



CYPEN & CYPEN
NEWSLETTER
for
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Never Forget September 11, 2001
and
Always Remember May 2, 2011

1. CORPORATE PENSION FUNDING STARTS 2017 ON THE RIGHT FOOT: Pionline.com reports the funded status of the largest U.S. corporate pension plans remained the same or rose slightly in January, per reports from Mercer, Wilshire Consulting and Legal & General Investment Management America. According to Mercer, the

estimated aggregate funding ratio of defined benefit plans sponsored by S&P 1500 companies was approximately 82% at the end of January, unchanged from the end of 2016. The estimated aggregate value of pension fund assets of S&P 1500 companies totaled \$1.81 trillion as of January 31, unchanged from December 31, while estimated aggregate liabilities totaled \$2.21 trillion, unchanged from the end of December, according to Mercer. The S&P 500 index and MSCI EAFE index returned 1.8% and 2.9%, respectively, in January, while the typical discount rates remained level at 4.04%. According to Wilshire, the aggregate funding ratio for S&P 500 companies with corporate pension plans was 83.2% as of January 31, up 1.2 percentage points from December 31. Asset values rose 1.2% in January, outpacing a 0.3% decrease in liability values, according to Wilshire. Positive returns for most asset classes drove the asset increase, while rising corporate bond yields drove the liability decline. According to LGIMA's 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 1.3 percentage points in January to an estimated 82.6%. Assets rose 1.7% over the month on the back of global equity returns of 2.8%. Despite a two-basis-point increase in the discount rate, liabilities for the traditional plan were up 0.1%. Separately, in a quarterly report, Milliman found that the funded status of the 100 largest U.S. corporate pension plans fell 1 percentage point in the fourth quarter to 70.1% as of December 31. Assets fell 0.46% over the quarter to \$3.267 trillion as benefits paid out exceeded contributions. Investments returned an aggregate

0.45% in the fourth quarter. Meanwhile, liabilities rose 0.84% over the three months ended December 31 to an estimated \$4.659 trillion.

2. CALSTRS TO CUT ASSUMED RATE OF RETURN TO 7%:

CalSTRS has approved lowering the pension fund's assumed rate of return to 7% from 7.5% over the next two years because of diminished capital market and inflation forecasts in a report from pionline.com. Milliman, the board's actuarial consultant, had recommended a reduction to 7.25%, but also offered the board the option of a 7% rate of return. The plan approved by the board of the \$196.4 billion California State Teachers' Retirement System would lower the rate of return to 7.25% as of July 1, and 7% as of July 1, 2018. The vote for the more aggressive reduction came at a meeting in San Diego after a report from one of CalSTRS' investment consultants, Pension Consulting Alliance, that the pension fund had a less than 50% chance of meeting the 7.25% rate of return long term. The vote also changes CalSTRS' long-term inflation assumption to 2.75% from 3%. A Milliman report had noted that over the past 20 years, "actual price inflation has been lower and is expected to remain below 3% in the future." Public pension plans across the U.S. have been lowering their assumed rates of return in light of less-than-rosy future capital market assumptions. In December, the \$306.6 billion California Public Employees' Retirement System, Sacramento, approved lowering its rate to 7% from 7.5% in stages over the next three fiscal years beginning in July. Lowering the rate of return sets CalSTRS on a course for a funding level dip to 64% from today's

68.5%, with the adoption of the fund's actuarial valuation in April. The West Sacramento-based pension system, the second largest in the U.S. by assets, had a 1.4% net return for the fiscal year ended June 30.

3. HEDGE FUNDS REACH NEW HIGHS AND LOWS IN 2016: For hedge funds, 2016 was the best of times and the worst of times, as the industry reached record levels of assets under management -- and investor disappointment. Hedge funds reported gains of 7.4% for the year, which was its best showing in three years, and reached a record \$3.22 trillion in total assets under management, according to Preqin's 2017 Global Hedge Fund Report. But at the same time, there were net outflows of \$102 billion, and a record 66% of hedge fund investors said that their portfolios had performed below their expectations for the year. And even more investor capital is expected to be redeemed in 2017, as 38% of investors plan on reducing their hedge fund exposure this year, while only 20% plan on increasing their exposure, according to the report. One of the main reasons many major investors are being turned off of hedge funds is because of concerns over high fees. The industry needs to "address issues over fees in order to win back the growing group of investors skeptical of the value of the asset class." Although hedge funds had their largest gains in three years, their performance in recent years, or lack thereof, has also been cited as a factor that's putting off potential investors. The report found that the proportion of hedge funds delivering positive annual returns has declined sharply since 2014. In

2014, approximately 80% of hedge funds added gains during that year, while only 49% of funds show positive returns in 2016. The report also said that the largest public pension funds with the most money allocated to hedge funds were ABP of the Netherlands, which has \$19.5 billion invested in hedge funds, Canada's CPP Investment Board, which has \$13.5 billion in hedge fund assets and South Korea's National Pension Service with \$923 million. At the start of 2017, investor dissatisfaction with hedge funds remains high, and that the pace of capital redemptions has been accelerating. However, many fund managers said they are confident returns for this year will surpass those of 2016. However, if outflows continue in 2017, we may continue to see a shakeout of those funds that have failed to meet investors' return expectations in recent years and a contraction in the size of the industry.

4. A LEGISLATIVE ROADMAP FROM U.S. CHAMBER OF

COMMERCE: Under the category of "I am here from Washington and I came to help you," U.S. Chamber of Commerce has released its Winter 2017 "Securing America's Retirement -- A Legislative Roadmap." U.S. Chamber of Commerce has developed private sector driven policy solutions focused on achieving retirement security for workers. As 2017 welcomes a new presidential administration and Congress, the Chamber is pleased to present its legislative roadmap of retirement proposals for policymakers to consider and enact. The roadmap focuses on strengthening the voluntary employment-based retirement benefits system and enhancing retirement security for

workers, while proposing would-be solutions to address the country's evolving workforce as demographics continue to change -- an important and pressing issue that policymakers will need to tackle in 2017. The proposals outlined in the roadmap are divided into three sections:

- Previously Introduced Legislation
- Legislative Recommendations
- Policy Ideas for Congressional Action

The Chamber looks forward to working with the incoming administration, Congress and stakeholder groups to develop legislative solutions addressing retirement security. The Chamber also welcomes the opportunity to partner with policymakers on public-private initiatives focused on educating Americans about financial literacy and retirement savings. Make sure closely to read the conclusion:

This roadmap has one overarching theme -- the voluntary nature of the private employer system. The system's voluntary nature is critical because it allows an employer to choose whether or not to offer a retirement plan, as well as the type of plan that is best for its workforces. As policymakers move to strengthen the retirement system, they must protect those parts of the system that are essential to its success. To that end, the Chamber stands ready to work with Congress, the administration, and all other interested parties to strengthen the voluntary, employer-provided retirement system. Right.

5. FORD TAKES A \$2 BILLION CHARGE DUE TO PENSIONS,

BENEFITS: According to a piece in the *USA Today*, Ford said its 2016 net income will drop by \$2 billion because of a change in the way it values pensions and retiree benefits. The automaker is changing how it values pensions and other retiree obligations and is now counting them in the year they were incurred instead of spreading out the impact over a number of years. Ford said the pension loss will now be recognized each year instead of in its automotive business units and will be reported as a special item, since it is not reflective of the underlying operating results of our automotive business. On an after-tax basis, the remeasurement loss will reduce Ford's full-year net income by about \$2 billion in 2016, said in a document filed with the U.S. Securities and Exchange Commission. The accounting change should not affect profit sharing for hourly workers represented by the United Auto Workers union because the formula is based on the automaker's pretax profits in North America. Last year, workers received an average pretax profit-sharing check of \$6,900. The automaker said the pension accounting change will not affect the company's pretax profits. Ford reported its year-end results and said it still expects to meet its guidance of about \$10.2 billion in pretax profits for 2016. The automaker does not release guidance for net income.

6. FLORIDA STATE LEGISLATORS TEAM UP ON ANOTHER

AMBITIOUS PENSION REFORM BILL: Florida Public Pension Trustees Association *Pension Clips* report that Representative Jason

Fischer and Senator Jeff Brandes have filed two bills in their respective chambers that would close the Florida Retirement System's defined benefit plan to new cities as previously reported ([See C & C Newsletter for February 2, 2017, Item 6.](#)) That bill has gotten pushback already from Republicans in both chambers. Now, a new bill is set to be filed in both chambers that would reform local pensions, Fischer's House Bill 603 and Brandes's Senate Bill 632 would put a check on the often optimistic rates of return on investments that create a rosier picture of solvency than actually exists in local pension plans. The Brandes/Fischer bills also create a new language: a "long range return rate." The definition, used in the 2014 Society of Actuaries Report on public pension plans, is the rate of return to be met at least 50% of the time over three decades. Starting in 2021, assumed rates of return that exceed that mark are prohibited, and public pension plan administrators will be compelled to lower their expected rate of return by 25 basis points a year until projections meet reality. The Brandes/Fischer legislation would require those long range return rates to be calculated every five years.

7. EARLY WITHDRAWALS FROM RETIREMENT PLANS:

According to the Internal Revenue Service, many people find it necessary to withdraw money from their IRA or retirement plan early. Doing so, however, can trigger an additional tax on top of income tax taxpayers may have to pay. Here are a few key points to know about taking an early distribution:

- **Early Withdrawals.** An early withdrawal normally is taking cash out of a retirement plan before the taxpayer is 59½ years old.
- **Additional Tax.** If a taxpayer took an early withdrawal from a plan last year, the taxpayer must report it to the IRS. The taxpayer may have to pay income tax on the amount taken out. If it was an early withdrawal, the taxpayer may have to pay an additional 10% tax.
- **Nontaxable Withdrawals.** The additional 10% tax does not apply to nontaxable withdrawals. These include withdrawals of contributions that taxpayers paid tax on before they put them into the plan. A rollover is a form of nontaxable withdrawal. A rollover occurs when people take cash or other assets from one plan and put the money in another plan. They normally have 60 days to complete a rollover to make it tax-free.
- **Check Exceptions.** There are many exceptions to the additional 10% tax. Some of the rules for retirement plans are different from the rules for IRAs.
- **File Form 5329.** If someone took an early withdrawal last year, the taxpayer may have to file Form 5329, Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts, with his federal tax return. Form 5329 has more details.
- **Use IRS e-file.** Early withdrawal rules can be complex. IRS e-file is the easiest and most accurate way to file a tax return. The tax software that taxpayers use to e-file will pick the right tax

forms, do the math and help get the tax benefits they are due. Seven out of 10 taxpayers qualify to use IRS Free File tax software. Free File is only available through the IRS website at [IRS.gov/freefile](https://www.irs.gov/freefile).

More information on this topic is available on [IRS.gov](https://www.irs.gov). IRS Tax Tip 2017-09 (February 6, 2017).

8. FAKE CHARITIES ON THE IRS “DIRTY DOZEN” LIST OF TAX SCAMS FOR 2017:

The Internal Revenue Service is warning taxpayers about groups masquerading as charitable organizations to attract donations from unsuspecting contributors, one of the “Dirty Dozen” Tax Scams for the 2017 filing season. Taxpayers should take the time to research organizations before giving their hard-earned money. Compiled annually, the “Dirty Dozen” lists a variety of common scams that taxpayers may encounter anytime, but many of these schemes peak during filing season as people prepare their returns or hire someone to prepare their taxes. Perpetrators of illegal scams can face significant penalties and interest and possible criminal prosecution. IRS Criminal Investigation works closely with the Department of Justice to shut down scams and prosecute the criminals behind them. The IRS offers these basic tips to taxpayers making charitable donations:

- Be wary of charities with names that are similar to familiar or nationally known organizations. Some phony charities use names or websites that sound or look like those of respected,

legitimate organizations. IRS.gov has a search feature, Exempt Organizations Select Check, which allows people to find legitimate, qualified charities to which donations may be tax-deductible. Legitimate charities will provide their Employer Identification Numbers (EIN), if requested, which can be used to verify their legitimacy through EO Select Check. It is advisable to double check using a charity's EIN.

- Do not give out personal financial information, such as Social Security numbers or passwords, to anyone who solicits a contribution. Scam artists may use this information to steal identities and money from victims. Donors often use credit cards to make donations. Be cautious when disclosing credit card numbers. Confirm that those soliciting a donation are calling from a legitimate charity.
- Do not give or send cash. For security and tax record purposes, contribute by check or credit card or another way that provides documentation of the gift.

Another long-standing type of abuse or fraud involves scams that occur in the wake of significant natural disasters. Following major disasters, it is common for scam artists to impersonate charities to get money or private information from well-intentioned taxpayers. Scam artists can use a variety of tactics. Some scammers operating bogus charities may contact people by telephone or email to solicit money or financial information. They may even directly contact disaster victims and claim to be working for or on behalf of the IRS to help the victims

file casualty loss claims and get tax refunds. Fraudsters may attempt to get personal financial information or Social Security numbers that can be used to steal the victims' identities or financial resources. Bogus websites may solicit funds for disaster victims. To help disaster victims, the IRS encourages taxpayers to donate to recognized charities. Disaster victims can call the IRS toll-free disaster assistance telephone number (866-562-5227). Phone assistants will answer questions about tax relief or disaster-related tax issues. Find legitimate and qualified charities with the Select Check search tool on IRS.gov. (EINs are frequently called federal tax identification numbers, which is the same as an EIN). IR-2017-25 (February 7, 2017).

9. NEW OFFICE ADDRESS: Please note that Cypen & Cypen has a new office address: Cypen & Cypen, 975 Arthur Godfrey Road, Suite 500, Miami Beach, Florida 33140. All other contact information remains the same.

10. CRAZY STATE LAWS: *Good Housekeeping* reminds us that there are crazy laws in every state. In In Arkansas, you cannot honk your horn near a sandwich shop after 9 p.m. A hungry fool is to blame for this law, but hey, most of the sandwich shops are closed in the sleepy state of Arkansas by 9 p.m. anyway. If you do feel the urge to honk after hours, you will be disturbing the peace and you will still be hungry.

11. ZEN PROVEN TEACHINGS TO LIVE BY: Some days you are the dog, some days you are the tree.

12. PONDERISMS: If electricity comes from electrons, does morality come from morons?

13. TODAY IN HISTORY: In 1953, Allen W. Dulles, becomes acting director of CIA.

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.

