



# CYPEN & CYPEN NEWSLETTER for August 27, 2020

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

## **1. PUBLIC PLAN FUNDING NOT SUCCUMBING TO VIRUS, RESEARCH FINDS:**

Public pension plans will see virtually no change in their average funding ratio during fiscal year 2020 despite the ongoing COVID-19 pandemic, [research from the Center for State and Local Government Excellence and the Boston College Center for Retirement Research](#) found.

And while the financial strains that the recession put on plan sponsors could make it more difficult for them to pay their required contributions, the research suggests that small public plans have sustainable cash flows. The exceptions, of course, are the worst-funded plans.

State and local plans appear to have similar short- and near-term paths. Funded ratios for state plans are projected to be 72.4% on average for 2020, vs. 70.8% for local plans.

The research projects local plans to have an aggregate funded ratio between 61.7% and 64.6% by fiscal year 2025, while state plans are projected to have an aggregate funded ratio between 65.2% and 68.2% and during that period.

"It is still unclear the extent to which the COVID-19 pandemic and related economic downturn will negatively affect the overall finances of state and local governments," said Joshua Franzel, SLGE president and CEO, in a news release. "Given the differences in revenue structures, intergovernmental transfers, access to capital and overall service and programmatic responsibilities, it is likely that there will be both similarities and differences regarding impacts on states vs. localities." James Comtois, *Pension & Investments*, [www.pionline.com](http://www.pionline.com), August 18, 2020.

## **2. ONLY 1 IN 5 OF THE 143 LARGEST PUBLIC PENSIONS IS STRONG:**

Only one in five of the 143 largest statewide public retirement systems in the U.S. are resilient, a new analysis published by the bipartisan nonprofit Equable Institute shows.

Public sector funding peaked in 2001, with nearly 3 out of 4 statewide plans 90 percent funded or better. By 2020, one in five statewide plans have a "resilient funded" status. The report, "State of Pensions 2020," analyzes trends in public pension funding, investments, contributions, cash flow and maturation of retirement systems that had more than \$1 billion in assets through 2019.

The current estimated funded ratio for 143 statewide plans is 67.9 percent, near the lowest point in modern history. And five states – California, Illinois, New Jersey, Pennsylvania and Texas – account for more than 50 percent of unfunded liabilities. The institute, which works with public retirement system stakeholders to solve complex pension funding challenges, found that nationally, public pension funding has been in decline since 2001. Despite the decade-long bull market, the recession following coronavirus shutdowns leave them in a worse position than the Great Recession did.

State and local public employee retirement systems in the U.S. manage over \$4.3 trillion in public pension fund investments, according to Pew Charitable Trusts. Returns on these assets account for more than 60 cents of every dollar available to pay promised benefits, it found in a December 2019 report.

"About three-quarters of these assets are held in what are often called risky assets – stocks and alternative investments, including private equities, hedge funds, real estate, and commodities," the Pew report said.

Research by The Pew Charitable Trusts found that since the Great Recession, public pension plans have lowered return targets in response to changes in the long-term outlook for financial markets. Pew analyzed the 73 largest state-sponsored pension funds, which collectively manage 95 percent of all investments for state retirement systems. The average assumed return for these funds was 7.3 percent in 2017, Pew found, down from over 7.5 percent in 2016 and 8 percent in 2007 just before the downturn began.

"The pension asset shortfall for statewide plans keeps growing," the Equable Institute report states. "At the end of 2019, there was no net recovery from losses during the Great Recession and Financial Crisis." The institute estimates that unfunded liabilities will grow to \$1.62 trillion in 2020, up from \$1.35 trillion in 2019, and from \$1.16 trillion in 2009.

"One of the most concerning findings from the report is a trend toward rapidly expanding net negative cashflows, as a result of plan maturation," the report states.

"Although contribution rates have progressively increased (a positive trend from the perspective of plan funding), benefit payments are also growing steadily (because of increased retirements), resulting in a net negative cashflow of -\$113 billion for 2019," it continues. Because the trend has steadily worsened since 2009, the institute says it will be increasingly difficult for governments to invest their pension plans back to health.

If assumed returns had kept pace with declining interest rates since 2001, the institute analysis says, average assumption in 2019 would have been around 5.1 percent. In 2020, the average assumed rate of return is 7.2 percent. "We estimate the average investment return for statewide plans as of June 30, 2020 is -0.44 percent based on the most recent asset allocation reports from each plan," the institute says. "This is 763 basis points below the average 7.19 percent assumed return for the fiscal year."

The report also analyzed unfunded liabilities relative to state GDP and found that states with some of the most visible pension funding challenges, including New Jersey, Kentucky and Illinois, have the largest share of unfunded liabilities relative to their state's GDP, topping 15 percent, respectively. Wire Reports, <https://insurancenewsnet.com/>, August 19, 2020.

### **3. STATE PENSIONS ENTERED PANDEMIC IN WORSE POSITION THAN IN 2008:**

Despite the benefit of the longest-running bull market in US history, new research finds that statewide public pension funds entered the COVID-19 recession in a worse position than they did the Great Recession of 2008.

According to a [report](#) from bipartisan nonprofit Equable Institute, some 80% of public pension funds are not resilient enough to withstand a market downturn in the future. The report defines a resilient pension as one that has a funded ratio of 90% or higher for at least two to three consecutive years. That's a near complete reversal from 2001 when nearly 75% of statewide pension plans had funded levels of 90% or higher.

"These [resilient] plans are generally in a strong position to recover from financial downturns," according to the report, "as funding policy improvements are easier to make when the plan's finances are stable."

The report also estimates that unfunded liabilities for state-managed pension funds will increase to \$1.62 trillion this year from \$1.35 trillion last year, bringing the aggregate funded ratio to "near its lowest point in modern history" at 67.9%.

The report analyzed trends in funding, investments, contributions, cash flow, and maturation for 143 of the largest statewide retirement systems with at least \$1 billion in accrued liabilities in all 50 states.

"For state leaders to understand the best ways to navigate their retirement system challenges in the age of COVID-19, it is critical to understand the trends for pension systems following the Great Recession," said Anthony Randazzo, Equable's executive director and co-author of the report. "There are lessons about what policies should be avoided, and what some states did to break from the pack and recover before this most recent economic downturn."

The report found that five states--California, Illinois, New Jersey, Texas, and Pennsylvania--account for more than half of the public pension unfunded liabilities in the US with an estimated \$693 billion in unfunded liabilities. The California Public Employees' Retirement System (CalPERS)'s unfunded liabilities of \$161 billion alone accounted for 12% of the total statewide pension plan funding shortfall in the US, while the Illinois Teachers' Retirement System (TRS)'s unfunded liabilities of \$81 billion are larger than nearly any other state's funding shortfall.

Because of the market volatility caused by the COVID-19 pandemic, half of the plans with a funded status greater than 90% at the end of last year slipped into what the report calls

a “fragile position,” which means the plans are between 60% and 90% funded. Another 12 plans moved from fragile to “distressed funded status,” which means their funded levels are below 60%.

Equable also found that states and pension boards have failed to lower “overly optimistic” assumed rates of investment return to match the pace of falling interest rates. It said that if assumed rates of return had kept up (or down) with declining interest rates since 2001, the average assumption in 2019 would have been around 5.1%, but instead it is 7.2%.

“The slow pattern of assumed return reduction relative to interest rates has tacitly meant pension funds are taking on risk,” the report said. “The growing gap between interest rates and assumed rates of return reflects as an increased amount of risk that pension funds are accepting.”

There was also a net negative cashflow of \$113 billion for 2019, according to the report. Despite contribution rates having risen in recent years, increased retirements mean benefit payments are also growing. The report said this decadelong trend will make it hard, or even impossible, for pension funds to find their way back to fiscal health though investing alone.

“We do not expect these negative trends will reverse without some intervention,” the report said. “Pension funds will not be able to invest their way out of the shortfall relative to growing promised benefits.” Michael Katz, Chief Investment Officer, [www.ai-cio.com](http://www.ai-cio.com), August 20, 2020.

#### **4. NEW LEGAL PRECEDENT SET FOR PUBLIC PENSION POLICY:**

The Washington Pension Funding Council recently [voted to maintain](#) a 7.5 percent assumed rate of growth for pension investments to ease financial pressure on the state and public employers which must both contribute to those plans. In Oregon, state lawmakers last year adopted a radical new approach to addressing its financial obligations by taking a portion of employee defined contributions in hybrid plans and using it to cover part of the employer-funded side.

The 2019 state law was challenged by several Oregon public employees, but was [upheld by the Oregon State Supreme Court](#) this month, setting a new precedent regarding public pension policy. The move by the Oregon state legislature also reflects the health of its public pension system compared to Washington state’s, though some analysts say that could change.

Under the 2019 Oregon state law, employees making \$30,000 or more a year and enrolled in a Public Employees' Retirement System (PERS) plan must contribute 2.5 percent of their salary to a stability account to offset unfunded parts of the employer contributions. Their remaining 3.5 percent salary contribution would still pay for their individual plan.

Ryan Frost is a policy analyst for the Reason Foundations' Pension Integrity Project. In an email, he wrote that the new Oregon high court ruling "seemingly created a court-validated playbook for any state that has underfunded pensions, and is currently using a hybrid benefit design for current members. That playbook is to steal contributions made by members to their DC (defined contributions) accounts to cover the rising costs of DB (defined benefits) pension debt.

The policy is intended to help curb the costs for 906 Oregon public employers that must contribute to pension funding. While most of Washington's pension system uses a 7.5 percent assumed rate of growth, Oregon currently uses a 7.2 percent rate. Oregon's unfunded liability is also much greater than Washington's, which [dropped from \\$12.6 billion in 2016 to \\$8 billion](#). Oregon's [unfunded liability is currently at \\$27 billion](#) and isn't expected to reach Washington's level until 2037.

Washington State Deputy Actuary Lisa Won told Lens that the organization doesn't comment on other state's pension policies, but noted that the only unfunded liabilities currently in Washington state's system are for PERS Plan 1 and Teachers' Retirement System (TRS) Plan 1, legacy retirement plans that were closed in the 1970s. Washington was the first state to offer hybrid plans, where both the employee and employer put money into the pension.

However, Washington's unfunded liability could go up if the long-term growth rate was below 7.5 percent, or if the state adopted lower growth assumptions without increasing employer contributions. State Actuary Matt Smith has twice recommended lowering the rate to 7.4 percent. Last month he told the Pension Funding Council that the state can either increase investments into the system now or have an even greater financial liability in the future.

"While WA's pensions are relatively healthy outside of the legacy Plan 1's, the continued budgetary pressures exacerbated by Covid-19 could lead to this type of scenario playing out in the future," Frost wrote. "We have already seen cost-saving measures enacted this month by the Pension Funding Council, who failed to adopt an accurate investment return assumption to save the state and employers money this upcoming biennium."

The effects of the ongoing recession and economic shutdown due to COVID-19 also won't be known until the 2023-25 biennium, when a 1989 state law requires TRS Plan 1 and PERS Plan 1 be fully funded. Employer contribution rates are also scheduled to decrease for all but two pension plans starting in the 2023-25 biennium.

The financial burden of the pension system could also grow if the ratio between active employees and retirees changes, though the State Actuary's Office projects it will remain between 1:3-1:15 through 2050. Currently, there are 330,000 active employees in Washington's pension system compared to 190,000 retirees.

State Office of Financial Management Director David Schumacher declined to comment for the story. Pension Funding Council members Sen. Braun (R-20), Rep. Drew Stokesbary (R-31) and Sen. Christine Rolfes (D-23) did not respond to requests for comment. TJ Martinell, <https://thelens.news>, August 19, 2020.

#### **5. DESPITE PANDEMIC, RETIREMENT SAVING STAYS STEADY:**

Though the COVID-19 pandemic has brought about economic stresses, Americans continued to save for retirement at a steady clip in the first half of the year, according to research published Wednesday by the Investment Company Institute.

Preliminary estimates indicate that only 2% of defined contribution plan participants stopped contributing to their plans in the first half of 2020, a typical rate for most of the 12 years ICI has tracked the data, according to its study "[Defined Contribution Plan Participants' Activities, First Half 2020](#)."

In the first half of 2009, another period of financial stress, 4.6% of DC plan participants stopped contributing and in the first half of 2019 the figure was 1.3%.

Withdrawal activity for DC plans remained low in the first half of year, although it was up slightly compared to the same period last year. In the first half of 2020, 2.8% of DC plan participants took withdrawals, compared with 2.5% in the first half of 2019, the report found.

Moreover, levels of hardship withdrawal activity were low: 1.1% of DC plan participants took hardship withdrawals in the first half of the year, the same share of participants as in the first half of 2019.

"These data reflect the long-term mindset of retirement savers," said Sarah Holden, ICI

senior director of retirement and investor research, in a news release. "We see a slight increase in withdrawal activity following the onset of economic volatility and hardship, but the increase is much smaller than you might expect, given the severity of the COVID-19 economic downturn."

The data also showed 2.9% of DC plan participants took a coronavirus-related distribution in the first half of the year, according to record keepers surveyed. The Coronavirus Aid, Relief, and Economic Security Act, known as the CARES Act, which Congress passed in March, provides penalty relief and increased flexibility in retirement plan withdrawals for individuals affected by COVID-19.

With coronavirus-related distributions now on the table, DC plan participants' loan activity edged down in the second quarter of 2020, the study found. At the end of June, 15.6% of DC plan participants had loans outstanding, compared with 16.3% as of March 31 and 16.1% on Dec. 31.

The ICI study tracks contributions, withdrawals and other activity in 401(k) and other DC retirement plans, based on DC plan record-keeper data covering more than 30 million participant accounts in employer-based DC plans as of June 30. Brian Croce, *Pension & Investments*, [www.pionline.com](http://www.pionline.com), August 19, 2020.

## **6. RETIREMENT LIVING: HERE'S WHAT IT COSTS TO RETIRE COMFORTABLY IN EVERY STATE:**

One of the reasons that many Americans get up and go to work every day is to put some money away for [retirement](#). While [Social Security](#) payments can be a helpful financial foundation in retirement, it is often not enough to cover anything but the most basic expenditures, especially in the uncertain financial times wrought by the coronavirus pandemic.

Based on average annual spending for American seniors and the national average life expectancy at age 65 of 19.4 years, the average American will spend about \$987,000 from retirement age on. And those hoping for a more comfortable and financially secure retirement should plan on saving a little more.

Of course, both cost of living and life expectancy vary considerably by state – and so, too, does the cost of retirement. Using the average annual spending of Americans 65 and older – adjusted at the state level for cost of living and life expectancy – 24/7 Wall St. calculated what it will cost to retire comfortably in each state. All data used in the ranking came from the Bureau of Economic Analysis, the Bureau of Labor Statistics, and

the [Institute for Health Metrics and Evaluation](#), an independent global health research center at the University of Washington.

One of the best ways to prepare financially is through retirement-specific accounts, such as IRAs or 401(k)s. These types of funds offer special tax benefits and often come with employer matches. Those who fail to save enough and take advantage of options like these – or draw from them before they hit retirement age – may have to work past age 65 in order to pay the bills. [Here is what you can do if COVID-19 is threatening your retirement.](#)

Just how much one needs to save to comfortably meet expected spending from age 65 on depends on a number of factors. Many who work in the public sector, for example, may benefit in retirement from regular pension payments, in addition to Social Security. The amount of these pension payments vary by state and employer. Even in some of the most expensive places to retire, state subsidies can help finance the cost of retirement. [These are the states spending the most to fund their residents' retirement.](#) Following is the estimated retirement spending for Florida.

#### **Florida:**

- **Est. total retirement spending:** \$1,194,451 (9th most)
- **Avg. cost of living:** +0.6% more than avg. (15th highest)
- **Avg. monthly homeownership cost for senior citizens:** \$494 (21st highest)
- **Pop. 65 and older:** 20.5% (2nd highest)

Florida's warm climate makes it an ideal location for many Americans to retire. In fact, more than one in every five residents of the Sunshine State are 65 or older, the second largest share of any state in the country. Residents who are 65 in the state are expected to live to an average of just over 85, about a year longer than the national average.

Due in part to the higher life expectancy, the estimated retirement costs in Florida are \$1,194,451, greater than the \$1,134,687 national average.

#### **Methodology**

To determine what it costs to retire comfortably in every state, 24/7 Wall St. calculated the amount of money needed to last the average retiree for the rest of his or her life using data from the Bureau of Labor Statistics, Bureau of Economic Analysis, and the Institute for Health Metrics and Evaluation. Our calculation was based on the average annual expenditure for U.S. residents 65 years and older in 2018 – \$50,860 – according to the BLS Consumer Expenditure Survey. We adjusted that figure by local cost of living, using

state-level data on regional price parity in 2017 from the BEA, and multiplied the result by 115% in order to reflect greater financial stability and comfort in retirement.

Finally, to determine the amount needed to last the average retiree for the rest of his or her life, we multiplied the adjusted annual expenditure figure by the number of years residents are expected to live at age 65, using state-level data from the IMHE's Global Health Data Exchange for 2017.

Data on the share of the population that is 65 and over, the mean annual earnings for 65+ households, the share of 65+ households with earnings, the 65+ homeownership rate, and homeownership costs came from the U.S. Census Bureau's 2018 American Community Survey. All data are for the most recent period available. *To view the entire list for all the states click [here](#).* Michael B. Sauter, *USA Today*, [www.usatoday.com](http://www.usatoday.com), August 17, 2020.

## **7. THE COMPANY RETIREMENT MATCH REMAINS THE NORM DESPITE CORONAVIRUS RECESSION:**

The overwhelming majority of companies offering matching contributions to their employee retirement plans have continued putting money on the table to help their workers save for retirement during the [coronavirus](#) downturn.

Only 11 percent of employers suspended their company match in the second quarter, according to the latest retirement savings trend report from Fidelity Investments.

As the spread of the novel coronavirus began to affect the economy earlier this year, many companies, forced to close and send employees home, [suspended](#) or reduced matching contributions to their employee retirement plans. Amtrak, citing an [unprecedented loss of ridership and revenue](#) because of the pandemic, suspended its 401(k) match.

During the Great Recession, many companies reduced or suspended matching contributions.

Financial experts often chide workers for not contributing at least enough to workplace retirement plans such as a 401(k) account to get the maximum match offer by their companies. Fidelity said the most popular match formula for the plans it manages is a 100 percent match for the first 3 percent of employee contributions, and then a 50 percent match for the next 2 percent. About 40 percent of 401(k) plans use this formula, according to Fidelity.

More than three-quarters of workers received an employer contribution in the second quarter. The average employer contribution was \$1,080.

“The company match can help drive participation in a workplace savings plan while providing employees with a savings goal to aim for, so we are encouraged to see that the majority of our clients continued to provide this important retirement savings benefit,” said Kevin Barry, president of workplace investing at Fidelity.

Among employers who suspended the company match, 32 percent said they plan to reinstate the benefit within the next year and 48 percent have plans to restore their matches as soon as corporate finances improve, according to the Fidelity report. Only 6 percent said they have no plans to go back to matching employee contributions.

The report also found that many retirement plan investors weren’t scared off by the volatility in the stock market. Eighty-eight percent of workers contributed to their 401(k), dropping only slightly from last quarter’s record high of 89 percent, Fidelity reported.

Just under 1 percent of 401(k) investors stopped their retirement contributions, and 9 percent increased their contribution rate.

If you can afford it, consider increasing your own contributions if your employer has suspended its match. Michelle Singletary, *The Washington Post*, [www.washingtonpost.com](http://www.washingtonpost.com), August 17, 2020.

#### **8. PENSION DEBT EXPECTED TO SURGE DUE TO COVID-19 VOLATILITY:**

Underfunded defined benefit (DB) pension plans can expect to see their liabilities surge over the next several months due to volatility from the COVID-19 pandemic. According to research from Moody’s Investors Service, companies are on pace to see a 6% increase in total adjusted debt in 2020 as modest asset returns fail to offset tumbling discount rates.

Moody’s said in a recent report that 2020 has so far “proved to be a roller coaster ride” for the two drivers of pension funding: the discount rate and the return on plan assets.

It noted that the discount rate has plunged 96 basis points (bps) to an all-time low of 2.26% as of the end of July, while asset returns have had monthly swings from being down 5% in March to a high of being up 2% in July relative to their fair market value at the end of 2019.

The report also said that the transportation and auto industries lead the list of companies

with legacy pension exposure that have also been affected by the pandemic. The top four companies in these two industries are American Airlines, Delta Airlines, Ford Motor Company, and General Motors.

Moody's noted that many of the larger corporate pension plans have calendar year-ends, and that pension disclosures are updated on an annual basis and included in a company's year-end filing.

"The world has vastly changed since Dec. 31, which means disclosed pension funding levels may not be recognizable when Dec. 31 Form 10-Ks are filed," according to the report.

The report also said that the "playing field for corporate plan sponsors will change once again" due to the Coronavirus Aid, Relief, and Economic Security (CARES) Act, a more than \$2 trillion economic stimulus bill that was signed into law in March. It said it expects many companies will take advantage of a provision of the CARES Act that allows plan sponsors to delay contributions that would have been due during calendar year 2020 until January 2021.

"Though the delay of these contributions will provide near-term cash flow relief for plan sponsors," said the report, "interest expense will be accrued at the plan's effective interest rate on these delayed payments, beginning on their original due date."

In the report, Moody's also noted that multiemployer pension plans (MEPPs) "are dangerously underfunded" due to a lack of regulation and a sharp drop in the number of companies participating in the plans.

"Many plans are now past a point where companies that contribute to these funds can cure the overall underfunding," said the report. "While MEPP reform has been proposed many times in the US Congress, there has been little headway within the House and Senate."

In the meantime, it said, the top 50 companies by multiemployer pension plan contribution "are seeing year-over-year growth in contributions that continue to be a drain on operating cash flow." Michael Katz, Chief Investment Officer, [www.ai-cio.com](http://www.ai-cio.com), August 17, 2020.

**9. PUBLIC PENSION FUNDING AND REFORM - OR LACK THEREOF - WHEN WE'RE NOT 'ALL IN THIS TOGETHER':** Regular readers [will know the story by now](#): the governors and legislators in charge of worst-of-the-worst underfunded public pension

plans -- Illinois, Kentucky, New Jersey, and Connecticut, each with a funded status hovering around 40% -- face a likelihood of funding levels worsening even more as they make their way through the corona-recession.

In one respect, the pension funding situation is not as bleak as it might have been: when the U.S. stock market crashed in March following the realization that we would not be spared in the coronavirus pandemic, the funded status of the nation's public pensions plans crashed -- or, at any rate, dropped considerably -- along with it. According to [Milliman's Public Pension Funding Index](#) (PPFI), funded ratios dropped from 74.9% down to 66% from year-end 2019 to March 31, 2020. As it turned out, of course, the stock market recovered -- for now, at least -- and the PPFI stands at 71.2%, the same level as it was on March 31, 2019.

But the stock market is only part of the picture. Illinois' revenue projections as of May 20 project a 12% tax revenue drop. Their response? Not budget cuts, certainly not a willingness to reconsider pension reform -- only borrowing and the hope for federal cash. New Jersey -- anticipated revenue drop 18% — has indeed cut spending and is also deferring indefinitely its scheduled pension contributions. Connecticut, which predicted an 11% revenue drop on April 30, is likewise business-as-usual, except without embarrassing its residents [by making an unseemly bailout request](#). And none of these states' leaders have found it even worth discussing, to talk about pension reform. (See the National Conference of State Legislatures for [revenue projections](#) and [state actions](#), as well as my [July article on the topic](#).)

Which brings me to a [webinar last week](#) sponsored by NIRS, the National Institute on Retirement Security, to revisit some of their take-aways from a 2011 report on the Great Recession, "[Lessons from Well-Funded Public Pensions: An Analysis of Six Plans that Weathered the Financial Storm](#)." In that report, they profiled six comparatively well-funded pension plans; in the webinar, they brought together experts from three of those plans, the statewide retirement systems for New York, Idaho, and Wisconsin.

Some of the characteristics of these plans are straightforward. For instance, they are more likely to have a small COLA, or at the discretion of the legislature, rather than Illinois' guaranteed 3% compounded COLA. They also consistently make the Actuarially Determined Contribution, year after year -- which means, of course, that there is no need for more burdensome catch-up contributions later on. (For example, one of the plans profiled in the original report, the Illinois Municipal Retirement Fund, is well-funded because the state compels municipalities to make their required contributions.)

But there's another key, as identified by Bob Conlin, representing the 99% Wisconsin Retirement System, and that's culture. Recall that the [Wisconsin system](#) involves risk-sharing: each year's employee contribution (not just employer contribution) varies based on the requirements due to the funded status/funding method, and retirees' benefits are adjusted up or down based on investment returns. And here are Conlin's comments (my transcription based on the [audio recording](#)), after some preliminary words on the importance of educating participants on how their benefits work, and being asked, "Do you attribute a part of your success to a healthy culture?"

"The shared risk system . . . has been fully engrained where taxpayers and employees and retirees are kind of all in this together, and that kind of goes with the communication aspect of it, but it's been a cultural phenomenon. It's a little bit different than a lot of public plans, and I think over the years we have been communicating more about that, and it has kind of created a, I think, a Wisconsin ethos around our public pension system that folks are touting. They like it, they understand there's risk with it, that retirees could actually see their pensions go down a bit, yet they're still supportive of that because in good times, they also share in that as well, so it is a cultural thing.

"People often ask, 'so can't we import the Wisconsin model into our systems?' And I -- well, there are certain things you can do, there is a cultural component to it I think that takes some breeding and some cultivation to develop over time."

Now, observing Wisconsin from across the border, there certainly appears to be more of a sense of solidarity and common culture among Wisconsinites than in Illinois. Cheese, beer, the corner tavern, the Packers, a [label for Illinoisans coming north](#) which, if written out, couldn't be printed in a family paper. Kenosha was the subject of a ["parachute-journalism" style article](#) at *Harper's Magazine*, which tried to find blue-collar union activism but missed Kenosha's car culture, typified by the summer car shows (well, cancelled this summer). Perhaps that's missing serious divisions not apparent to the outsider, but that raises the question of whether a state like Illinois with its long legacy of corruption, of unions and machine politicians in it for themselves, and, quite honestly, without any "glue" that holds it together, is simply incapable of implementing a retirement system that requires an "all in this together" attitude.

How do you get from here to there? So far, Illinois hasn't figured that out, and its leaders (who are busily promoting a constitutional amendment enabling a graduated income tax, by labelling it a "fair tax" and claiming only the very rich will be affected) don't really seem to have recognized how important this is in the first place. Elizabeth Bauer, Forbes, [www.forbes.com](http://www.forbes.com), August 23, 2020.

## 10. WHY TAKING SOCIAL SECURITY EARLY COSTS TOO MUCH:

Starting Social Security early typically means getting a smaller benefit for the rest of your life. The penalty is steep: Someone who applies this year at age 62 would see their monthly benefit check reduced by nearly 30%.

Many Americans have little choice but to accept the diminished payments. Even before the pandemic, about half of retirees said they quit working earlier than they'd planned, often due to job loss or health issues. Some have [enough retirement savings](#) to delay claiming Social Security, but many don't. And now, with unemployment approaching Depression-era levels, claiming early may be the best of bad options for older people who can't find a job.

But the penalty for early filing, and the bonus for delaying your application, are based on old formulas that don't reflect gains in life expectancy, says economist Alicia Munnell, director of the Center for Retirement Research at Boston College. The result is a system that unfairly penalizes early filers, unjustly benefits late filers " and hurts lower-income people the most.

'Low-income people disproportionately collect benefits at 62 and their benefits are cut too much, and high-income people disproportionately delay claiming till 70 and their benefits are increased too much,' Munnell says. 'So you penalize the low-income and you benefit the high-income.'

### The problem started off as a solution

Originally, Social Security had one retirement age: 65. In 1956, Congress authorized a reduced benefit for women, to allow them to retire [at the same time as their typically older husbands](#). The reduced benefit option was extended to men in 1961.

The amount of the reduction was meant to be 'actuarially neutral,' so that the cost to Social Security would be the same whether those with average life expectancies claimed the smaller check earlier or the larger check later.

As life expectancies rose, though, early filers wound up living with the penalty for longer. In 1956, a 65-year-old woman had an average life expectancy of 16.9 years. Today, it's 21.6 years, Munnell says. Instead of being actuarially neutral, in other words, the current system results in early filers with average life expectancies getting less.

On top of that, Social Security [offers a bonus](#) for those who can afford to wait. A 1%

delayed retirement credit was introduced in 1972, and the amount was increased over the years to the current 8%. So each year you put off claiming Social Security past your full retirement age adds 8% to your payment. Full retirement age varies according to birth year and is 67 for people born in 1960 or later.

Let's say your full retirement age is 67 and your benefit, if started then, would be \$1,000 a month. Starting at 62 would shrink the benefit to \$700, while waiting until 70 to begin would boost the amount to \$1,240.

The longer you live, the more you can benefit from a delayed filing" and the higher your income, the longer you're likely to live. In fact, most of the gains in life expectancy in recent years have accrued to higher-income people.

Between 2001 and 2014, for example, life expectancy rose by more than two years for men and nearly three years for women with incomes in the top 5%, according to a study for the Social Security Administration. During the same period, life expectancies for those in the bottom 5% of incomes rose a little less than four months for men and about two weeks for women.

#### **How benefits could change to be fairer**

To restore actuarial fairness, the penalty for early filing should be lower, Munnell says. Someone who retires at 62 instead of 67 should get 22.5% less, rather than 30% less. Similarly, the bonus for waiting should be reduced to just below 7% per year.

'The way it's set up now, people will get 124% of their full benefit if they wait till 70 and they really should only get 120%,' Munnell says.

Obviously, Social Security has bigger problems. Once its trust fund is depleted, as projected in 15 years or so, the system will be able to pay only 79% of promised benefits in 2035. That proportion is estimated to drop to 73% by 2094.

When Congress finally gets around to fixing the system, Munnell says, it should consider making the payouts more fair.

'I think there'll be some grand bargain on Social Security at some point because I don't think anybody's really going to allow benefits to be cut 25%,' Munnell says. 'This [actuarial fairness] probably should be put on the agenda.' Liz Weston, [www.goerie.com](http://www.goerie.com), August 20, 2020.

## **11. TAX MISTAKES IN 2020 THAT COULD RUIN YOUR RETIREMENT:**

Assuming you still have some form of income, tax planning does not end once you retire. The Internal Revenue Service (IRS) will always expect you to pay taxes on your retirement income. For those who are well prepared to maintain their standard of living in retirement, many find their tax bills are similar to when they were working full time. Some of you may even find you are paying more in taxes; this is common for retiring business owners.

As the saying goes, nothing is certain except death and taxes. How can you make the most of your retirement investments and keep more of your hard-earned retirement income from getting sucked up by taxes? First, take the time to do the necessary tax planning to avoid the following retirement income tax mistakes that can drastically reduce your financial security as you age. Making tax-smart moves can help you get the absolute maximum enjoyment from your retirement income. Ignoring these retirement tax mistakes could lead to both paying more in taxes and running out of money earlier than necessary.

### **Retirement Tax Mistake #1: Assuming Your Taxes Will Be Lower in Retirement**

Even if they were able to live tax-free, most Americans are not prepared financially to maintain their standard of living in retirement. Still, many assume their taxes will be lower once they leave the workforce. Those who do end up paying fewer taxes in retirement often do so by simply having a smaller retirement income, which is not likely the dream retirement.

After suffering through nearly four years of the Trump Presidency, we are in the midst of a global pandemic, and the national debt has skyrocketed. Tens of millions of Americans are out of work. Thousands of baby-boomers are reaching retirement age, leaving the workforce, and moving onto rolls of government programs like Social Security and Medicare. We have known for decades that changes will need to be made to keep these expensive government programs solvent. It is hard to see how that will happen without taxes being raised at some point in the future. As a financial planner, I know that cutting benefits would be untenable, politically, and devastating for the millions of retirees who rely on Social Security to meet their basic needs.

On a brighter note, Americans have saved trillions of dollars into tax-deferred retirement accounts like a 401(k) or IRA. Keep in mind that taxes will be due once funds are withdrawn from those accounts. If tax rates increase, you may have similar, or even [higher, tax bills in retirement](#).

### **Retirement Tax Mistake #2: Not Planning for Taxes on Social Security**

Have you ever heard of provisional income? I'm guessing most of you said, "No." Provisional income is what the IRS uses to determine whether or not your [Social Security benefits will be taxed](#). Yes, Social Security income can be subject to taxation from the IRS.

For those with distributions from retirement accounts like an IRA or 401(k), they count as part of your provisional income. These distributions are added to any 1099 forms you receive from your taxable investments and to one-half of your Social Security benefits for the year. If that income totals more than \$34,000 for singles or \$44,000 for a married couple, filing jointly, a whopping 85% of your Social Security benefits will become taxable at your highest marginal tax bracket.

Talk to your financial planner to determine whether you will be above those relatively small retirement-income numbers in retirement. There are a variety of ways to strategically minimize the taxes on your Social Security benefits. Lumping IRA withdrawals into one year and diversifying your retirement savings into taxable and non-taxable accounts are a couple of ways. Higher earners (above \$200,000 per year) may want to check out the [Rich Person Roth IRA for even more tax-free income in retirement](#).

### **Retirement Tax Mistake #3: Not Contributing to Roth IRAs and Roth 401(k)s While Eligible**

The contribution limit for a Roth IRA is just \$6,000, per year, in 2020. For the average American, only saving that amount each year, and only having one type of retirement account, will most likely not be enough savings for retirement. Yes, you read that right. Solely contributing the maximum amount of \$6,000 each year into a Roth IRA will not likely grow enough to help you achieve financial independence. Luckily, there is now a Roth 401(k) option with an annual \$19,500 contribution limit. However, your employer has to offer this option as part of the employee benefits package.

Many of you reading this will likely make too much money to contribute to a Roth IRA. Married couples making more than \$203,000, per year, in 2020 are not eligible to contribute to a Roth IRA at all.

Some of you might be asking, "Why is ignoring a Roth IRA a problem?" The reason is that having both a Roth IRA account and traditional IRA or 401(k) allows you to diversify some of your tax-rate risk in retirement. If you have a big-income year, or taxes are higher in one year, you can pull more money from the Roth (tax-free withdrawals) and less from the 401(k) (taxable withdrawal).

#### **Retirement Tax Mistake #4: Ignoring Taxes All Together**

Have you ever looked at a retirement calculator, or projection, and said, “I could live off that amount of retirement income.”? Perhaps you did not realize that the retirement income estimate was before taxes? This problem is easy to fix when you are years away from retirement. When you have already left the workforce, it will be much harder to make up the difference. It is essential to point out that for those with large retirement nest eggs, federal taxes can be as high as 37% (current tax rates for 2020).

Additionally, state taxes can also be high. California’s tax rate is 13.3%. States with lofty tax rates often cause people to ask themselves, [“Should I move from my high-tax state after I retire?”](#)

#### **Retirement Tax Mistake #5: No Strategy to Minimize Taxes**

For retirees relying solely on Social Security, there is not much tax planning needed. For everyone else with higher retirement incomes, a penny saved is a penny earned, as the saying goes. Be proactive with tax planning. That will help you keep more of your hard-earned money out of Uncle Sam’s hands. If you need a little push, contact a [Certified Financial Planner](#) who can help you develop a strategy to minimize taxes.

#### **Retirement Tax Mistake #6: Taking Withdrawals from your retirement accounts in the Wrong Order**

Throughout this article, we have been talking about putting off taxes as long as possible and how to minimize taxes in retirement. This often leads people to spend down their post-tax investment accounts first, in retirement. This can lead many to feel like they have more money than they do. Without taxes being due on withdrawals, you will take home more money from a post-tax investment account compared to IRA or 401(k) accounts.

You may see your net worth continues to grow even after withdrawals. That has been especially true over the last few years of the bull market. If that has been the case, you could be sitting on a tax time bomb. Once the post-tax money is gone, all your retirement income will be taxable (assuming funds are held in IRA or 401(k) accounts). You will have little to no options to minimize taxes once that happens.

While it is a bit more complicated, most people will benefit from taking some money from accounts like a 401(k) now. Yes, you would pay taxes when you withdraw the money, but the goal would be to minimize taxes over your entire retirement while paying as little as possible on each withdrawal.

Bottom line - Do not forget about taxes when planning for retirement. A little proactive tax

planning will help you earn income in your golden years as efficiently as possible. Also, you want to pay the least amount of taxes as possible so you can keep as much of your hard-earned money as you can. David Rae, Forbes, [www.forbes.com](http://www.forbes.com), August 23, 2020.

## **12. IRS - 50,000 SPOUSES TO GET CATCH-UP ECONOMIC IMPACT PAYMENTS:**

The Internal Revenue Service will soon send catch-up Economic Impact Payment checks to about 50,000 individuals whose portion of the EIP was diverted to pay their spouse's past-due child support.

These catch-up payments are due to be issued in early-to-mid-September. They will be mailed as checks to any eligible spouse who submitted [Form 8379](#), Injured Spouse Allocation, along with their 2019 federal income tax return, or in some cases, their 2018 return. These spouses do not need to take any action to get their money. The IRS will automatically issue the portion of the EIP that was applied to the other spouse's debt.

The IRS is aware that some individuals did not file a Form 8379, Injured Spouse Allocation, and did not receive their portion of the EIP for the same reason above. These individuals also do not need to take any action and do not need to submit a Form 8379. The IRS does not yet have a timeframe but will automatically issue the portion of the EIP that was applied to the other spouse's debt at a later date.

Affected taxpayers can check the status of their Payment by using the [Get My Payment tool](#), available only on IRS.gov. For more information, see the Receiving My Payment section of the Frequently Asked Questions in the [Economic Payment Information Center on IRS.gov](#). IRS Newswire IR-2020-192, [www.irs.gov](http://www.irs.gov), August 25, 2020.

## **13. EARNING SIDE INCOME: IS IT A HOBBY OR A BUSINESS?:**

Whether it's something they've been doing for years or something they just started to make extra money, taxpayers must report income earned from hobbies in 2020 on next year's tax return.

What the difference between a hobby and a business? A business operates to make a profit. People engage in a hobby for sport or recreation, not to make a profit.

Here are nine things taxpayers must consider when determining if an activity is a hobby or a business:

- Whether the activity is carried out in a businesslike manner and the taxpayer maintains complete and accurate books and records.

- Whether the time and effort the taxpayer puts into the activity show they intend to make it profitable.
- Whether they depend on income from the activity for their livelihood.
- Whether any losses are due to circumstances beyond the taxpayer's control or are normal for the startup phase of their type of business.
- Whether they change methods of operation to improve profitability.
- Whether the taxpayer and their advisors have the knowledge needed to carry out the activity as a successful business.
- Whether the taxpayer was successful in making a profit in similar activities in the past.
- Whether the activity makes a profit in some years and how much profit it makes.
- Whether the taxpayers can expect to make a future profit from the appreciation of the assets used in the activity.

The IRS has many resources to help taxpayers report their income correctly. See the more information section below for additional guidance.

More Information:

[Publication 17](#), Your Federal Income Tax

[Publication 525](#), Taxable and Nontaxable Income

[Publication 535](#), Business Expenses

[Publication 334](#), Tax Guide for Small Business, For Individuals Who Use Schedule C

Share this tip on social media -- #IRSTaxTip: Earning side income: Is it a hobby or a business? <https://go.usa.gov/xfSMK>. IRS Tax Tip-2020-108, [www.irs.gov](http://www.irs.gov), August 25, 2020.

#### **14. A REAL OR FAKE SAVINGS CLUB?:**

Imitation is the greatest form of flattery. It's also the greatest form of "scammy." That's why scammers are imitating a type of informal savings club known as a "sou sou" or "susu" to trick people into joining what amounts to an illegal pyramid scheme.

If you've never heard of the term "sou sou," a quick internet search will tell you that it's a rotating savings club with historic roots in West Africa and the Caribbean. It's a savings arrangement between a small group of trusted people – usually family and friends – who regularly pay a fixed amount into a common fund and take turns getting paid out. In a sou sou, you don't earn interest, never get out more than you paid in, and there's no reward for recruiting people to join. This way of saving is based on the honor system, and it is not without risk.

So, it's not surprising that scammers are pitching fake sou sou savings clubs and opportunities like "[The Circle Game](#)," "[Blessing Loom](#)," "[Money Board](#)". These kinds of illegal pyramid schemes are the exact opposite of a sou sou: They promise you'll make more money than you put in and depend on recruiting new people to keep money flowing into the fund. Like all other pyramids, once they run out of new recruits to bring into the club, the money dries up, leaving everyone waiting for their pay out holding the bag.

If you see a post or get a direct message on Instagram, Facebook, or other social media about one of these clubs, think twice and remember the warning signs. If the offer comes from a friend or family member, tell them about this scheme. And, if you've if you've been contacted to join a fake sou sou, please tell us: [ftc.gov/complaint](https://www.ftc.gov/complaint). Your report can help us protect others from a scam. Karen Hobbs, Assistant Director, Division of Consumer and Business Education, FTC, [www.ftc.gov](https://www.ftc.gov), August 10, 2020.

**15. FOR THOSE WHO LOVE WORDS (LOGOPHILES):**

Alternative facts are aversion of the truth.

**16. EVER WONDER?:**

Why is the man who invests all your money called a broker?

**17. INSPIRATIONAL QUOTE:**

Creativity is intelligence having fun." - *Albert Einstein*

**18. TODAY IN HISTORY:**

On this day in 2008, Barack Obama becomes the first African-American to be nominated by a major political party for President of the United States.

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