



CYPEN & CYPEN

NEWSLETTER

for

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

1. TREASURER CALLS FOR REVIEW OVER CALPERS CEO'S POTENTIAL MISREPRESENTATIONS AFTER BOARD OKAYS RAISE, BONUS:

The board of the \$360 billion [California Public Employees' Retirement System](#), Sacramento, approved giving CEO Marcie Frost a 4% raise resulting in a salary of \$330,720 for the 2019 fiscal year and a 26.7% bonus of \$84,873 for the 2018 fiscal year. Following the board meeting, California Treasurer John Chiang, who is a member of the

CalPERS board, issued a statement calling for an independent review by a neutral third party into whether Ms. Frost made misrepresentations regarding a college degree. Even so, Mr. Chiang voted for the raise and the bonus. Margaret Brown was the only CalPERS board member to vote against the raise and bonus. In response to questions about Mr. Chiang's vote, spokesman John Wark referred to his statement that "since her appointment in June 2016, Marcie Frost has largely proven her competency as the CEO of the nation's largest pension fund, and I have submitted extensive performance evaluations that reflect my favorable opinion of her." He added in the statement that although he hopes Ms. Frost will be exonerated, that his fiduciary duty to CalPERS comes first. However, given recent press reports, Mr. Chiang said in his statement that "I can no longer sit on the sidelines, watching how some have been quick to paint Ms. Frost as an untruthful villain, while others have too casually dismissed what are serious allegations. Both are a rush to judgment." "The treasurer has made his thoughts and recommendations known to all of his colleagues as well as the CEO," Mr. Wark said. Board President Priya Mathur responded in a statement that "there is no need for an independent review." She said that Ms. Frost is an "extraordinary professional who has distinguished herself throughout her career and, in particular, during her two years leading CalPERS." "The board's review this week on all matters regarding her performance sends a clear and unequivocal message that she has delivered for California public-sector workers and retirees," Ms. Mathur said. The performance, compensation and talent management committee recommended the board award Ms. Frost the raise and bonus after a more than four hour closed session during which it conducted Ms. Frost's annual performance review, said Bill Slaton, a board trustee and committee chairman. In a personal comment following the board's vote to give Ms. Frost a raise and a bonus one day later, Mr. Slaton said: "We have a great hire in the CIO (Yu Ben Meng) that's coming on board and the CFO (Michael Cohen) that's coming on board. So I think the committee feels we have the right team here and that we're very excited about our future going forward in serving our members and retirees." Ms. Frost's recommended bonus was slightly under the target of 27%, according to CalPERS' most recent executive compensation policy. The committee could have given Ms. Frost a bonus of up to 40% of base pay, according to the policy. The CEO's maximum pay range is \$224,000 to \$352,800, under the current policy. There was no discussion during the committee's open meeting concerning the current controversy surrounding inaccurate representations in a

news release and candidate memorandum when Ms. Frost was hired, which said she was working on a dual bachelor's and master's degree. Ms. Frost was enrolled but did not complete a program at Evergreen State College that awards units toward a bachelor's degree based on experience. "So, I know that we usually do not have a performance compensation talent management with such a large audience," Mr. Slaton quipped at the start of the open session. He added that the committee would not be discussing Ms. Frost's performance. "In closed session we spent a long time reviewing all matters regarding Ms. Frost's performance and now in open session we are convening in compliance with our policy regarding personnel matters to discuss compensation only." Arleen Jacobius, *Pensions & Investments*, September 26, 2018.

2. TRANSLATING ACCOUNT BALANCES TO MONTHLY RETIREMENT INCOME HELPS PARTICIPANTS:

Many Americans do not always understand how their retirement account balances will translate into income during their retirement years, Life Insurance and Market Research Association (LIMRA) Secure Retirement Institute (LIMRA SRI) research finds. More than half (52%) of all U.S. workers (ages 20 to 79) surveyed by LIMRA SRI say it is difficult to know how retirement savings will translate into monthly income. The study suggests [offering workers retirement savings income estimates](#) can help bridge this gap. Fifty-two percent of respondents say they have seen an estimate of their retirement income. About four in 10 retirees wished they had seen more frequent estimates of how much monthly income their savings would generate in retirement before becoming retired. When it comes to generations, Baby Boomers are more likely to have seen an estimate of their monthly income than Gen X or Millennials. LIMRA SRI says viewing their monthly income in actual dollar amounts, rather than as a percentage of pre-retirement income, is more meaningful to Baby Boomers. Since they will most likely be retiring sooner than younger generations, they may have a better sense about what their retirement expenses will be. Retirement income estimates help improve the retirement decisions of workers. As a result of seeing their estimated income, almost half of all workers (48%) increased their retirement savings. This could have the greatest impact on the savings habits of younger workers as they have more time to accrue savings. LIMRA SRI finds 55% of Millennials increased their retirement savings after seeing their estimated retirement income. Understanding how retirement savings translates into retirement income also boosts

workers' confidence in their retirement. Among workers who received an estimate of what their income would be in retirement, almost seven in 10 were confident they would live the retirement lifestyle they desired, and seven in 10 were confident they were saving enough to live comfortably in retirement. In contrast, only three in 10 workers who did not receive this kind of estimate were confident in their retirement security. Additionally just three in 10 who did not receive their estimate said they were confident they were saving enough to live comfortably in retirement. More results from the LIMRA SRI study may be found [here](#).
Rebecca Moore, *Plansponsor*, September 25, 2018,

3. THE FED HAS SOLVED THE BOND MARKET'S PENSION PUZZLE:

One of this year's bond-market mysteries might be solved: After the Federal Reserve revised one of its key data releases, strategists now know where U.S. corporate pension plans have been investing. Corporate pension plans, which manage [\\$1.6 trillion in assets](#), have been in the spotlight this year, thanks to a quirk in the U.S.'s new tax law. Specifically, pension contributions made during the "[grace period](#)" before Sept. 15 could be [deducted](#) at 2017's higher tax rate, while contributions made afterward will probably need to be deducted at the lower corporate tax rate that goes into effect next year. That apparently encouraged the \$1 billion [pension contributions](#) from [Verizon Communications](#) (VZ) and [General Electric](#) (GE) in the first quarter of this year. Overall, analysts at [Goldman Sachs](#) estimated early this week that companies would contribute \$60 billion to their pension plans this year, on top of \$63 billion last year. That has left investors and market-watchers to wonder where exactly that cash has gone. Normally, this question can be answered with the Fed's [Financial Accounts data](#), which measures the [flow of funds](#) from investors such as pensions, insurers, investment funds and households. (The data discussed here cover only pension plans managed by employers, and excludes public pensions and individual retirement accounts. The Fed reports quarterly flows as a seasonally adjusted annual rate.) There was just one problem: The [June report](#) said that private-sector pensions sent \$14 billion into the corporate bond market and sold \$300 million of Treasuries. But the market itself has not clearly reflected demand for the long-term corporate debt favored by pensions. Strategists at [Bank of America Merrill Lynch](#) highlighted the gap between yields on 10-year and 30-year corporate bonds (specifically nonbank issuers with A credit ratings). That gap widened to nearly 35 basis points this month, from a low of near 25 basis points in May. The opposite happened in the Treasury

market, according to Bloomberg data: The difference between 10-year and 30-year yields has narrowed to roughly 14 basis points after slipping under 20 basis points in May. Thankfully, the Fed revised the data in its [flow of funds report](#) released, which helped [strip away](#) some of the confusion. This latest picture of corporate-pension demand looks very different. Private-sector pensions were actually on pace to buy \$53 billion of Treasuries and just \$8 billion of corporate bonds in the first quarter, according to the report. In the second quarter, they shifted toward corporate debt, but only slightly, with \$51 billion of Treasuries and \$9 billion of corporate bonds. Bank of America strategist Hans Mikkelsen pinpointed one potential source of the mix-up in a note. He and his colleagues wrote that a certain type of Treasury security might have been “mis-classified” as corporate debt. These are Treasuries in “stripped form,” meaning investors have bought only the principal or coupon parts of a long-term bond or note. (They are also known as STRIPS, which is an acronym for “Separate Trading of Registered Interest and Principal of Securities.”) There has been a noticeable pick-up in the amount of STRIPS outstanding. At the end of August, investors held 13% more Treasuries in STRIPS form than they did the year before, according to [data](#) from the Treasury Department. That followed an increase of 14% during the prior 12 months. Those constituted a big acceleration from the previous two years, when STRIPS holdings rose 4% and 1%. Now that September 15, 2018 has passed, the question is whether the U.S. Treasury yield curve will get steeper. The short answer? Probably not, according to Praveen Korapaty and Avisha Thakkar, strategists at Goldman Sachs. The strategists wrote that corporate pension plans will probably keep buying Treasuries as their funding ratios improve, so they can better match their liabilities. They also said that accounting-rule changes could discourage some company pensions from owning stocks or other risky assets. Additional demand could come from government pension plans, which manage more than [\\$3.6 trillion in assets](#). Those funds have been buying Treasuries to improve their portfolios’ liquidity as they raise allocations to real estate and private equity. They could also be buying inflation-protected securities because their payments to pensioners are adjusted for inflation, the strategists wrote. “Some rough calculations suggest... buying totaling about \$400 billion over the next five years, and would likely outweigh any marginal decline in tax-related buying,” wrote Korapaty and Thakkar. “Both of these inflows are likely to be gradual, but over time will weigh on the long end of the yield curve.” Alexandra Scaggs, *Barron's*, September 24, 2018.

4. AGENCIES APPROVE AMENDMENTS TO SWAP MARGIN RULE:

Press Release

Board of Governors of the Federal Reserve System
Farm Credit Administration
Federal Deposit Insurance Corporation
Federal Housing Finance Agency
Office of the Comptroller of the Currency

SUMMARY: The Board, OCC, FDIC, FCA and FHFA (each an Agency and, collectively, the Agencies) are adopting amendments to their rules establishing minimum margin requirements for registered swap dealers, major swap participants, security-based swap dealers, and major security-based swap participants (Swap Margin Rule). These amendments conform the Swap Margin Rule to rules recently adopted by the Board, the OCC, and the FDIC that impose restrictions on certain qualified financial contracts, including certain non-cleared swaps subject to the Swap Margin Rule (the QFC Rules). Specifically, the final amendments to the Swap Margin Rule conform the definition of “Eligible Master Netting Agreement” to the definition of “Qualifying Master Netting Agreement” in the QFC Rules. The amendment to the Swap Margin Rule ensures that netting agreements of firms subject to the Swap Margin Rule are not excluded from the definition of “Eligible Master Netting Agreement” based solely on their compliance with the QFC Rules. The amendment also ensures that margin amounts required for non-cleared swaps covered by agreements that otherwise constitute Eligible Master Netting Agreements can continue to be calculated on a net portfolio basis, notwithstanding changes to those agreements that will be made in some instances by firms revising their netting agreements to achieve compliance with the QFC Rules. In addition, for any non-cleared swaps that were “entered into” before the compliance dates of the Swap Margin Rules – and which are accordingly grandfathered from application of the rule’s margin requirements – the amendments state that any changes to netting agreements that are required to conform to the QFC Rules will not render grandfathered swaps covered by that netting agreement as “new” swaps subject to the Swap Margin Rule. FDIC: PR-64-2018. Here is the [Final Rule](#).

5. LAWSUIT DISMISSED AGAINST KENTUCKY RETIREMENT SYSTEMS OVER ALT INVESTMENTS:

A lawsuit alleging that [Kentucky Retirement Systems](#), illegally invested some participants' retirement assets in private equity and hedge funds has been dismissed, said David Eager, executive director of KRS, which has \$12.3 billion across its five pension plans. Fort Wright, Ky., filed a class-action lawsuit against the KRS board in 2014, alleging board members breached fiduciary and statutory duties by investing funds of the County Employees Retirement System in unauthorized, high-risk and costly alternative investments. Fort Wright is a participant in CERS, which is administered by KRS. Franklin County Circuit Court Judge Thomas Wingate ruled in favor of the KRS board, saying, "There is nothing in the record or in the city's pleadings to this court that persuades this court that the board did not follow the law or did not appropriately apply the facts to the law." These investments were not permitted by Kentucky state statutes, the suit alleged. "The court ruling certainly affirmed what we have believed all along: that we're in our legal right to make investments, and the investments we made were legal," Mr. Eager said in response the court's decision. Mr. Eager added that the plaintiffs have 30 days to appeal the decision. James Comtois, *Pensions & Investments*, September 21, 2018.

6. OXYMORONS:

Why do they call it a TV set when you only have one?

7. INSPIRATIONAL QUOTES:

When one door of happiness closes, another opens, but often we look so long at the closed door that we do not see the one that has been opened for us. – Helen Keller

8. TODAY IN HISTORY:

On this day in 1986, Ronald Reagan and Mikhail Gorbachev open talks at a summit in Reykjavik, Iceland.

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

Items in this Newsletter may be excerpts or summaries of original or secondary source material, and may have been reorganized for clarity and brevity. This Newsletter is general in nature and is not intended to provide specific legal or other advice.