CYPEN & CYPEN

NEWSLETTER

for

March 8, 2018

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

1. FEDERAL EMPLOYEES' RETIREMENT SYSTEM: SUMMARY OF RECENT TRENDS:

Katelin P. Isaacs, a specialist in Income Security, has released a report that describes recent trends in the characteristics of annuitants and current employees covered by the Civil Service Retirement System (CSRS) and the Federal Employees' Retirement System (FERS), as well as the financial status of the Civil Service Retirement and Disability Fund

(CSRDF).

· In FY2016, 94% of current civilian federal employees were enrolled in FERS, which covers employees hired since 1984. Six percent were enrolled in CSRS, which covers only employees hired before 1984.

· In FY2016, more than 2.6 million people received civil service annuity payments, including 2,077,804 employee annuitants and 533,884 survivor annuitants. Of these individuals, 72% received annuities earned under CSRS.

· About one-third of all federal employee annuitants and survivor annuitants reside in five states: California, Texas, Florida, Maryland and Virginia.

· The average civilian federal employee who retired in FY2016 was 61.3 years old and had completed 25.6 years of federal service.

· The average monthly annuity payment to workers who retired under CSRS in FY2016 was $4,755. Workers who retired under FERS received an average monthly annuity of $1,714. Employees retiring under FERS had a shorter average length of service than those under CSRS. FERS annuities are supplemented by Social Security benefits and the Thrift Savings Plan (TSP).

· At the end of FY2016, the balance of the CSRDF was $879.8 billion, an amount equal to more than 10 times the amount of outlays from the fund that year. The trust fund balance is expected to reach $909 billion by the end of FY2018.

· From FY1970 to FY1985, the number of people receiving federal civil service annuities rose from fewer than 1 million to nearly 2 million, an increase of 105%. Between FY1985 and FY2016, the number of civil service annuitants rose by 680,000, an increase of about 35%.

· In FY2013, the number of civilian federal employees, including Postal Service employees, totaled 3.3 million workers. This was 254,000 less than the number of employees in FY2000, and 480,000 fewer than the number of employees in FY1994.

· In FY2016, all CSRS employees were aged 45 or older, compared with 61% of FERS employees who were aged 45 or older (38.6% of FERS employees were younger than 45). Fifty five percent of CSRS employees were aged 60 or older, whereas 13% of FERS employees were in this age range. For a general overview of current benefits and financing under CSRS and FERS, see CRS Report 98-810, *Federal Employees' Retirement System: Benefits and Financing*. For summary information on recent reform proposals related to CSRS and FERS, see CRS In Focus IF10243, Civilian Federal

Retirement: Current Law, Recent Changes, and Reform Proposals.

2. CHINA'S "BIGGEST FISCAL RISK IS PENSION RISK" FROM AGING POPULATION:

China's pension shortfall is emerging as the next big challenge for policy makers as they intensify their years-long campaign to keep rising debt from derailing the economy. Aging in the world's most populous country means pension contributions by workers no longer cover retiree benefits, forcing the government to fill that gap since at least 2014. Pension expenses rose 11.6 percent to 2.58 trillion yuan ($410 billion) in 2016, leaving the government a 429.1 billion yuan tab to cover the shortfall, according to the latest available data from the Finance Ministry. That shortfall will reach 600 billion yuan this year and 890 billion yuan in 2020 if the system is not reformed, according to Wang Dehua, a researcher at the National Academy of Economic Strategy in Beijing. Enodo Economics in London, which has advised policy makers on the matter, forecast last year that it could soar to 1.2 trillion yuan by 2019. The finance ministry does not release estimates. "China's biggest fiscal risk is pension risk," said Wang, whose institute is under the Chinese Academy of Social Sciences, the government's top think tank. "There are big problems in the pension system if it can only keep operating with large fiscal subsidies." The shortfall adds urgency to President Xi Jinping's quest to stem rampant growth in corporate debt, given the government will need to fund widening deficits of its own in coming years. Leaders may offer an update to the pension outlook on March 5 when they convene for the annual National People's Congress in Beijing. While government revenue rose 7.4 percent last year for its first acceleration since 2011, that is unlikely to keep rebounding amid slower economic growth. That would limit Beijing's ability to cover the shortfall, which may push policy makers to issue debt to bridge the gap. China has been doing so well in many aspects in the past years, but it has really been left behind in pensions. Premier Li Keqiang pledged in his report to last year's congress to increase the allowances. "We will weave a strong safety net to ensure people's well-being," Li said. "We will continue raising basic pension payments and see they are paid on time and in full." The population is graying quickly. The State Council said last year that about a quarter of China's population will be 60 or older by 2030, up from 13.3 percent in the 2010 census. Meanwhile, scrapping the one-child policy has not raised birth rates as high living costs deter larger families. Births fell to 17.2 million last year from 18.5 million in 2016. Still, unbalanced demographic and employment trends may help the economy as they support further rebalancing and consumer spending, Enodo's Chief Economist Diana Choyleva says. "China's graying population is often analyzed in the context of a rising old-age dependency ratio and the strain it implies for the public finances," she wrote in a report this month. "But it Is worth pointing out that a higher proportion of pensioners, who consume but do not produce, should lead to a structural increase in the share of consumer spending in GDP." Those benefits aside, signs of strain are already visible in the pension system, and the deficit is poised to "quickly increase" after 2020, according to Liu Shangxi, director of Chinese Academy of Fiscal Sciences, a think tank affiliated with the Finance Ministry. The central government said in November that a handful of larger state-owned enterprises and financial institutions would transfer 10 percent of their state-owned equity to social security funds to help ease pension payment pressure. New details have not been released. The Finance Ministry and Ministry of Human Resources and Social Security did not respond to requests for comment faxed Monday morning. The MOHRSS has delayed the release of annual social insurance reports, offering a less-timely glimpse into the nation's pension burdens. China has been paying retirees with contributions made by the working population since it set up the current pension system in early 1990s. The gap between money coming in and payments going out has been widening as more retire and fewer join the workforce. China should encourage individuals to invest more for their retirement to reduce the burden on the government, which cannot shoulder the responsibility all on its own.

3. UBIT OVERVIEW? -- YOU BET!:

Private pension plans described in section 401(a) of the Internal Revenue Code (the Code) are generally exempt from federal income tax under section 501(a) of the Code. However, under section 511(a), otherwise tax-exempt organizations must pay Unrelated Business Income Tax (UBIT) on income derived from a trade or business that is "unrelated" to the organization's tax-exempt purpose. The basic rationale is that without UBIT, tax-exempt investors would be willing to pay more than private investors for the same investment if they did not have to pay federal income tax on investment gains. By putting private and tax-exempt investors on the same playing field, UBIT prevents tax-exempt investors from gaining an unfair economic advantage. UBIT arises in two ways. First, tax-exempt organizations generally pay UBIT on net income derived from any unrelated trade or business. For example, a private pension plan that invests in a fund that operates an active trade or business (*e.g.*, a retail clothing outlet) generally pays UBIT on gains derived from that investment. Second, tax-exempt organizations pay UBIT on so-called "debt financed" income, that is, income derived from investments acquired either directly or indirectly by borrowing. For example, a private pension plan that purchases real property, 75% of which is funded with debt, pays UBIT on 75% of the rental income derived from the investment (unless an exception applies). So-called "passive" income streams (*e.g.*, dividends, interest, royalties, and rents) remain exempt from UBIT unless derived from debt-financed property. Where UBIT does apply, tax-exempt organizations incur it either directly or on a pass-through basis (*i.e.*, through a partnership or LLC in which it invests). Unrelated business income is taxed at trust rates, which accelerate quickly to 37%. Historically, many state and local governmental pension plans have taken the position that, because they perform an "essential government function" with income that is exempt from federal income tax under section 115(1) of the Code, they remain exempt from UBIT. While there is limited guidance addressing this position, to date, the IRS has not challenged plans on this point. Thus, even though governmental plans are described in section 401(a) of the Code and would, therefore, generally incur UBIT under section 511(a)(2)(A), for decades governmental plans have treated themselves as exempt from UBIT. *GRS Insight*, January 2018

4. BIGGEST GAINS IN UNION MEMBERSHIP IN 2017 WERE FOR YOUNGER WORKERS:

The Bureau of Labor Statistics released data on changes in union membership from 2016 to 2017. It was good news for workers, as the total number of union members grew by 262,000 in 2017. Three-fourths of these gains (198,000) were among workers aged 34 and under, who account for less than 40 percent of total employment. Historically, younger workers have been less likely than older workers to be a member of union. In 2017 about 7.7 percent of workers 16–34 were members of a union, compared with 12.6 percent of workers age 35 and older. But last year, of the 858,000 net new jobs for workers under age 35, almost one in four (23 percent) was a union job. In a recent EPI paper, we explain that one reason younger workers are joining unions is to address current workforce trends that are increasing work insecurity from the rise of part-time work and unpaid internships to increased numbers of contract workers.

5. GAO UNABLE TO RENDER AN OPINION ON THE U.S. GOVERNMENT'S ANNUAL FINANCIAL STATEMENTS:

The U.S. Government Accountability Office (GAO) was unable to render an opinion on the federal government's consolidated financial statements for fiscal year 2017. GAO cited shortcomings that have plagued the financial statements in past years, including persistent problems with the Department of Defense's (DOD) financial management and auditability, the federal government's inability to account for and reconcile certain transactions, and an ineffective process for preparing the consolidated financial statements. Such deficiencies undermine the federal government's ability accurately to report much of its financial information. "It's essential that the federal government be able adequately to track all revenues and expenses, along with its assets and liabilities. It is critical to improving the accountability, effectiveness and efficiency of government operations," said Gene L. Dodaro, Comptroller General of the United States and head of the GAO. "GAO's audit report makes clear the continuing challenges to providing policymakers with the accurate and complete financial information needed for ensuring accountability and making difficult policy decisions." For 2017, with few exceptions, all of the 24 Chief Financial Officers Act agencies received unmodified or "clean" opinions on their respective individual entities' fiscal year 2017 financial statements. However, about 38 percent of the federal government's reported total assets as of September 30, 2017, and approximately 20 percent of the federal government's reported net cost for FY 2017, involved federal entities that were unable to issue audited financial statements, unable to receive audit opinions on the complete set of financial statements, or unable to receive an opinion on their FY 2017 financial statements. Notably, DOD, the Department of Housing and Urban Development, and the Department of Agriculture have continuing impediments to receiving a clean opinion on their financial statements. GAO also could not render an opinion on the sustainability financial statements due to significant uncertainties about achieving projected reductions in Medicare cost growth and a material weakness in internal control over financial reporting. These sustainability financial statements consist of the 2017 and 2016 Statements of Long-Term Fiscal Projections; the 2017, 2016, 2015, 2014, and 2013 Statements of Social Insurance; and the 2017 and 2016 Statements of Changes in Social Insurance Amounts. Acknowledging ongoing efforts to resolve the government's financial management challenges, Dodaro called for strong and sustained commitment by DOD and other federal entities, along with continued leadership by the U.S. Department of the Treasury and the Office of Management and Budget, to achieve more accurate and complete financial reporting. Dodaro also raised concerns about the problem of improper payments by federal agencies, which GAO reported as a material weakness. Such payments are estimated at about $141 billion for FY 2017. Other material weaknesses reported by GAO this year included information security across government and tax collection activities. Dodaro said he was pleased by the recent actions which will allow the federal government to continue to borrow funds to finance the decisions already enacted by Congress and the President. He emphasized the importance of safeguarding the full faith and credit of the United States and noted that GAO has recommended the Congress change how it deals with the debt limit so that decisions about borrowing are tied to the spending and revenue decisions at the time when those decisions are made. Dodaro added that the Financial Report, and simulations by CBO and GAO, all show that the federal government currently is on an unsustainable long-term fiscal path. He noted GAO has recommended that the Congress develop a plan to address this long-term outlook, even as it must respond to near-term economic and national priorities. Dodaro thanked the Inspectors General throughout government for their hard work and professionalism in auditing the annual financial statements of their respective departments and agencies. GAO's audit report on the U.S. government's consolidated financial statements is included in the 2017 Financial Report of the United States Government, which is prepared by the Department of the Treasury in coordination with the Office of Management and Budget. GAO's audit report is available on GAO's website at www.gao.gov/products/GAO-18-316R. GAO has also updated its guide to the Financial Report of the United States Government. The guide is intended to help those who seek to obtain a better understanding of the Financial Report and is available on GAO’s website at www.gao.gov/products/GAO-18-239SP. For more information, contact Chuck Young, Managing Director of Public Affairs, at 202.512.4800. Press Release (February 15, 2018)

F.Y.I., the Government Accountability Office, known as the investigative arm of Congress, is an independent, nonpartisan agency that exists to support Congress in meeting its constitutional responsibilities. GAO also works to improve the performance of the federal government and ensure its accountability to the American people. The agency examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO provides Congress with timely information that is objective, fact-based, nonideological, fair, and balanced. GAO's commitment to good government is reflected in its core values of accountability, integrity and reliability.

6. EX-SPOUSE BENEFITS AND HOW THEY AFFECT YOU:
Just like during tax season, it is good to have all the information you need early so you can prepare and get any money you are due. If you are age 62, unmarried and divorced from someone entitled to Social Security retirement or disability benefits, you may be eligible to receive benefits based on his record. To be eligible, you must have been married to your ex-spouse for 10 years or more. If you have since remarried, you cannot collect benefits on your former spouse's record unless your later marriage ended by annulment, divorce or death. Also, if you are entitled to benefits on your own record, your benefit amount must be less than you would receive based on your ex-spouse's work. In other words, we will pay the higher of the two benefits for which you are eligible, but not both. You can apply for benefits on your former spouse's record even if he has not retired, as long as you divorced at least two years before applying. If, however, you decide to wait until full retirement age to apply as a divorced spouse, your benefit will be equal to half of your ex-spouse's full retirement amount or disability benefit. The same rules apply for a deceased former spouse. The amount of benefits you get has no effect on the benefits of your ex-spouse and his or her current spouse. Visit *Retirement Planner: If You Are Divorced* to find all the eligibility requirements you must meet to apply as a divorced spouse. Our benefits planner gives you an idea of your monthly benefit amount. If your ex-spouse died after you divorced, you may still quality for widow's benefits. You will find information about that in a note at the bottom of the website. Visit *Retirement Planner: If You Are Divorced* today to learn whether you are eligible for benefits on your ex-spouse's record. That could mean a considerable amount of monthly income. What you learn may bring a smile to your face … even on tax day! Posted on February 15, 2018 by Jim Borland, Acting Deputy Commissioner for Communications

7. 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.

8. CLEVER WORDS:
Pharmacist: A helper on the farm.

9. INSPIRATIONAL QUOTE:
The most common way people give up their power is by thinking they do not have any. – Alice Walker

10. LEXOPHILES:
Bakers trade bread recipes on a knead to know basis.

11. TODAY IN HISTORY:
On this day in 1948, US Supreme Court rules in McCollum v. Board of Education that religious instruction in public schools is unconstitutional.

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

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