3% from 82.7%. Getting back above the 80% funded level before the end of the year remains a significant hurdle for the Milliman 100 plans in aggregate as the funded status deficit has risen by \$103 billion so far in 2016.

**2. ARIZONA LAW THAT CHANGED FORMULA, CALCULATED FUTURE BENEFIT INCREASES FOR RETIRED PLAN MEMBERS AND INCREASED AMOUNT EMPLOYEE PLAN MEMBERS CONTRIBUTED TOWARD PENSIONS VIOLATES CONSTITUTIONAL PROVISION AGAINST DIMINISHMENT OR IMPAIRMENT:**

In 2011 Arizona enacted changes to the Elected Officials' Retirement Plan. The law changed the formula for calculating future benefit increases for retired plan members and increased the amount that employed plan members must contribute toward their pensions. Retired members of the plan challenged the provision changing the formula for calculating future benefit increases. They argued that the change violated the Pension Clause of the Arizona Constitution, which provides that public system retirement benefits shall not be diminished or impaired. In a prior decision in 2014, the Supreme Court of Arizona agreed that the provision is unconstitutional as applied to retired members. Employed members in the plan also challenged the bill. First, they argued that the unilateral changes to the benefit increases formula and to the amount they were required to contribute toward their pensions violated the Pension Clause based upon the earlier case. Second, relying upon a long-standing decision, they argued that because their pensions were part of employment contracts that vested when they began employment, the Legislature could not unilaterally change the terms of their pensions to their detriment. The trial court granted the employed members summary judgment, invalidating the provisions at issue. The court denied the members' request for attorneys' fees and

prejudgment interest, however. The court also denied the members' request to have the judgment run against the state, which had intervened in the case. On appeal by the state/plan and cross-appeal by the members, the Arizona Supreme Court affirmed and granted summary judgment to the employed plan members. And, based upon the 2014 decision, held the change to the benefit increase formula violated the Pension Clause because it "diminished and impaired" the employed members pension benefits. The law changes to the benefit increases formula and the contribution rate also violated its long-standing decision because the Legislature cannot unilaterally change terms of members' pension contracts once their rights to those terms have vested at the beginning of the members' employment. Contrary to the trial court's ruling, however, the Supreme Court held that the employed members were entitled to attorneys' fees, and prejudgment interest, and the judgment must run against the state as well as the plan. *Hall v. Elected Officials Retirement Plan*, No. CV-15-0180 (Ariz. November 20, 2016). Some observers believe the state will be required to refund as much as \$220 million to members. See: <http://www.azcentral.com/story/news/local/arizona-investigations/2016/11/14/arizona-supreme-court-ruling-public-safety-pension-trust-refunds/93805222/?from=global&sessionKey=&autologin>.

**3. TREASURY DENIES TEAMSTERS LOCAL 469 BID TO REDUCE PENSION BENEFITS:** Teamsters Local 469 Pension Plan, Hazlet, New Jersey, has been denied its Treasury Department application to

reduce benefits for participants, including retirees according to pionline.com. The pension fund had applied March 30 under the Multiemployer Pension Reform Act of 2014, which allows trustees to reduce benefits of deeply underfunded pension plans that would be insolvent within 15 years of when the application is approved, after they have tried all other means. The application proposed to begin the benefit cuts, known as suspensions, on January 1, 2017. In a recent letter to the board of trustees, Kenneth Feinberg, Treasury's special master overseeing the MPRA application process, said the pension fund's assumptions about investment returns and spousal survival benefit takeup "are not reasonable," thereby failing the law's key test that benefit cuts be reasonably estimated to avoid insolvency. The pension fund assumed an annual investment return of 7.25% for the entire 45 years projected in the application to achieve solvency. Mr. Feinberg said those assumptions were not reasonable because they did not use appropriate investment forecast data, were overly optimistic, and inappropriate given a negative cash flow and other factors. Teamsters Local 469 Pension Plan has 1,781 total participants, 128 of them active, assets of \$122.6 million and liabilities of \$279.9 million for a funded status of 43.8% as of December 31, 2014, according to its Form 5500 filing. With significantly more inactive participants than active, it is likely to require financial assistance from the PBGC by 2029. The plan has been in critical status for eight years and is projected to become insolvent within the next 19 years. In 2015, Teamsters' Central States Pension Fund filed a similar request, ([see C & C Newsletter for May 26, 2016, Item 4.](#))

#### **4. ERA OF LOW INTEREST RATES HAMMERS MILLIONS OF PENSIONS AROUND WORLD:**

Central bankers lowered interest rates to near zero or below to try to revive their gasping economies. In the process, though, they have put in jeopardy the pensions of more than 100 million government workers and retirees around the globe according to the *Wall Street Journal*. In Costa Mesa, California, Mayor Stephen Mensinger is worried retirement payments will soon eat up all the city's cash. In Amsterdam, language teacher Frans van Leeuwen is angry his pension now will be less than what his father received, despite 30 years of contributions. In Tokyo, ex-government worker Tadakazu Kobayashi no longer has enough income from pension checks to buy new clothes. Managers handling trillions of dollars in government-run pension funds never expected rates to stay this low for so long. Now, the world is starved for the safe, profitable bonds that pension funds have long needed to survive. That has pulled down investment returns and made it difficult for funds to meet mounting obligations to workers and retirees who are drawing government pensions. As low interest rates suppress investment gains in the pension plans, it generally means one thing: standards of living for workers and retirees are decreasing, not increasing. "Unless ordinary people have money in their pockets, they do not spend," the 70-year-old Mr. Kobayashi said during a recent protest of benefit cuts in downtown Tokyo. "Higher interest rates would mean there would be more money at our disposal, even if slightly." The low rates exacerbate cash problems already bedeviling the world's pension

funds. Decades of underfunding, benefit overpromises, government austerity measures and two recessions have left many retirement systems with deep funding holes. A wave of retirees world-wide is leaving fewer active workers left to contribute. The 60-and-older demographic is expected to roughly double between now and 2050, according to the United Nations. Government-bond yields have risen since Donald Trump was elected U.S. president, though few investors expect a prolonged climb. Regardless, the ultralow bond yields of recent years have already hindered the most straightforward way for retirement funds to recover -- through investment gains. Pension officials and government leaders are left with vexing choices. As investors, they have to stash away more than they did before or pile into riskier bets in hedge funds, private equity or commodities. Countries, states and cities must decide whether to reduce benefits for existing workers, cut back public services or raise taxes to pay for the bulging obligations. Pension funds around the world pay benefits through a combination of investment gains and contributions from employers and workers. To ensure enough is saved, plans adopt long-term annual return assumptions to project how much of their costs will be paid from earnings. They range from as low as a government bond yield in much of Europe and Asia to 8% or more in the U.S. The problem is that investment-grade bonds that once churned out 7.5% a year are now barely yielding anything. Global pensions on average have roughly 30% of their money in bonds. Low rates helped pull down assets of the world's 300 largest pension funds by \$530 billion in 2015, the first decline since the financial crisis,

according to a recent Pensions & Investments and Willis Towers Watson report. Funding gaps for the two biggest funds in Europe and the U.S. have ballooned by \$300 billion since 2008, according to a *Wall Street Journal* analysis. Few parts of Europe are feeling the pension pain more acutely than the Netherlands, home to 17 million people and part of the eurozone, which introduced negative rates in 2014. Unlike countries such as France and Italy, where pensions are an annual budget item, the Netherlands has several large plans that stockpile assets and invest them. The goal is for profits to grow faster than retiree obligations, allowing the pension to become financially self-sufficient and shrink as an expense to lawmakers. ABP currently holds 90.7 cents for every euro of obligations, a ratio that would be welcome in other corners of the world. But Dutch regulators demand pension assets exceed liabilities, meaning more cash is required than actually needed. Japan is wrestling with the same question of generational inequality. Roughly one-quarter of its 127 million residents are now old enough to collect a pension. More than one-third will be by 2035. The demographic shift means contributions from active workers are not sufficient to cover obligations to retirees. The government has tried to alleviate that pressure. It decided to gradually increase the minimum age to collect a pension to 65, to require greater contributions from workers and employers and to reduce payouts to retirees. A typical Japanese couple who are both 65 would collect today a monthly pension of ¥218,000 (\$2,048). If they live to their early 90s, those payouts, adjusted for inflation, would drop 12% to ¥192,000. The Japanese government has turned to its \$1.3 trillion

Government Pension Investment Fund for cash injections six of the past seven years. That fund, the largest of its kind in the world, manages reserves for Japan's public-pension system and seeks to earn returns that outpace inflation. The more it earns, the more it can shore up the government's pension system. In February, Japanese central bankers adopted negative interest rates for the first time on some excess reserves held at the central bank so commercial banks would boost lending. The pension-investment fund raised a political ruckus in August when it said it lost about ¥5.2 trillion (\$49 billion) in the space of three months, the result of a foray into volatile global assets as it tried to escape low rates at home. The fund's target holdings of low-yielding Japanese bonds were cut to 35% of assets, from 60% two years ago, and it has added heaps of foreign and domestic stocks. It is now considering investing more in private equity. The government-mandated target is a 1.7% return above wage growth. The fund posted a loss of 3.8% for the year ended in March because of the yen's surge and global economic uncertainty. It was its worst performance since the 2008 global financial crisis. In the U.S., the country's largest public-pension plan is struggling with the same bleak outlook. The California Public Employees' Retirement System, which handles benefits for 1.8 million members, recently posted a 0.6% return for its 2016 fiscal year, its worst annual result since the financial crisis. Its investment consultant recently estimated that annual returns will be closer to 6% over the next decade, shy of its 7.5% annual target. CalPERS investment chief's strategy for the era of lower returns is to reduce costs and the complexity in the fund's

\$300 billion portfolio. He and the board decided to pull out of hedge funds, shop major chunks of CalPERS' real-estate and forestry portfolios and halve the number of external money managers by 2020. Yet the Sacramento-based plan still has just 68% of the money needed to meet future retirement obligations. That means cash-strapped cities and counties that make annual payments to CalPERS could be forced to pay more. That is a concern even for cities such as affluent Costa Mesa in Orange County, which has a strong tax base from rising home prices and a bustling, upscale shopping center. The city has outsourced government services such as park maintenance, street sweeping and the jail, as a way to absorb higher payments to CalPERS. Pension payments currently consume about \$20 million of the \$100 million annual budget, but are expected to rise to \$40 million in five years. The outsourcing and other moves eliminated one-quarter of the city's workers. The cost of benefits for those remaining will surge to 81 cents of every salary dollar by 2023, from 37 cents in 2013, according to city officials. The mayor, is hopeful for a state solution involving new taxes or a benefits overhaul, either from lawmakers in Sacramento or from a California ballot initiative for 2018 that would cap the amount cities pay toward pension benefits for new workers. Weaker cities across California could face bankruptcy without help, said former San Jose Mayor Chuck Reed, who oversaw a pension overhaul there in 2012 and is backing the 2018 initiative that would shift onto workers any extra cost above the capped levels. "Something is broken," he said. "The plans are all based on assumptions that have been overly optimistic." Costa Mesa ended the

latest fiscal year with an \$11 million surplus, its largest ever. But that will soon disappear, as pension costs swallow up \$2 of every \$5 spent by the city.

#### **5. MANDATORY ARBITRATION FOR ARMED SERVICE HIRES IS**

**UPHELD:** The Ninth Circuit Court of Appeals, joining three other circuit courts, has recently ruled that the Uniformed Services Employment and Reemployment Rights Act does not prohibit the compelled arbitration of claims made under the Act. Passed in 1994, USERRA protects active and reserve military personnel with regard to civilian employment before or after their active service. The Ninth Circuit's ruling helps solidify the right of employers to compel arbitration of USERRA claims under a valid arbitration agreement, particularly in light of the Circuit's perceived hostility towards arbitration of employment-related claims, according to [todaysgeneralcounsel.com](http://todaysgeneralcounsel.com). The ruling, provides further support for the view that a properly drafted arbitration agreement provides employers with the ability to arbitrate USERRA claims and avoid litigation.

#### **6. DOES PUBLIC PENSION FUNDING AFFECT WHERE PEOPLE**

**MOVE?:** *Center for Retirement Research at Boston College* has issued a new research brief entitled "*Does Public Pension Funding Affect Where People Move?*" In prior briefs, the Center has focused on the impact of pensions on state and local finances, including their influence on total budgets, borrowing costs, and the fiscal health of

troubled jurisdictions. Overall, this research found that pensions play only a modest role. However, one other way that pensions may impact public finances is through where individuals choose to live. Past research has found that individuals are more likely to move to places with the best “bundle” of amenities and opportunities. Influential factors may include house prices and jobs, as well as government finances, such as taxes and debt. More recently, unfunded pension liabilities have raised concerns about jurisdictions’ ability to manage their finances, as an increasing portion of today’s taxes must be used to cover past shortfalls and future taxes may end up being higher as well. The brief explores the role that unfunded pension liabilities play in migration from state to state. Policymakers care about migration, because it is linked to economic consequences. For example, when many people leave a state, the loss of income tax revenue and consumer spending can hurt the state’s economy. Therefore, understanding the underlying forces that contribute to migration patterns is important. The discussion proceeds as follows. The first section describes broad migration patterns. The second section summarizes the data used for the analysis. The third section explains the methodology for analyzing how state differences in unfunded pension liabilities relate to interstate migration patterns. The fourth section presents the findings. The final section concludes that while economic factors and the distance between locations are the primary drivers of migration, a state’s pension funding also plays a role, albeit small. To read the entire research brief visit:

[http://crr.bc.edu/wp-content/uploads/2016/10/slp\\_52.pdf](http://crr.bc.edu/wp-content/uploads/2016/10/slp_52.pdf). Number 52,

(October 2016).

**7. RETIREMENT MONEY FOR EX-PRESIDENTS:** In his Pulitzer-Prize winning biography of the 33rd President of the United States Harry Truman, author David McCullough wrote that upon his retirement, Truman left the White House unprotected by the Secret Service and with no support from the federal government besides an army pension of \$112,560. He and his wife Bess had put aside part of his \$100,000 a year salary in government bonds, but McCullough said it was in all probability a modest amount. Truman was known to have taken out a loan in his last weeks as president. He had numerous opportunities to leverage his position as a former president, but unlike those who followed him, he refused them all and said, "I could never lend myself to any transaction, however respectable, that would commercialize on the prestige and dignity of the office of the presidency." The financial difficulties Truman faced prompted the passage of the Former President's Act in 1958. The Act authorized the General Services Administration to provide former presidents with a pension, support staff, office space, and travel funds. They also receive a lifetime of Secret Service protection and their children remain protected until they are 16 years old. The pension for former presidents matches the annual pay for senior political officials of the Executive Level 1 ranking. In 2016, this figure was \$205,700. Widows of ex-presidents are entitled to \$20,000 a year. Last year, the federal government spent a total of \$3.25 million on the four former presidents still living. According to a recent report by the

Congressional Research Service, George W. Bush alone accounted for \$1 million of this. (Nancy Reagan, spouse of President Ronald Reagan who died in March 2016, waived her pension and only availed of franking or mailing privileges.) Pensions were the second highest category of federal benefits to former presidents in 2015, with the first being "office space." A total of \$1.18 million was spent on office spaces. George W. Bush received the highest amount at \$434,000, closely followed by Bill Clinton's request for \$429,000. George H. W. Bush received \$207,000 and Jimmy Carter received \$112,000. The White House 2017 budget requested an addition of \$588,000 to the GSA's allocation for former presidents. President Obama will leave office on January 20, 2017 and become eligible for the benefits and pension. So do former presidents need all of this? According to Politico, George W Bush gave 200 paid speeches from 2009 to 2015 and charged between \$100,000 and \$175,000 for each. CNN reported that the Clintons raked in more than \$150 million for paid speeches from 2001 to early 2015. A recent investigation by Politico showed that Bill Clinton, who has said he became richer post-presidency, used the federal funds to supplement the salaries of Clinton Foundation staffers and provide them with federal government benefits. The Former President's Act was enacted to "maintain the dignity" of the Office of the President, but since it appears to be supplementing the much larger incomes of some Presidents, there was recently a bipartisan push to curb the load on taxpayers. In July, however, President Obama vetoed a bill passed in the House and Senate that looked to cap the annual monetary allowance of former

presidents at \$200,000. The bill also looked to increase the pension of surviving spouses from \$20,000 to \$100,000. The White House released a statement saying, "This bill as written would immediately terminate salaries and all benefits to staffers carrying out the official duties of former Presidents -- leaving no time or mechanism for them to transition to another payroll. As written, this bill would also impair Secret Service's ability to protect former Presidents by ending GSA's role in managing operations, equipment and office space." In 2015, the median pension and annuities received by former employees at private companies was \$9,376. Former federal government employees received \$22,669 according to Investopedia.com.

#### **8. IRS ADVISORY COUNCIL RELEASES ITS 2016 ANNUAL**

**REPORT:** The Internal Revenue Service Advisory Council has released its annual report for 2016 to IRS Commissioner John Koskinen. The report includes recommendations on a wide range of tax administration issues. "IRSAC members play an important role in tax administration by providing insights from outside the agency on the most pressing tax issues of the day," said Koskinen. "They volunteer their time and energy for the benefit of all taxpayers." The IRSAC is an advisory group to the entire agency. The IRSAC's primary purpose is to provide an organized public forum for the Commissioner, senior IRS executives and representatives of the public to discuss relevant tax administration issues. Advisory council members convey the public's perception of professional standards and best practices for tax professionals and IRS activities, offer

constructive observations regarding current or proposed IRS policies, programs and procedures, as well as suggest improvements to IRS operations. Based on its report findings and discussions over the last year, the IRSAC made several recommendations on a broad range of issues and concerns including:

- Evaluating the Effects of Penalties on Voluntary Compliance;
- Promoting Confidentiality of Treaty-Exchanged Information;
- Improving Fraud Prevention through Individual Taxpayer and Business Master File Authentication;
- Enhancing the IRS2Go Mobile Application and Online Accounts;
- Revising and Updating Circular 230.

The IRSAC is administered by the Office of National Public Liaison and draws its members from the taxpaying public, the tax professional community, small and large businesses and the payroll community. The 2016 Internal Revenue Service Advisory Council Public Report can be found at: <https://www.irs.gov/pub/irs-utl/2016irsacfinalreport.pdf>. IR-2016-149 (November 16, 2016).

**9. FUN WITH WORDS:** The guy who fell onto an upholstery machine is now fully recovered.

**10. PARAPROSDOKIAN:** Behind every great man is a woman rolling her eyes.

**11. TODAY IN HISTORY:** In 1913, Panama Canal opens.

**12. 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.

**13. 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>.

**14. REMEMBER, YOU CAN NEVER OUTLIVE YOUR DEFINED RETIREMENT BENEFIT.**