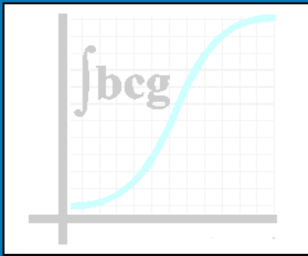

BCG Retirement News Roundup

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Boomershine Consulting Group (BCG) has launched this monthly news roundup of highlighted significant articles from the retirement industry – for clients and friends. Retirement plan news has become increasingly pertinent for many audiences these days, including:

- **Retirement Plan Sponsors – addressing both private and public sector issues**
- **Employers – dealing with complicated decision making for their plans**
- **Employees – educating the Boomer generation that is nearing retirement**
- **Industry Practitioners - helping to understand and resolve today's significant challenges**

We review numerous industry news services daily and will include a collection of timely and significant articles each month concerning compliance, actuarial plan costs (including assumption debates), plan design change issues and benefit trends, as well as other related topics.

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Public Sector/Government Plans

Settlement fails in Rhode Island pension overhaul

A proposed settlement that would have ended the legal fight over Rhode Island's 2011 landmark pension overhaul has been rejected, and a judge has ordered the parties back into mediation.

Lawyers for the unions and retirees who sued said Monday the proposal was rejected by police union members.

The overhaul has been a model for other states seeking to rein in runaway pension costs. The outcome marks a defeat for Gov. Lincoln Chafee (CHAY'-fee) and Treasurer Gina Raimondo (ray-MAHN'-doh), who argued it was a good deal for all parties and preferable to continued costly litigation.

The proposal was an attempt to resolve lawsuits filed by public-sector unions and retirees.

The balloting was for members of the unions and retiree coalitions. Six groups had to approve the deal, and the police group did not.

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Public Pensions and the Lessons of Success

Some state and local retirement systems have found a formula for stability.

Do we learn more from success or failure? When it comes to state - and local - government pensions, we tend to focus on the plans that are struggling. But there are valuable lessons to learn from public-sector retirement plans that have remained well funded and from governments that have successfully negotiated changes to put their pension systems on a path to full funding.

Well funded in Illinois: Given all the headlines about Illinois' seemingly endless struggle to reform its pensions, some might be surprised to learn that that the Illinois Municipal Retirement Fund (IMRF), the state's second-largest public pension, is a model of fiscal responsibility.

What distinguishes the IMRF from Illinois' other three statewide plans, which are struggling, is that all 2,969 governments that participate in it are required to pay 100

percent of their annual required contribution. As a result, the IMRF has remained more than 80 percent funded, even after the investment losses that public and private plans suffered from the 2008 recession.

It is also noteworthy that the IMRF is separate from the Illinois state government and its assets are not included in the state's financial statements. (State law does, however, determine employee benefits, including retirement age, employee contributions, vesting period and cost-of-living increases.)

The IMRF maintains fully funded reserves for employees and retirees, has a highly diversified portfolio and assumes a conservative 7.5 percent return on investments, even during periods of stock-market growth. This long-term approach helps the fund ride out market swings.

Navigating change in Georgia: Some governments focus all their attention on costs when they look at pension-plan changes. Because pensions are part of a broader human-resources strategy, it's important to involve employees in the discussions and to consider recruitment and retention issues.

In 2007, Gwinnett County, Ga., decided to take control of its defined-benefit plan, which had been managed by the Association County Commissioners of Georgia. Key drivers of the county's desire for change were to gain control over the county's pension assets and control cost increases.

The county sought to put new employees into a defined-contribution plan. Before making the change, county staff conducted benefit comparison studies, carried out market research to learn what benefits were important to young professionals, and analyzed the short- and long-term costs of closing the defined-benefit plan to new employees. (When a pension plan is closed, the unfunded liabilities are amortized over a shorter period in keeping with sound actuarial principles, and with a fixed group of employees to serve, demographic assumptions must be revised.)

While county staff calculated that closing the defined-benefit plan would be more costly in the short run, the analysis showed long-term cost savings. County commissioners voted to move forward.

Although the costs to service the closed plan were higher than expected due to asset losses from the 2008 economic downturn, the county has continued to make its full annual required contribution. The closed plan was 70.2 percent funded in 2010 and reached the 76.8 percent level in 2012. So far, the county has not experienced any measurable changes in its ability to recruit or retain workers.

Legislating stability in Iowa: Sometimes, as in the case of the Iowa Public Employees' Retirement System (IPERS), state legislation is needed so it is possible to make the full

annual required contribution (ARC). While the IPERS' funded ratio had remained relatively good, it was trending downward.

One problem IPERS had was a statutory required contribution rate that was well below the ARC. It had not been adjusted since 1979. The Iowa General Assembly authorized changes in 2006, 2010 and 2012 to increase the combined employer-employee contribution. Now IPERS has the authority to adjust the contribution rate to an annually adjusted cap and the funded ratio is over 80 percent again. For fiscal year 2014, the required contribution rate is at 100 percent of the ARC.

As these stories illustrate, there's no one-size-fits-all approach to strengthening state and local pension plans. Each has a unique legal framework, and a solution that works for one government may be totally off the mark elsewhere. But while solutions for retirement plans can vary from place to place, there's no debate about the importance of an adequate retirement income for government workers.

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Pace of pension reform ebbs after 49 states change laws

Post-recession focus shifts to making DC plans mandatory

As the flood of reform efforts aimed at public pension funds becomes a trickle, the main concern is whether the newfound fiscal discipline will hold.

While the sense of urgency has diminished, reform attempts have become a legislative staple, as public retirement systems continue to grapple with unfunded liabilities and political pressure to change.

The financial crisis and its aftermath sparked some kind of pension reform in every state except Idaho. Now “it appears to be the slowest pace of reforms since 2008,” said Keith Brainard, Georgetown, Texas-based research director of the National Association of State Retirement Administrators. In a study of 32 plans in 15 states representing 65% of participants in its public plans database, the Center for Retirement Research at Boston College found most already have taken steps to reduce future pension costs by some combination of increasing employee contributions, raising age and tenure requirements, trimming salary calculation formulas used to set pension levels and shrinking or stopping cost-of-living increases.

Surprisingly, while reform debates were often seen as taking a page from the private sector and moving away from defined benefit plans, research due later this spring from the center will show less activity than expected. CRR researchers found that just 15% of

public plan sponsors introduced some form of defined contribution plan after 2008, compared with 20% pre-crisis.

A key distinction of the post-recession approaches to DC plans is their mandatory nature, unlike earlier moves that gave employees the option of having a DC plan. Six states — Georgia, Michigan, Rhode Island, Utah, Tennessee and Virginia — shifted to a mandatory hybrid plan since 2008, while Kentucky and Kansas went the cash balance plan route. Louisiana tried to mandate DC participation but was blocked by the courts after participants sued. Only Michigan and Alaska require new hires to participate solely in a defined contribution plan.

Many of the reforms to date have focused on newly hired workers. Those savings will take longer to realize, "but in the long run these cuts are going to get the costs below what they were before the recession," said Alicia Munnell, director of the retirement research center. "That does take care of the criticism that they can't afford DB."

In terms of reform attempts, the National Conference of State Legislatures found 29 states saw 166 pension bills introduced in 2014 alone, many of which addressed minor changes or proved too controversial to survive. One of the most high-profile reform bids came from Chuck Reed, the mayor of San Jose, Calif., who sought a voter referendum to allow local governments to renegotiate pension benefits for public employees. That bid was defeated in court last month.

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Detroit makes deal with retired cops, firefighters to preserve current pensions

The city of Detroit has reached a deal with retired police officers and firefighters that would preserve current pensions but trim annual cost-of-living payments -- the first major agreement with retirees in the bankruptcy case, mediators announced Tuesday.

The city retreated from an earlier proposed 6 percent cut in pensions and the elimination of the 2.25 percent cost-of-living payment. Leaders of the Retired Detroit Police and Fire Fighters Association, which has more than 6,000 members, endorsed the deal along with creation of a health plan.

A spokesman for Detroit emergency manager Kevyn Orr, who took the city into bankruptcy last summer, didn't immediately respond to a message Tuesday from The Associated Press. More details could be disclosed at the next court hearing Thursday.

"This has been one of the more vocal class of creditors," bankruptcy expert Doug Bernstein said of police officers and firefighters. "Maybe the city is getting some momentum where hopefully the remainder of the case won't be so contentious. That's optimistic. There's going to be good days and bad days, but this is certainly significant."

The agreement still is subject to a vote by retirees as well as current employees who are eligible for a future pension. It also must go through Judge Steven Rhodes as part of Detroit's plan to exit bankruptcy by fall.

"Judge Rhodes will not approve a plan that over-promises," Bernstein said. "They are definitely going to have to back up their numbers."

Finally, the deal is tied to the city getting $816 million from foundations, philanthropists and the state of Michigan. Lawmakers still haven't approved the state's $350 million share, which has been endorsed by Gov. Rick Snyder.

The pot of money would prevent the sale of city-owned art and be earmarked solely for more than 20,000 Detroit retirees who draw benefits from two underfunded pension funds.

The average annual pension for police and fire retirees is $32,000. They would keep about half of their annual cost-of-living payments under the deal announced Tuesday. The reduction could be restored in the future if the fund's finances improve.

The city still is negotiating with other retired workers, although their pension fund is in worse shape. Orr has proposed a 26 percent cut to current benefits; even more if the $816 million rescue falls apart.

Detroit filed for bankruptcy last July, citing $18 billion in unmanageable long-term liabilities. It's the largest public filing in U.S. history.

The city last week settled with holders of $388 million in bonds, agreeing to pay 74 cents for each dollar owed. Separately, the judge signed off on an $85 million agreement that releases Detroit from a disastrous debt deal made years ago that carried high rates of interest.

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Treasury Department starting unit that includes oversight of public pension funds

The Treasury Department is creating an Office of State and Local Finance to coordinate the department's efforts to oversee developments in state and local financial markets, including public pension fund liabilities.

Kent Hiteshew was named the office's first director; he will start in mid-May, according to a Treasury representative. Mr. Hiteshew is currently managing director at J.P. Morgan Chase, responsible for public finance in the Northeast U.S. as well as the bank's housing finance group.

The new office will “support policies to improve the management of public pensions and other liabilities” as well as monitor municipal bond markets and potential federal policy responses to municipal financing issues, the Treasury representative wrote in an e-mail.

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Private Sector

U.S. Senate Extends MAP-21 Discount Rates

The U.S. Senate passed a bill yesterday that delays the phase-out of the pension funding stabilization provisions in the Moving Ahead for Progress in the 21st Century (MAP-21) Act until 2018. The pension provisions were added to the Emergency Unemployment Compensation Extension Act of 2014 (H.R. 3979) to help “pay-for” this extension, a requirement under the Statutory Pay-As-You-Go Act of 2010.

YOUR PRACTICE-Helping clients choose annuities or lump sums

Your client plans to retire soon and his employer's defined benefit plan offers a choice: take a monthly pension or a lump sum distribution that can be rolled over to an Individual Retirement Account. The client wants your input because a good chunk of his net worth is tied up in the plan, not to mention his retirement security.

If his main retirement goal is to be happy, have him take the pension or a similar lifetime annuity. A 2012 report from consultants Towers Watson, "Annuities and Retirement Happiness," found that among retirees of similar wealth and health, those with annuitized incomes were happier than those without annuities.

Any financial adviser worth her credentials would argue that this happiness is likely to be short-lived, though. Rising life expectancies guarantee that even low inflation will eventually erode a pension's purchasing power. Fixed incomes are like aging knees: what works at age 65 won't get you nearly as far at 80.

There's another angle. Pensions don't generate commissions or asset management fees; rollovers do. So how do you help clients make informed decisions and manage the inherent conflict of interest?

SEEING THE NUMBERS

David Kudla, chief executive officer of Mainstay Capital Management LLC in Grand Blanc, Michigan, has worked on numerous pension-or-payout decisions. Many of his clients work for the auto companies, which have offered lump-sum buyouts to tens of thousands of employees in recent years.

For Kudla, the first round of the analysis is a math question. He knows the client's age and life expectancy (and his spouse's, if the client is married) from the IRS tables. The plan provides the pension payments and the available lump sum. Using those numbers, he can back out the discount rate - the internal rate of return - the plan sponsor is using in its calculations.

He then estimates the return the rolled-over lump sump could earn if he were managing it, based on typical historic returns of the various asset classes he would recommend. If the investment portfolio produces a higher value, then it makes financial sense to roll over the funds; otherwise, the pension can be a better choice. Armed with that result, Kudla and the client start to consider the qualitative factors in the decision.

Larry Frank Sr., owner of Better Financial Education in Roseville, California, runs customized spreadsheet calculations to compare annuitized incomes with managed accounts. In an article he co-authored for the April 2014 Journal of Financial Planning, he compared buying a single-premium immediate annuity - a privately purchased pension - to investing in simulated investment portfolios with varying allocations between stocks and bonds.

"We found that for those with normal health and normal longevity expectations, it doesn't make sense to annuitize in most cases," says Frank.

THE CASE FOR ROLLOVERS

The monthly benefit check may be valued for its dependability, but it lacks flexibility. A check for the same amount shows up each month whether or not the client needs the cash - and those benefits typically are considered taxable income. When pension recipients die, the checks stop and their heirs get nothing. In contrast, lump sum distributions turned into rollover accounts allow investment choice, control over income- and tax-timing and more flexible estate planning.

Larger pension payments are also at risk for reduction if the plan goes bankrupt. Beginning in 2014, the Pension Benefit Guarantee Corporation's coverage limit for a 65-year-old retiree is $59,318 annually. Clients taking early retirement face lower age-adjusted limits and payments from supplemental executive retirement plans go on the chopping block, as well.

Kudla has encountered these limits with early retirees from Delphi Corp, which went bankrupt in 2005. "There were people that saw their pension payment get cut by a quarter ... (or) a third for the rest of their life," he says.

BEYOND THE NUMBERS

But it is not just about numbers. Clients' financial goals and risk tolerances vary, and some people find it easier to overlook the slow loss of buying power to inflation than to ignore the stock market's headline-grabbing gyrations.

Both Frank and Kudla say their role as fiduciaries requires them to accommodate clients' preferences, even when they believe a rollover is the better option. Consequently, they'll make their case but will refrain from trying to sell the client on taking the payout.

Kudla's experience with General Motors' buyout offer in 2012 provided a good example of how client feelings play into the whole calculation. Only 27 percent of his clients there took the lump sum; the rest chose to receive a monthly payment.

But their reasons had little to do with the calculations Kudla prefers, and more to do with psychology: During their careers they had planned on receiving a monthly pension and that was their mindset.

In the end, says Frank, it's a question of which risk makes the client least uncomfortable. (Editing by Linda Stern and Jonathan Oatis)

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Social Security to resume benefits statement mailings

Paper Social Security benefits statements, which used to be mailed out every year and then fell victim to budget cuts, are going to make a partial comeback.

Starting this September, the Social Security Administration (SSA) will resume mailings at five-year intervals to workers who have not signed up to view their statements online, an agency spokesman told Reuters. The statements will be sent to workers at ages 25, 30, 35, 40, 45, 50, 55 and 60, he said, adding the agency would continue to promote use of the online statements.

The SSA stopped mailing most paper statements in 2011 in response to budget pressures, and saved the SSA $70 million annually - about 50 cents per mailed statement. But the decision has been a sore point with some critics, who argue the statement provides a valuable annual reminder to workers of what they can expect to get back from payroll taxes in the future.

The annual statement includes an estimate of monthly benefits at various claiming ages, and for disability claims. It explains how benefits are calculated, and displays the worker's history of income subject to Social Security tax.

The SSA budget is funded mainly by the same payroll tax revenue used for paying benefits but Congress, which approves the agency's budget, has approved less than the agency's request in 14 of the past 16 years. In fiscal 2012, for example, SSA operated with $11.4 billion, just 88 percent of the amount requested.

The cuts have led to sharp reductions in SSA customer service. Nationwide, staff is down to 62,000 from a peak of 70,000 in the 1990s.

So far, only 10 million American wage earners - just 6 percent of all workers - have signed up at the site. (www.1.usa.gov/1d3xvuZ). Critics note that many of the workers who will be most reliant on Social Security in retirement are least likely to have Internet access, including low-income and non-English speaking minorities.

The partial restoration of mailed statements was made possible by an improved budget outlook. The SSA's fiscal 2014 budget was boosted to $11.7 billion and President Barack Obama's fiscal 2015 budget request is $12 billion.

"It's a step in the right direction," said Nancy Altman, co-director of Strengthen Social Security, an advocacy group. "But the mailings shouldn't be limited to workers who haven't signed up (for) online accounts. Just because people have signed up, it does not mean that they revisit it to check their earnings statements."

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Heinz 'derisks' pension plan
Food company wants obligation off of its books

Arnold Waldo is boycotting products made by the H.J. Heinz Co.

The Carrick resident who is near his 83rd birthday knows that losing his business is probably not going to make or break the Pittsburgh-based food company that reports billions in sales annually. But for him the symbolism is strong.

Mr. Waldo started work for Heinz in 1951 and — except for a stint in the military — worked there until his retirement in 1985. He had several aunts who also worked for the company that was founded in Sharpsburg in the 19th century and employed generations of Pittsburghers at both its headquarters and its former North Side plant.

A few months ago, the company — which was acquired for more than $28 billion by new owners last June — sent a letter telling him that his annual retiree reimbursement account to cover certain medical expenses was being cut from $3,500 a year to $1,093.

Then the mailbox delivered another blow from Heinz. The company doesn't want to manage his pension plan anymore. "At Heinz, we are committed to being the best food company in the world and pension plan management is not our core competency," said the letter dated Feb. 26 sent to people like Mr. Waldo who were involved in one of two pension plans covering salaried employees and nonunion hourly workers.

Like many other companies before it, Heinz is planning to shift the pension obligations off its books — a process called "de-risking" by organizations like the Pension Rights Center, an advocacy group on retirement issues in Washington, D.C. GM and Verizon made news in recent years by taking similar steps.

Some experts see it as a logical move that will give Heinz relief from a volatile obligation that needs regular infusions of cash. They think the step might even offer a more secure guarantee that pensions won't be threatened if Heinz ever runs into trouble or ends up in bankruptcy.

The Pension Rights Center has concerns, arguing that both offering people lump-sum buyout offers and transferring pensions to insurance companies in the form of annuities could open retirees up to new risks. Individuals may not be prepared to invest the sums properly to make the money last, and they'll no longer be backed by the Pension Benefit Guaranty Corp. Instead, the annuities will be insured by State Guaranty Associations, which vary from state to state.

For its part, Heinz believes the changes to its U.S. and Canadian pension plans will protect retirees' benefits while helping the company. "The value of pension benefits earned to date under these plans will not be affected by these changes," said Michael Mullen, senior vice president of corporate and government affairs for Heinz. "We are simply changing the way pension benefits will be managed and delivered in the future."

He, too, noted that Heinz isn't a trailblazer on this issue. "Many companies have recently made similar changes providing greater flexibility for plan participants and more efficient operations for plan sponsors whose core business is something other than managing and delivering pension benefits."

Heinz has significant pension obligations, according to information in regulatory filings made in the months after the sale to a joint venture of Berkshire Hathaway and 3G Capital in June.

In a filing earlier this year, Heinz indicated it had defined benefit pension and other post-retirement benefit plan obligations of $3.225 billion, with service and interest costs of $92 million as of Dec. 31. The fair value assets behind the plans increased during the

period to $3.7 billion, which included $156 million in employer contributions and $162 million in actual return on plan assets.

The company said it maintains retirement plans for the majority of its employees. The defined benefit plans are mainly for domestic union and for foreign employees, according to a regulatory filing. Defined contribution plans — a term that generally refers to 401(k) plans and individual retirement accounts that both employees and the company contribute to — are offered to most of the company's nonunion hourly and salaried employees.

The changes outlined in the letter sent to Mr. Waldo affect only a small number of Heinz retirees. The company recently merged the plan for salaried employees that he is a participant in with another one that was set up for nonunion hourly employees, a move the company said simplifies administration. The two plans combined include 5,173 participants, with 521 of those still active. The rest are retired or separated from service. Effective April 30, the combined plan is to be terminated, according to the letter send to Mr. Waldo.

Most benefits in the plan have been frozen since 1992, “meaning many participants have not been accruing any benefits in these plans for more than 20 years,” the company said.

Heinz has also merged two other plans, known as Plan B and Plan C, which cover both active and former employees covered under collective bargaining agreements, said Mr. Mullen. That second combined plan is not being terminated, but the company is offering lump sum payments for vested participants and annuities for retirees already receiving benefits.

In the case of Mr. Waldo’s plan, Heinz is offering those who have not started getting benefits the option of getting a lump sum payment. If they reject that, the company will purchase an annuity from an insurance company approved by government regulators.

Participants can expect to receive a lot more letters and updates as Heinz works its way through the IRS and other agencies assigned to regulate pensions, said Donald Fuerst, senior pension fellow at the American Academy of Actuaries in Washington, D.C.

In buying annuities, Heinz will be required to choose an insurance company large enough to securely handle the size of its plans. When GM made the move a couple of years ago, the sheer size of the pension plans limited its options.

In the past when an insurance company failed — a rare enough thing that the Pension Rights Center uses the term “unlikely” — plan participants have been able to get help from the courts if they proved their employer didn’t properly vet the annuity supplier, said Geoffrey Dietrich, vice president of administration at Dietrich & Associates in Plymouth Meeting, Pa.

“The only way for a company to truly relieve themselves of the liability is to go through this process and dot their i’s and cross their t’s,” he said. Mr. Dietrich’s firm has been helping companies shift pension plans into alternative vehicles for years, as more businesses move to individual retirement account-style offerings.

It’s all confusing and confounding to Mr. Waldo, who is getting tired of official letters that arrive and give him what feels like is little time to study and understand their impact on him and his wife.

He understands that companies have to make decisions to help their businesses. He thinks the passage of the Affordable Care Act helped spur the decision by Heinz to end his health care insurance a few years ago and switch to a health payment. But when that payment was cut, it left him scrambling, which he is doing again in response to the pension change.

As for company management, he said, “All you people involved in doing what you are doing to retired pensioners consider this: Eventually it will happen to you.”

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