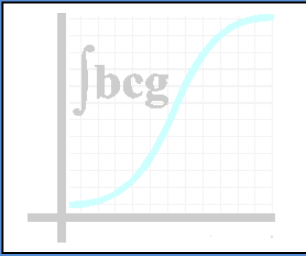

BCG Retirement News Roundup

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Boomershine Consulting Group (BCG) provides 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. If you would like to discuss any of these issues, please contact us.

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Public Sector/Government Plans

Pension fund CIOs see diminished hope in achieving assumed rate of return

Chief investment officers of some of the largest U.S. pension funds acknowledged they have little hope of earning their assumed rate of return over the next couple of years, according to a CIO round table panel at the Pension Bridge Annual Conference in San Francisco on Wednesday.

The Federal Reserve's actions in keeping interest rates low is resulting in lower returns and lower funding ratios, explained John D. Skjervem, CIO of the of the Tigard-based Oregon Investment Council, which runs the $68.1 billion Salem-based Oregon Public Employees Retirement Fund, who spoke on a panel that was moderated by Richard M. Charlton, founder and chairman emeritus of consulting firm NEPC.

Pension fund officials have added as much risk to Oregon's portfolio as they can without taking irresponsible risks, Mr. Skjervem said.

"We are return takers, not return makers," Mr. Skjervem said.

Thomas Tull, CIO of the Texas Employees Retirement System, Austin, said on the panel that officials at the $24.1 billion pension fund think the low-return environment will require "more tactical asset allocation … and going outside the box."

What's more, Texas ERS officials will keep scrutinizing fees and costs in their pension fund's growing alternative investment portfolios.

Pension fund boards have to understand that this is an investment environment in which the chances of making a pension fund's assumed rate of return in the next year or so are not high, said Scott C. Evans, deputy comptroller for asset management and CIO of the $162.1 billion New York City Retirement Systems, who also spoke on the panel.

Investment officials could invest more aggressively, "which might be fun but that is not our job," Mr. Evans said.

"Our job is to make the board understand the realities of the marketplace," Mr. Evans said.

Education is also a focus at Kaiser Permanente, said William D. Lee, CIO and vice president of Kaiser Permanente's $75 billion in foundation and pension assets.

The low-interest-rate environment is making investing more difficult, and pension fund and foundation executives have done everything they can do to boost investment returns, Mr. Lee said.

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Treasury Says Hedge Funds Have Stunted Oversight After Public Pension In New York Divests Billions

Less than a week after New York City's largest pension announced it was divesting from hedge funds because of high fees and poor performance, the U.S. Treasury Department released a report Monday noting there is no single regulator in the U.S. that has the ability to totally understand and monitor the risk profile of those investments.

"No single regulator has a complete window into the risk profile of hedge funds," said the report, which focused on the amount of borrowing and leverage involved in different types of investment.

The report notes that $3.4 trillion is now invested in hedge funds. A sizable portion of that comes from public pensions — some of which have been reconsidering their hedge fund portfolios.

The decision on behalf of the Big Apple's largest public pension, New York City Employees' Retirement System (NYCERS), to divest from hedge funds was seen as a significant blow to the industry, which likes having pension investments because they tend to leave their money invested longer than individuals do and add stability. But, the divestment also follows the 2014 decision by the California Public Employees' Retirement System (CalPERS) to pull its $4 billion investment in hedge funds. NYCERS, which had a total of $51.2 billion in assets earlier this year, contributed to what some researchers said was a $19.8 billion outflow from hedge funds in January, which would make it the worst month for the industry in that regard since 2009, according to Reuters .

At the time, the CalPERS decision was seen as symbolic and perhaps emblematic of a growing dissatisfaction with hedge funds in general. In addition to the lack of transparency, hedge funds are frequently criticized for having high costs while providing lackluster returns. CalPERS paid out around $135 million in fees in its final year with hedge fund investments and NYCERS paid $40 million in fees in 2015.

In addition to noting the opaque nature of hedge funds, the report also lists several steps it says should be considered to counteract this seeming lack of accountability for hedge funds, which use high-risk methods of investment with borrowed money. Those measures include the adoption of

new liquidity risk management practices, limiting the ability of hedge funds to own assets with low levels of liquidity, requiring hedge funds to report liquidity profiles and further disclosure of external sources of financing for the funds.

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Puerto Rico's other crisis: impoverished pensions

For years, the territory's government piled on the benefits without paying for them. Now, it faces the prospect of stiffing retirees, or foreign creditors ... or both.

SAN JUAN, Puerto Rico – When Puerto Rico attempted to shore up its chronically underfunded public-employee pensions in 2013, Francisco del Castillo "knew grown men and women who wept."

Under the reform package, retirement ages rose. So did employee contributions. Current and future participants were transferred to less-generous defined-contribution accounts, similar to 401(k) retirement savings plans. Del Castillo, then the deputy chief of the island's largest government-employee pension system, said members of his own staff who were on the verge of retirement suddenly faced the prospect of working seven or eight more years for reduced benefits.

The law extracted "a pound of political flesh" from those, like del Castillo, who helped craft it, he said. "We wanted it to work."

It didn't, largely because Governor Alejandro Garcia Padilla's government hasn't held up its end of the bargain.

To give the politically painful fixes time to take hold, the reforms required government employers to fund the pensions in the short term through annual lump-sum payments. The central government was supposed to have made $367.6 million in such payments since 2014; so far, it has forked over just $22.7 million.

Governor Garcia Padilla's office declined to comment for this article.

Failed fixes like the 2013 reforms help explain why Puerto Rico's public-employee pensions today are nearly broke – a financial debacle decades in the making, and now deeply entangled with the island's $70 billion debt crisis.

Since Puerto Rico gained self-rule in the late 1940s, improvident populist governments have lavished additional pension benefits on public employees, from holiday bonuses to loans for international travel. These measures have rarely been accompanied by moves to pay for them, and occasional efforts to fill the funding gap have fallen short.

Puerto Rican leaders have been eternal optimists, “always thinking things would eventually improve,” said del Castillo, 40 years old and now legal counsel to the Teachers Retirement System (TRS), one of two main public-employee pensions on the island. “But things continued to deteriorate, and deteriorate, and deteriorate.”

Today, TRS and the other main pension fund, the Employees Retirement System (ERS), together covering about 330,000 workers and retirees, are virtually penniless. Their combined unfunded liability totals $43.2 billion. With about $1.8 billion in assets to pay $45 billion in liabilities, the 96 percent combined shortfall is among the biggest of any U.S. state pension this century, and probably the biggest ever for pensions “of this size and scale,” said Keith Brainard, research director at the National Association of State Retirement Administrators.

And they’re only sinking further. Their combined burn rate – the difference between what they pay out and what they receive in contributions – is more than $1 billion a year, forcing them to rapidly liquidate assets. At that rate, they are forecast to run out of money in 2019, according to a 2015 report by actuarial and consulting firm Milliman, on whose recommendations the government relies.

TRS officials declined several interview requests. ERS Administrator Pedro Ortiz Cortes said pensions “kind of fell off the radar” after the 2013 reforms. The legislation was “reasonable in theory,” he said, though “the ability to comply was not taken into consideration.”

SHIFTING THE BURDEN

Absent a permanent fix, the responsibility to cover benefits will shift to the Puerto Rican government, creating a pay-as-you-go system funded mostly by taxpayers. At $1 billion a year, retirement benefits would cost the island around 11 percent of annual revenue, an unsustainable burden when combined with the 36 percent of revenue now going toward paying bondholders.

The upshot is that an island of 3.5 million people, where nearly half the population lives below the poverty line and the economy has been contracting for most of the past decade, is at a crossroads where neither path forward is appealing.

It can protect pensions, forcing hedge funds and other bondholders to accept draconian cuts under a debt restructuring – a scenario that could wreck Puerto Rico’s ability to borrow internationally for

years.

Or, it can lessen the burden for bondholders by cutting pensions as well, sparking domestic political backlash and fueling outmigration that would further shrink an already dwindling tax base.

“I would need to go to the U.S., sell my house and start looking for a job” if pensions were cut, said Obdulia Lopez, 60, a retired social services worker from rural Juana Diaz who lives on a pension check of about $1,000 a month, after taxes.

Puerto Rico can’t fully control which path it takes. Governor Garcia Padilla’s administration on Feb. 1 unveiled a plan that would preserve pensions while reducing what’s owed to bondholders. The Obama administration also promoted a plan to protect pensioners over investors, and Puerto Rico’s top financial adviser, turnaround specialist Jim Millstein of Millstein & Co, in February said the island has taken pension reform as far as it can under current law.

But creditors with lobbying power -- including hedge funds, mutual funds and bond insurers -- want the Puerto Rican government to do more to curb spending, on pensions and other things. One source in the creditor camp called it “insane” to propose that “bondholders … effectively take all the hit.” Another said: “Puerto Rico’s people are really the ones being victimized. If I had a heart, it would be breaking for them.”

Majority Republicans in Congress are standing with bondholders. In a written response to questions from Reuters, Utah Republican Orrin Hatch, who chairs the Senate Finance Committee, said: “It’s pretty clear a pay-as-you-go Puerto Rico pension system is no more sustainable than Puerto Rico’s debt.”

In March, a group of 170 House Republicans voiced opposition to a draft bill by the House Natural Resources Committee that would allow for debt restructuring.

Garcia Padilla has warned that without a resolution of some sort, Puerto Rico stands to default on some of its $70 billion in debt as early as May, when $422 million comes due.

The government payments into the pension funds under the 2013 law were designed to avoid the very conflict now playing out. Instead, they ended up as yet another example of how solutions can create new problems in the complexities of Puerto Rico’s crisis.
To reduce costs, Puerto Rico has cut its government payroll in recent years through layoffs and other measures that have led to declines in pension contributions. The payments from the government’s general revenue fund were calculated in part to offset those declines, so skipping them means the island’s payroll savings have only deepened the hole for retirees.

Maria Carattini Alvarado, a 72-year-old former teacher who spends more than half of her monthly pension on medicines for a blood condition, supplements her income by making ribboned hats that she sells for $5 a pop. “I’d go live with my son in Texas” if pensions were cut, Carattini said.

In Puerto Rico, teachers, as well as police officers, are ineligible for Social Security, so pension payments are often all they have in retirement. Like many retired teachers, Carattini gets affordable healthcare and housing through programs set up by the Associacion de Maestros, one of Puerto Rico’s teachers’ unions.

But those benefits could disappear, too, if pensions collapsed, said union President Aida Diaz. “If people can’t afford their dues, we can’t provide those services,” said Diaz, herself a pensioner.

Most pensions have a few decades to mature, building up assets in the early years before members retire. Puerto Rico’s pensions carried big unfunded liabilities nearly from the outset, inheriting them from retirement systems in place before the island became a self-governed U.S. commonwealth in 1948. From there, longer life expectancies helped deepen the gap.

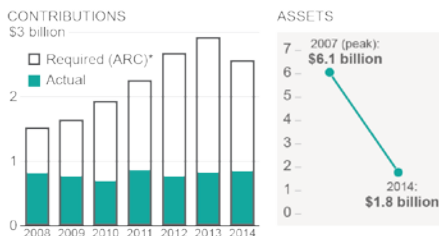
So, too, did island leaders. Populist Luis Munoz Marin, Puerto Rico’s first elected governor, in 1956 instituted cultural excursion loans for pensioners. Puerto Rico was in “a stage of rapid social, economic and political development,” the 1956 law said, and should aim to enable “the largest possible number of Puerto Ricans to travel to foreign countries.”

Today, ERS and TRS participants can take out as much as $5,000 to travel if they can show that the trip will be culturally rewarding. The pensions also offer as much as $5,000 for personal loans and $100,000 for mortgage loans. Together, the two funds have more than $1 billion tied up in illiquid loan portfolios.

‘CANDY TO CHILDREN’

Digging a deeper hole

Government contributions to Puerto Rico’s two main pensions have fallen below a third of the amount required to close their funding gap, and their combined assets have plummeted by nearly 70 percent since the 2007 peak.



* Refers to the amount that would be required in order to close the funding gap over 30 years, otherwise known as the annual required condribution, or ARC.
Source: actuarial reports

The largess continued under Luis Ferre, governor from 1968 to 1972, who increased benefits and instituted mandatory Christmas bonuses. Last December, creditors griped privately when Puerto Rico doled out about $120 million of the bonuses even as it missed some minor bond payments.

Christmas and medication bonuses, ad hoc cost-of-living adjustments, death benefits and other perks were expanded periodically throughout the 1980s, '90s and 2000s. These now account for nearly $3 billion in liabilities, according to Milliman's latest actuarial report, even after reductions under the 2013 reforms.

Rafael Hernandez Colon, president of the Puerto Rico Senate during Ferre's administration, said his party went along with the Christmas bonuses "for political reasons" to avoid being labeled obstructionist, but did not consider it good governance. "We looked at it as giving candy to children," Hernandez Colon said in an interview at his foundation in Ponce, a city on Puerto Rico's southern coast.

Yet when Hernandez Colon won the governor's seat in 1972, his administration approved perhaps the most structurally damning benefit of all. Under a 1973 amendment to existing pension law, government employees who retired at 55, with 30 years of service, were entitled to lifetime annual payouts worth 75 percent of their salary.

That percentage was based not on a worker's career average salary, but on the average of his three highest salaries. So those who were promoted close to retirement, or for only a short time, could earn lifetime pensions disproportionate to contributions.

"People were making pensions that might not have reflected the average of what they were putting in over decades," said Marcos Rodriguez-Ema, a banker and former government official involved in pension reform efforts in the 1990s and 2000s.

Familiar populist language peppered the 1973 legislation, vowing to "stimulate the creative vitality" of workers who had dedicated their lives to Puerto Rico, and cushion them against the "uncertainty that comes with age."

The amendment brushed off concern about future financial strain on the pensions, saying their investments were producing revenue twice what actuaries had approved, so the "measures won't be burdensome."

"I feel that I was very sensitive to the pensioners and tried to comply with them in a responsible way," Hernandez Colon, now 79, told Reuters. "Whether it was in fact responsible, you'd have to analyze it."

The benefit structure remained in place until reforms in 1990 – during Hernandez Colon's second stint as governor – reduced benefits for future workers. Today, of ERS's $30.2 billion total unfunded liability, about $24 billion – 80 percent – is attributable to that era, owed to people who worked, retired or were hired before the 1990 changes.

Another set of reforms in 1999, known as System 2000, eased the pensions' long-term liabilities by moving future retirees to a defined-contribution system. But legislation to ensure adequate long-term funding for benefits, such as by increasing employer contributions, has been rare. Unlike in some states, the rate Puerto Rico contributes to its pensions is set by statute, rather than the recommendation of actuaries, and requires legislation to change. This makes pension contributions a political issue.

"People don't want to make hard decisions today for savings that, when it would occur, they were not going to be in office," del Castillo said.

Rodriguez-Ema helped shape what would become System 2000 as president of Puerto Rico's Government Development Bank (GDB). He said that so long as Puerto Rico's economy kept growing and ratings agencies weren't concerned about pension liabilities, strengthening the pensions wasn't a priority. "We realized we were going to have a problem, but it was in the future," he said. "We could fund the retirement system without any problems whatsoever."

ILL-FATED BONDS

That blithe approach came to an end by the mid-2000s, as the island's economy showed its first signs of decline. When Anibal Acevedo Vila assumed the governor's chair in 2005, the two pensions' combined unfunded liability stood at around $12 billion. The new governor pushed a bill to authorize a $2 billion bond issue from the government's books, with proceeds to go to ERS.

The bill died in Puerto Rico's legislature, a victim of political feuding.

Acevedo Vila's next effort to boost pension funding proved disastrous. To skirt the need for legislative approval, his administration arranged for ERS to issue its own bonds – unheard-of for a public pension – and put up employer contributions as collateral. But, Acevedo Vila said, the government "needed to assure people the pension would not collapse."

The plan was to raise $7 billion -- the amount the administration calculated was necessary to earn enough interest to cover ERS's annual burn rate. The pension in 2008 sold $2.9 billion in the first of multiple planned tranches underwritten by UBS and arranged by Jorge Irizarry, then president of the GDB.

But Acevedo Vila, plagued by a lengthy indictment on charges he violated campaign finance laws, lost his 2008 re-election bid. (A jury later found him not guilty.) His successor, conservative Luis Fortuno, had no interest in issuing more bonds.

Instead, in what is widely viewed today as a political maneuver, Fortuno commissioned consultants Conway MacKenzie to examine his predecessor's handling of ERS. The firm's 2010 report excoriated the bond deal, calling elements of it so "obviously flawed and not logical" that it "could imply a lack of understanding" of the deal by island officials.

Conway concluded that UBS was hired to place the bonds locally only after Merrill Lynch failed to place them internationally, showing a lack of appetite for the full $7 billion. The report said Alfredo Salazar, GDB's chairman at the time, and Irizarry should have known that raising less than $7 billion would fail to generate sufficient returns to pay bondholders and cover ERS's burn rate, only adding to the pension's liability down the road.

In separate interviews, Irizarry and Salazar said it was never the idea to issue all the debt at once. Conway's report "misstated many facts and omitted others," Irizarry said.

Salazar said the bonds were issued locally so they could qualify as tax-free. "We decided," he said in an interview, "to do whatever capacity we could get in the local market and then move on to the taxable market if we needed more."

A Conway spokesman did not return calls seeking comment. UBS and Merrill declined to comment.

Conway's politically convenient conclusions may have taken pressure off Fortuno to solve the pensions' problems, but few independent observers dispute one of its major findings: The bonds increased "the complexity of … fixing [ERS's] fundamental structural problems."

The bonds saddled pensioners with a big new obligation without generating enough returns to stave off insolvency. Chunks of government pension contributions are now going out the door to pay bondholders who rank ahead of pensioners in the payout line.

A former Acevedo Vila administration official told Reuters that if the administration had known that only $2.9 billion would be raised, it "wouldn't have issued the bonds at all."

Acevedo Vila insists the bonds extended the pension's life. "I never said I fixed the problem," the former governor, now 54, said at his law office in San Juan's Rio Piedras neighborhood. "But I was doing something to give the pensions more time."

FORTUNO'S EFFORTS

As governor, Fortuno signed a 2011 law that raised the government's pension contributions – the first increase since the 1990 reforms – then appointed a bipartisan commission to explore more comprehensive changes.

In the end, he could not save the pensions, either. The commission never produced any draft legislation. Fortuno blames the man who eventually succeeded him as governor, Garcia Padilla.

In early 2012 – an election year – Fortuno's commission began to coalesce around a proposal to reduce bonuses, raise retirement ages and increase employee contributions, Fortuno said during a phone interview from his Washington, D.C., law office.

Garcia Padilla, then a senator who headed the opposition party, withheld his party's cooperation on any pension fixes, according to Fortuno and members of his administration. Garcia Padilla "was saying, 'Luis Fortuno is the enemy of retirees. We're not going to work with him. Vote against him,' " Fortuno said.

When pressed on whether he could have done more to reverse the pensions' downward spiral, Fortuno said: "Maybe I could have done more in 2009 or 2010 to ram [pension reform] down the throats" of lawmakers by shutting down Puerto Rico's government, "but I didn't want to further shatter people's faith in their economic future."

As the crisis over pension funding was reaching fever pitch, Garcia Padilla, newly installed as governor, signed into law the kind of comprehensive pension reform that had eluded earlier generations – and which he had months earlier criticized Fortuno for trying to enact.

The April 2013 reform – the one del Castillo said caused some people to cry – imposed stricter terms on plan participants to improve ERS's funding over the long term while requiring the government to pay into the system for a few years to cover short-term needs. The law "created a healing process" for ERS, del Castillo said, putting it on track to stabilize as legacy obligations die out.

Lawmakers tried to enact similar reforms at TRS, but Puerto Rico's Supreme Court invalidated some key elements, putting teachers' benefits in jeopardy in both the short and long term. Pension reform efforts generally have not addressed teachers, who today remain eligible for guaranteed, defined-benefit payouts.

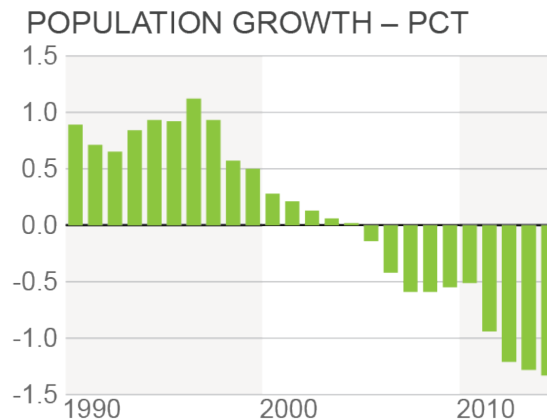
Some people attribute this lack of action to the power of teacher groups. "They're homogeneous, they're well-organized, and they lobby hard," said Hector Mayol, the top official at both ERS and TRS from 2009 to 2013. Pension cuts are more politically charged at TRS because beneficiaries don't

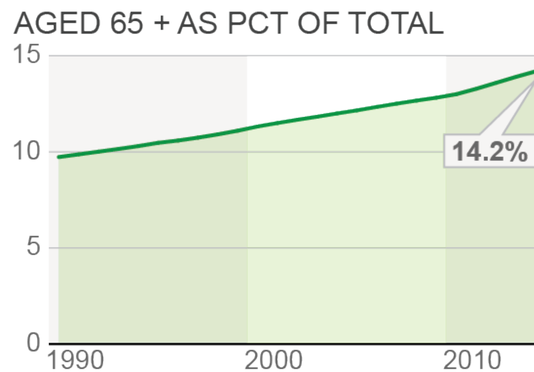
receive Social Security.

The 2013 law has hardly fixed ERS, though, largely because Puerto Rico has failed to follow its own law by withholding the bulk of payments into ERS, so-called additional uniform contributions (AUCs).

A shrinking, aging population

As Puerto Rico's population shrinks due to emigration, tax revenues fall and retirees claim a growing slice of the demographic pie.





Source: World Bank

Maintaining pension benefits in the near term was part of the shared sacrifice to ensure pensioners' long-term concessions were not made in vain. But 14 months after the 2013 reforms were passed – and on the heels of credit downgrades by S&P and Moody's – Puerto Rico enacted Act 66, a fiscal emergency law that let the government suspend some financial obligations.

ERS is still waiting on about $345 million of the combined $367.6 million in AUCs owed by Puerto Rico's central government, according to data provided by ERS. Actuary Milliman raised the AUC for the current year, in part to offset decreases in pension contributions from layoffs and other payroll cuts, and in part to make up for previous years' missed payments.

But Ortiz Cortes, the ERS administrator, said the pension has not received any of this year's infusion from the central government, and only about $23 million from municipalities, public agencies and other employers.

That means next year's AUC will shoot even higher, and Ortiz Cortes said his staff has been told by the island's budget officials not to expect close to a full payment then, either.

Through a spokeswoman, Budget Director Luis Cruz Batista declined to comment.

"It's going to be a bumpy road" for pensions, Ortiz Cortes said. "Whatever goes down, it's going to be bumpy."
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GASB STATEMENT NO. 82 AMENDS STATEMENT NO. 67, NO. 68 AND NO. 73:

Governmental Accounting Standards Board has issued Statement No. 82 to address certain issues that have been raised with respect to Statement No. 67, Financial Recording for Pension Plans, No. 68, Accounting and Financial Reporting for Pensions, and No. 73, Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68.

Specifically, the Statement addresses issues regarding (1) presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and treatment of deviations from guidance in an Actuarial Standard of Practice for financial reporting purposes and (3) classification of payments made by employers to satisfy employee (plan member) contribution requirements. Prior to the issuance of the Statement, Statements 67 and 68 required presentation of covered-employee payroll, which is the payroll of employees who are provided with pensions through the pension plan, and ratios that use that measure, in schedules of required supplementary information. The Statement amends Statements 67 and 68 instead, to require presentation of covered payroll, defined as payroll on which contributions to a pension plan are based, and ratios that use that measure.

The requirements of the Statement are effective for reporting periods beginning after June 15,

2016, except for requirements of the Statement for the selection of assumptions in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. As usual, earlier application is encouraged.
The requirements of the Statement will improve financial reporting by enhancing consistency in application of financial reporting requirements to certain pension issues. No. 359 (March 2016.) (Note that member Fish descended, believing that the Statement makes it more difficult for users to make comparisons, and does not provide information essential to their understanding of the amounts recognized and disclosures made in the financial statements regarding pension contributions.)

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SUMMARY OF THE QUARTERLY SURVEY OF PUBLIC PENSIONS FOR FOURTH QUARTER 2015:

For the 100 largest public-employee pension systems in the country, assets (cash and investments) totaled $3,243.3 billion in the fourth quarter of 2015, increasing 0.9% from the third quarter level of $3,215.9 billion. This increase in assets is mainly due to positive earnings, as evidenced by a gain of $63.6 billion in the fourth quarter. Compared to the same quarter in 2014, assets for these major public pension systems decreased 3.0% from $3,343.6 billion.

The major asset categories highlighted in this summary (equities, debt instruments, and cash equivalents) do not reflect all the categories published for the Quarterly Survey of Public Pensions. International securities had a quarter-to-quarter increase of 4.1%, from $575.1 billion to $598.7 billion in the fourth quarter of 2015. Conversely, international securities decreased 1.8% year-to-year, from $609.6 billion to $598.7 billion. International securities comprised less than a fifth (18.5%) of total cash and investments of major public pension systems for the current quarter. Corporate stocks had a quarter-to-quarter increase of 2.0%, from $1,154.8 billion to $1,177.8 billion during the fourth quarter of 2015. However, corporate stocks experienced a year-to-year decrease of 3.4% from $1,219.1 billion in the fourth quarter of 2014.

Corporate stocks comprised more than a third (36.3%) of the total cash and investments of major public pension systems for the current quarter. Corporate bonds had a quarter-to-quarter decrease of 0.4% from $414.1 billion to $412.4 billion in the fourth quarter of 2015. However, corporate bonds increased year-to-year by 2.7% from $401.5 billion in the fourth quarter of 2014. Corporate bonds comprised about an eighth (12.7%) of the total cash and investments of major public pension systems for the current quarter.

Employee contributions had a quarter-to-quarter increase of 30.5%, from $9.3 billion to $12.1 billion during the fourth quarter of 2015, and a year-to-year increase of 13.7%, from $10.6 billion in

the fourth quarter of 2014. During the same time periods, government contributions had a quarterly increase of 3.1%, from $28.8 billion to $29.7 billion, and a year-to-year increase of 20.1%, from $24.7 billion in the fourth quarter of 2014. The ratio of government contributions to employee contributions was 2.5 to 1, as government contributions comprised 71.1% of total contributions. Total benefit payments decreased 2.0% to $63.8 billion, from $65.1 billion from a quarter ago.

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Private Sector

Boomer Expectations for Retirement 2016

Trouble Ahead! Baby Boomers' Retirement Outlook on the Decline
IRI Study Finds Few Boomers Are Confident in Attaining Financial Security in Retirement, Many Not Saving and Planning for Retirement

WASHINGTON, D.C. – The Insured Retirement Institute (IRI) today released a new research report that found less than a quarter of Baby Boomers, 24 percent, are confident they will have enough savings to last throughout their retirement years. This is the lowest level since IRI began this research study in 2011, when 37 percent of Boomers had this same level of confidence.

The sixth annual study also found that this lack of confidence is understandable, given Boomers' readiness for retirement. Only 55 percent of Boomers reported having savings for retirement. And nearly half of those Boomers with savings, 42 percent, have saved less than $100,000 – an amount that would generate less than $7,000 a year in retirement income. Overall one in five Boomers are concerned they will not have enough savings to cover basic living expenses.

"The road to a confident financial future begins with developing a holistic retirement plan," IRI President and CEO Cathy Weatherford said. "Unfortunately most Boomers are not taking important planning steps. Less than 40 percent have determined a savings goal, and just over a quarter are seeking help from a financial professional. Time is running out. Unless Boomers begin to focus on their long-term needs now and commit to savings, they will need to work longer and make steep cutbacks to make ends meet in retirement."

The IRI study also offers some helpful tips for future generations, including GenXers and Millennials. The study found that Boomers lacking confidence in their retirement security have some common regrets, with 68 percent wishing they had saved more and 67 percent wishing they started saving earlier.

Other key findings from the report:
•Only 22 percent of Boomers are confident with their preparations for retirement, 27 percent are confident their savings with be sufficient to cover health care costs in retirement, and only 16 percent are confident they can cover the cost of long-term care.
•During the past year, 30 percent of Boomers postponed their plans to retirement. About six in 10 Boomers, 59 percent, now plan to retire at age 65 or later. This includes 26 percent who plan to retire at age 70 or later. In 2011, only 17 percent of Boomers expected to retire at age 70 and beyond.
•If their financial resources become exhausted in retirement, 71 percent will try to cut back to rely only on Social Security, and 54 percent said they will try to return to work if able.
•Three in 10 Boomers stopped contributing to a retirement account, and 16 percent of Boomers took premature withdrawals from their retirement accounts.
•Nearly six in 10 Boomers, 59 percent, expect Social Security to be a major source of income in retirement, up from 43 percent in 2014.
•Six in 10 Boomers believe their retirement income will cover basic expenses as well as some for travel and leisure activities.
•Only 46 percent of Boomers believe it is important to leave money to heirs, down from a high of 67 percent in 2013.
•More than eight in 10 Boomers who work with a financial professional said they are better prepared for retirement as a result.
•68 percent of Boomers who own annuities and 78 percent of Boomers who work with financial professionals have at least $100,000 saved for retirement, compared to only 58 percent of all Boomers.
•Of divorced Boomers, 24 percent said being divorced will leave them worse off in retirement, and 23 percent said they will need to work longer as a result.
•More than six in 10 Boomers, 62 percent, would prefer to meet with a financial professional in-person. An equal amount said they are unlikely to use an automated, online solution.
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IRS Withdraws Troubling Provision of Proposed Nondiscrimination Regulations

Yesterday, the IRS released Announcement 2016-16 withdrawing parts of the nondiscrimination regulations it proposed at the end of January. Those proposed regulations had troubled many in the defined benefit industry since their proposal for a number of reasons (more below). From the standpoint of the IRS, the troubling part of the proposal addressed some serious abuses by practitioners and the sponsors they consult to. From the standpoint of practitioners, the proposed regulations took an objective test that has been around for quite a while and essentially changed the rules of the game.

I'm going to have to get a little bit technical here before I bring you back to reality. What the proposed regulations would have done was to make retirement plans with multiple formulas show that each formula applied to reasonable business classifications of employees or to pass a more difficult test.

Under regulations that were finalized in 1993 and then amended for cross-tested plans in the late 90s, a rate group in the testing population must have a coverage ratio at least equal to either

- 70% if the plan uses the Ratio Percentage Test to pass minimum coverage tests or
- The midpoint of the safe harbor and unsafe harbor (the midpoint is typically in the 25% to 40% range, but is determined through a somewhat convoluted formula) if the plan uses the Average Benefit Test to satisfy minimum coverage

It is far easier for a rate group to satisfy a lower minimum coverage ratio than a higher one. And, many plans had been designed around satisfying the lower threshold. While the preamble to the proposed regulation said that it was targeting QSERPs, practitioners found that they also were potentially problematic for many plans of small businesses and plans of professional service firms.

Why would this be troubling? Certainly, among larger corporations, the prevalence of ongoing defined benefit plans has dropped precipitously, but many small businesses and professional service firms have adopted new defined benefit plans (DB) over the last 15 years or so and many of these plans would have found it more difficult or perhaps impossible to pass these proposed rules.
This doesn't mean that DB plans of this sort are out of the woods yet, so to speak. Clearly, the current Treasury Department views that plans of this sort may be abusive in their application of the nondiscrimination regulations, so we could see another effort from the IRS to make the regulations a bit less QSERP-friendly.
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Disappearing pensions hurt U.S. economy as well as workers

Retirement has taken a back seat to corporate profitability for more than 40 years as the United States has embraced the reduction of pensions, and now the U.S. economy is paying the price with lowered productivity.

Without pensions, older workers are being forced to work longer hours and stay in the workforce longer, and that means they're squeezing out some of the most productive workers of all, known as core workers, according to a study by the University of Paris-Sorbonne.

The study compared workers in three different age groups: younger workers (ages 15-24), core workers (ages 25-54) and older workers (ages 55-64). The percentage of those in the older group who are currently working widened to 61% in 2014, up from 60% in 2004, while the percentage of

those in the core group currently working has shrunk to 77% in 2014 from 79% in 2004, according to the Organization for Economic Cooperation and Development (OECD).

On one hand, the U.S. economy has become more productive by pushing older workers into the labor force, along with women and migrants who have also increased their participation in the labor force. However, by doing so the U.S. has also decreased its productivity per worker, the Sorbonne study showed.

Inequality has widened as a result

The drop in U.S. pensions also contributed to the rising gap between the rich and poor, and that inequality led in part to the Great Recession of 2008-2009, said French economist Thomas Piketty at a conference this month in Paris. By eliminating pensions, the U.S. has moved closer to a capitalist economy where companies no longer rely on pensions to attract workers and also don't have a safety net where companies and workers are taxed to raise money for their pensions, as is the case in most European countries. That change has led to increased inequality, because low- and middle-class workers cannot afford pensions, whereas the wealthy can.

What's more, by pushing older workers into the labor force, the U.S. economy has taken jobs away from younger workers who could be more productive. Keep in mind this is not to suggest that older workers can't be as productive as younger workers. Experience and knowledge go a long way. But when taken across the entire U.S. economy, older workers tend to be less productive on average, according to the study at the Sorbonne. Globally, the peak average age for workers in terms of their productivity tends to be about 43.

Riding on the coattails of abuses by several public and private pension plans, the Employee Retirement Income Security Act (ERISA) was sold to the American public in 1974 as a way of protecting people's pensions by ensuring that they would be made secure and backed by the federal government.

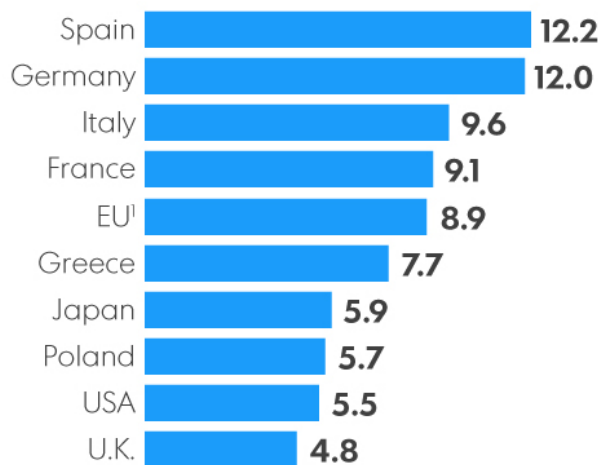
It worked, but not as the American public thought it would. It did protect pensions, but it also made them costlier for employers. As soon as the ink was dry on ERISA, Corporate America began eliminating pensions from its balance sheets. From 1980 through 2015, the proportion of private wage and salary workers participating in defined benefit pension plans fell from 38% to 15%, according to the U.S. Bureau of Labor Statistics. DB plans are the traditional pension plans that your father or grandfather's generation were accustomed to, but now they're as rare as a gold watch at retirement.

The U.S. government later created the 401(k) in 1978, but it was never expected to support workers through retirement. It has been embraced by corporations as a way to attract workers by having the workers pay for their own retirement, thus eliminating pensions from corporate balance sheets. Also, by eliminating pensions, corporations no longer needed the voice of workers at the bargaining table.

What has the effect been on retirees?

Currently, about 43% of private workers take part in their 401(k) or other defined contribution plan, according to the U.S. BLS. That isn't enough to support most of the retirees throughout their retirement. Through the end of 2015, the average 401(k) balance at Fidelity Investments, one of the country's biggest 401(k) providers, was just $91,300 — a paltry amount compared with what experts say you would need to save for retirement.

Below is a graph that shows how little the U.S. has saved for pensions when compared with other countries:



So is the answer just to keep working and save more in your 401(k) and hope for the best? Or does the answer require a broader perspective, bringing government, corporations and workers together to look at ways of either resurrecting pensions or creating legislation that requires companies to contribute more to employees' 401(k)s?

Washington seems too worried about saving Social Security and Medicare to be concerned with the much broader issue of saving pensions. That leaves U.S. corporations and workers to solve the issue themselves.

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The Fight to Move PBGC Premiums Off-Budget Goes to Capitol Hill

A group of 7 associations –The ERISA Industry Committee (ERIC), the American Benefits Council, the American Retirement Association, the Committee on Investment of Employee Benefit Assets, the National Association of Manufacturers, the Society for Human Resource Management, and U.S. Chamber of Commerce –today sent a letter to Congressmen Jim Renacci (R-OH) and Mark Pocan (D-WI) thanking them for introducing the Pension and Budget Integrity Act of 2016. The Act would ensure any future pension premium increases are only used towards retiree payments from the Pension Benefit Guaranty Corporation (PBGC) and not double counted for budget scoring purposes, which was the original intent of Congress when the PBGC was created in 1974.

The PBGC was established in 1974 to ensure adequate funds would be available for pension plans in the event an employer sponsoring a plan enters bankruptcy. However, Section 406 of The Multiemployer Pension Plan Amendments Act of 1980 allowed PBGC premiums to be calculated as general fund revenue for budget scoring, even though the premiums themselves are not used to pay for unrelated programs. While the premiums are not used to pay for other programs the increases are counted for budget purposes as a revenue raiser, leaving sponsors of single-employer defined benefit plans to shoulder additional financial burdens. Increases in premiums introduced last year were made despite projections that show the single-employer pension system will be in a good financial health over a ten-year window.

The Pension and Budget Integrity Act of 2016 is good governance. It removes a budget gimmick that will help to stabilize single-employer pension plans and provides more certainty for America's companies and their employees.

"Discipline is needed to ensure that PBGC premiums are used solely to protect the pension system and not as a budget gimmick to pay for unrelated federal programs," said Annette Guarisco Fildes,

president and CEO, The ERISA Industry Committee. "The predictability of costs is critical as employers weigh whether to continue sponsoring defined benefit plans and there is nothing predictable about Congress raising premiums at any time to pay for other programs."

"Unfortunately over the past few years, single-employer pension premiums have been increased by nearly $21 billion, diverting billions of dollars that businesses could otherwise use to fund employee benefits, business investments and job creation." said National Association of Manufacturers Director of Tax Policy Christina Crooks. "Manufacturers support the Pension and Budget Integrity Act to ensure businesses will no longer be saddled with unnecessary increases in PBGC premiums, a tax on employers that provide defined benefit pension plans."

"The trend over the past few years of increasing PBGC premiums to offset deficit spending elsewhere in the federal budget, without regard to the true financial condition of the PBGC, is shortsighted because it removes good policy from the equation and perpetuates the image of a broken legislative process," said Lynn Dudley, senior vice president, global retirement and compensation policy for the American Benefits Council. "The measure introduced today will encourage lawmakers to consider more carefully the well-being of the PBGC and the Americans it protects."

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Shorter Life Expectancy Reduces Projected Lifetime Benefits for Lower Earners

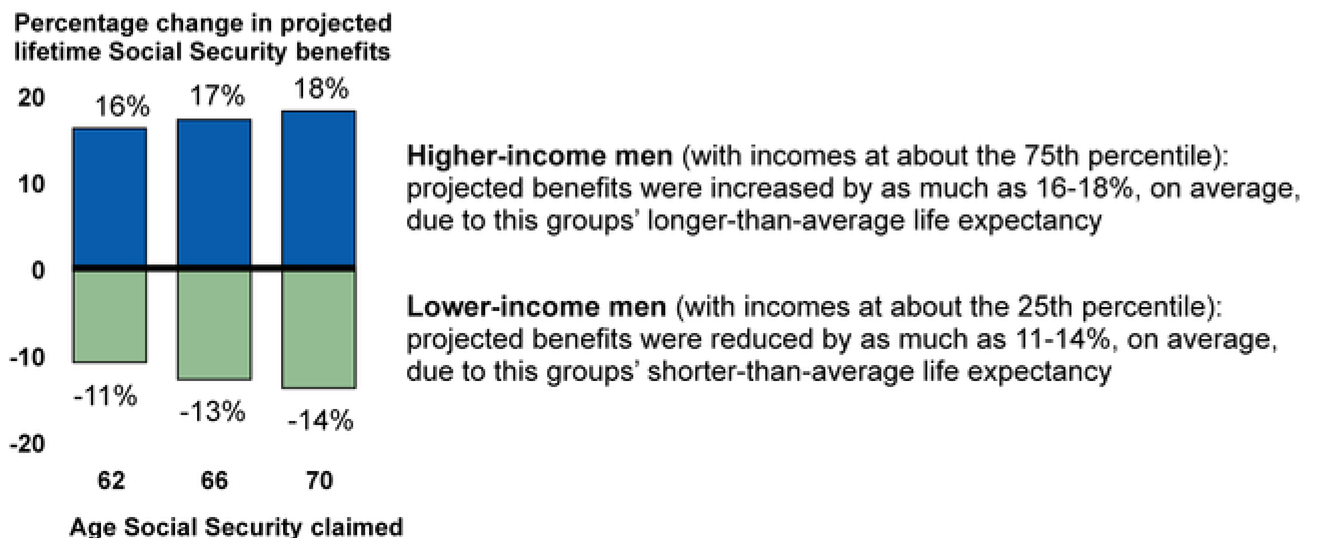
What GAO Found

The increase in average life expectancy for older adults in the United States contributes to challenges for retirement planning by the government, employers, and individuals. Social Security retirement benefits and traditional defined benefit (DB) pension plans, both key sources of retirement income that promise lifetime benefits, are now required to make payments to retirees for an increasing number of years. This development, among others, has prompted a wide range of possible actions to help curb the rising future liabilities for the federal government and DB sponsors. For example, to address financial challenges for the Social Security program, various options have been proposed, such as adjusting tax contributions, retirement age, and benefit amounts. Individuals also face challenges resulting from increases in life expectancy because they must save more to provide for the possibility of a longer retirement.

Life expectancy varies substantially across different groups with significant effects on retirement resources, especially for those with low incomes. For example, according to studies GAO reviewed, lower-income men approaching retirement live, on average, 3.6 to 12.7 fewer years than higher-

income men. GAO developed hypothetical scenarios to calculate the projected amount of lifetime Social Security retirement benefits received, on average, for men with different income levels born in the same year. In these scenarios, GAO compared projected benefits based on each income groups' shorter or longer life expectancy with projected benefits based on average life expectancy, and found that lower-income groups' shorter-than-average life expectancy reduced their projected lifetime benefits by as much as 11 to 14 percent. Effects on Social Security retirement benefits are particularly important to lower-income groups because Social Security is their primary source of retirement income.

Disparities in Life Expectancy Affect Lifetime Social Security Retirement Benefits



Social Security's formula for calculating monthly benefits is progressive—that is, it provides a proportionally larger monthly earnings replacement for lower-earners than for higher-earners. However, when viewed in terms of benefit received over a lifetime, the disparities in life expectancy across income groups erode the progressive effect of the program.

Why GAO Did This Study

An increase in average life expectancy for individuals in the United States is a positive development, but also requires more planning and saving to support longer retirements. At the same time, as life

expectancy has not increased uniformly across all income groups, proposed actions to address the effects of longevity on programs and plan sponsors may impact lower-income and higher-income individuals differently. GAO was asked to examine disparities in life expectancy and the implications for retirement security.

In this report, GAO examined (1) the implications of increasing life expectancy for retirement planning, and (2) the effect of life expectancy on the retirement resources for different groups, especially those with low incomes. GAO reviewed studies on life expectancy for individuals approaching retirement, relevant agency documents, and other publications; developed hypothetical scenarios to illustrate the effects of differences in life expectancy on projected lifetime Social Security retirement benefits for lower-income and higher-income groups based on analyses of U.S. Census Bureau and Social Security Administration (SSA) data; and interviewed SSA officials and various retirement experts.

GAO is making no recommendations in this report. In its comments, SSA agreed with our finding that it is important to understand how the life expectancy in different income groups may affect retirement income.

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