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

N.J. governor pushes for higher contribution to state pension fund

New Jersey Gov. Phil Murphy on Tuesday proposed raising the state's general fund contribution to the New Jersey Pension Fund, Trenton, to $3.75 billion for the fiscal year beginning July 1, an increase over the $3.2 billion slated for the current fiscal year.

Mr. Murphy made his recommendation in his budget message to a joint session of the New Jersey legislature in Trenton, according to a transcript of his remarks.

Although the proposed amount is the largest in the pension fund's history, it still only represents 70% of the actuarially determined contribution. The current fiscal year's contribution represents 60% of the actuarially determined contribution.

Mr. Murphy has pledged to increase state contributions by 10-percentage-point annual increments — a practice started by former Gov. Chris Christie — until 100% annual contributions are reached.

The general fund contributions augment the estimated $1 billion annual contribution to the $70.9 billion pension fund via the New Jersey Lottery. Mr. Christie signed a law in July 2017 transferring the lottery to the pension fund as a pension fund asset.

Last month, the state Treasurer's office issued a request for qualifications, seeking financial advisory firms that could help determine if converting other state assets — such as roads, transit facilities and airports — could be used like the lottery to help support the pension fund.

Mr. Murphy's budget proposal contains about $1.1 billion in savings, most notably in public employee health benefits, as well as tax increases on the state's wealthiest residents.

For the current fiscal year, Mr. Murphy signed a law increasing taxes on residents who earned $5 million or more. For the upcoming year, he wants the tax extended to those earning $1 million or more, according to the budget document.

Negotiations with the Legislature portend to be contentious given legislators' reluctance to raise taxes.

"I understand the budget I am proposing today will not be identical to the one I will ultimately sign," the transcript of Mr. Murphy's remarks said. "We will talk, we will negotiate, and we will compromise. That is as it should be."

Beyond the negotiations for the next fiscal year, independent sources have raised concerns about the current fiscal year, saying the state's revenue through January is behind the revenue predictions the governor made.

Total tax collections through January 2019 were 2.9% higher than the corresponding year-ago period, a Feb. 21 report by the Office of Legislative Services said. The governor's budget for the current fiscal is counting on a 7.2% full-year growth vs. fiscal 2018, the report said.

"Expectations that weak estimated payments in December would recover in January were not met," the report said.

"Continued revenue growth below current fiscal 2019 budget targets could point to longer economic and revenue pressure," a Feb. 25 report by S&P Global said.

For example, gross income taxes through January were down 6% vs. the same period last year. The governor's budget for the full fiscal 2019 calls for a 5.4% gain vs. the previous fiscal year.

"While a major portion of income tax is received in April ... the extended revenue shortfalls in the first half of the year will make catching up by the end of the year more difficult," S&P said, "even if currently slow revenue trends reverse."

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New pension-cut rulings begin with little change

Voter-approved pension cuts were the first wave of court cases after public pension investment funds had huge losses in a stock market crash a decade ago, creating the need for big bites out of government budgets to pay alarming debt.

Ballot measures in cities large and small were overturned by the courts, from a blunt-force cap on annual payments to CalPERS in Pacific Grove to a stark choice for employees in San Jose: pay more for

pensions earned in the future or begin earning a smaller pension.

The local measures ran afoul of the "California Rule," a series of state court rulings believed to mean the pension offered at hire becomes a vested right, protected by constitutional contract law, that can only be cut if offset by a comparable new benfit, erasing any savings.

A unanimous appeals court panel ruling in 2015 that overturned a San Francisco ballot measure cutting a supplemental cost-of-living adjustment for city pensions was based on one of the key California Rule issues.

"This diminution in the supplemental COLA cannot be sustained as reasonable because no comparable advantage was offered to pensioners or employees in return," said the ruling in the San Francisco case.

Then a year later in a Marin County case another unanimous appeals court ruling, like the San Francisco ruling citing more than a dozen previous rulings, followed its presumably logical legal path to an opposite conclusion.

"There is no absolute requirement that elimination or reduction of an anticipated retirement benefit 'must' be counterbalanced by a 'comparable new benefit,'" said the *Marin ruling.*

The Marin case is part of a new wave of court challenges to pension cuts, this time to fringe parts of the Public Employees Pension Reform Act (PEPRA) pushed through the Legislature by former Gov. Jerry Brown that took effect on Jan. 1, 2013.

Main cost-cutting parts of the reform, such as working longer to earn the equivalent of a pre-reform pension, are limited to employees hired after the reform who do not yet have vested rights, thus avoiding a clash with the California Rule.

The state Supreme Court has agreed to hear at least five cases challenging the governor's reform. An issue in most of the cases is whether pension cuts applied to vested employees hired before the reform, not just new hires, violate the California Rule.

Last week the high *court ruled* on the first of the five cases, unanimously upholding the reform ban on boosting pensions by buying up to five years of additional service credit. It's called "air time" because the employee does no work to get credit for the years.

In two steps mentioned in a court summary before the ruling, the court first found air time was not a

vested right and then did not, as the state and others urged, consider the California Rule because air time was found to be unprotected by constitutional contract law.

"For that reason, we have no occasion in this decision to address, let alone to alter, the continued application of the California Rule," the Supreme Court said.

The ruling was a rare pension court loss for unions, led by Cal Fire Local 2881. While awaiting the next case, lawyers are analyzing the 45-page ruling written by Chief Justice Tani Cantil-Sakauye for any hint of clarifying or reshaping the California Rule.

Among the main points in the ruling is that public employment is ordinarily statutory, rather than contractual, and can be modified by the governing body. But constitutional protection can arise in two ways:

When statutes creating an employment benefit "clearly evince an intent by the relevant legislative body to create contractual rights," or when "contractual rights are implied as a result of the nature of the employment benefit, as is the case with pension rights."

The ruling said the air time legislation did not show intent to create contractual rights. "Further, unlike core pension rights, the opportunity to purchase ARS (additional retirement service) credit was not granted to public employees as deferred compensation for their work."

The California Rule got its name in part because it has not been widely adopted elsewhere. The ruling said a research paper by Amy Monahan notes that "of the twelve states to adopt the rule, three have since modified it."

Left to right, standing: Justice Mariano-Florentino Cuéllar, Justice Carol A. Corrigan, Justice Goodwin H. Liu, and Justice Leondra R. Kruger
Left to right, seated: Justice Kathryn M. Werdegar *(retired August 2017)*, Chief Justice Tani G. Cantil-Sakauye, and Justice Ming W. Chin

The next California Rule case heard by the high court may be the *"Alameda" case,* a consolidation of union challenges in three county retirement systems to Brown reform "anti-spiking" provisions, which curb improper boosting of the final pay that sets pension amounts.

The court put three other pension reform cases on hold, pending a decision on the Alameda County case (combined with similar cases in the Contra Costa and Merced county systems) about spiking curbs applied to vested pre-reform employees, not just new hires.

On the long list of items banned from final pay by the reform and the counties are, for example, one-time pay for performance and bonuses, cashing out unused vacation and sick leave, on-call and call-back pay, and terminal pay not earned in the final compensation period.

The three reform cases put on hold are a Los Angeles firefighter whose pension was cut after a felony conviction, six judges elected before the reform but who took office after the reform and must pay high new-hire pension rates, and the Marin case.

Like Alameda, the Marin County case is about the reform anti-spiking provisions. But the Marin appellate ruling was issued in August 2016, long before the unanimous appellate ruling in the Alameda case in January last year.

So, why did the high court make the lead case Alameda, which sets a high hurdle for pension cuts, and put the Marin case that contradicts the California Rule on hold, pending a decision on the Alameda case?

An attorney for the firefighters in the air time and Marin cases, Gregg Adam, has said he thinks the likely explanation is that the Marin trial court ruled on a "demurrer" requiring no evidence, unlike the Alameda trial court evidentiary hearing that produced a well-developed file.

"Courts usually prefer to work off a voluminous, well-run trial court record rather than the Marin case, which basically is nothing," Adam said.

Former San Jose Mayor Chuck Reed, whose ballot measure lost a key provision under the California Rule, said last week the court also may think the complicated Alameda case has more parts from which to choose to make rulings than the Marin decision.

Although he is confident the high court will provide some guidance, Reed, a lawyer, said it's not unusual for a big issue to go in and out of the courts several times before final clarification after a decade or so.

Brown said early last year he has a “hunch” the courts will modify the California Rule, so “when the next recession comes around the governors will have the option of considering pension cutbacks for the first time.”

His legal office replaced the state attorney general in the defense of the Air Time ban. An attorney for Brown, Rei Onishi, made the oral argument for the Air Time ban and also intervened in the Alameda case last year on behalf of the govenor’s reform.

Gov. Newsom reportedly told a firefighter group during his campaign last year that he supports the California Rule. His media office did not respond to a question last week about whether Onishi will continue to intervene in the Alameda case in defense of the pension reform.

Reporter Ed Mendel covered the Capitol in Sacramento for nearly three decades, most recently for the San Diego Union-Tribune. More stories are at Calpensions.com. Posted 11 Mar 2019

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Texas Supreme Court affirms ruling that DROP changes at pension fund are constitutional

By Rob Kozlowski · March 11, 2019 4:16 pm · Updated 4:20 pm

The Texas Supreme Court affirmed an earlier state appeals court ruling that changes to the DROP interest rate and distribution policy at the Dallas Police & Fire Pension System that were approved in 2014 were constitutional.

The opinion issued by the state high court on March 8 affirms the December 2016 decision by the court of appeals for Texas' fifth district. In October 2014, the $2.1 billion pension fund's board and 88% of active participants approved reducing the future interest rate paid on DROP accounts to 7% from 8% in 2015, 6% in 2016, 5% in 2017 and potentially lower thereafter. Changes to the DROP distribution policy were also approved to prohibit members from maintaining their accounts indefinitely.

Shortly thereafter, a group of active and retired Dallas police officers sued the pension fund, arguing the changes violated the state constitution's clause that retirement system benefits should not be reduced or impaired. A trial court ruled in favor of the plaintiffs in 2014, but a year later reversed that decision, ruling the changes were constitutional.

In December 2016, the appeals court affirmed that decision, one that came almost a week after the

pension fund board voted to halt withdrawals from the Deferred Retirement Option Plan. High withdrawals from that program helped reduce the pension plan's funding ratio to 36% and led to a pension reform package signed by Texas Gov. Greg Abbott in June 2017. That package included changes to DROP, including limiting participation to 10 years when it was previously unlimited, and no longer allowing retirees to defer payments.

Kelly Gottschalk, executive director of the pension fund, said the fund was "obviously pleased" about the decision since the changes were an "important piece in the solvency of the plan."

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Chicago Symphony Orchestra musicians on strike over pension plan

After 11 months of negotiations over a new contract, the 100 full-time musicians who comprise the famed Chicago Symphony Orchestra walked out on strike at 9:30 p.m. Sunday.

Picket lines went up in front of Orchestra Hall, the CSO's home performance space, at 8 a.m. on Monday morning.

Steve Lester, bassist and chair of the musicians' contract negotiating committee, said the picket line will stretch across all doors of Orchestra Hall for 12 hours a day until a contract "that is fair to musicians" is reached. Lester also requested that no orchestra, performer or patron cross the picket line.

At the core of the dispute is whether a new contract will continue to offer musicians the defined-benefit pension plan that has been in place for more than 50 years and that musicians want to remain in place

BSO Musicians performed at the American Visionary Art Museum to rally support for more financing for the orchestra.
Joanna Sullivan

The Baltimore Symphony Orchestra is facing its own contract battle but has not discussed the possibility of a strike. The orchestra's 74 on-stage musicians and two full-time librarians are still engaged in negotiations with BSO management, which has suggested reducing the orchestra's season from 52 weeks to 40 weeks a year to save money. The Baltimore Symphony Players Committee estimates the change would result in a 20 percent cut to pay and benefits for the musicians.

The CSO board of trustees and orchestra management headed by parent Chicago Symphony Orchestra Association President Jeff Alexander want to replace the defined-benefit plan with a defined-contribution plan, a change CSO musicians have been adamant about rejecting.

But orchestra management and the board insist the pension change is necessary to ensure the orchestra's long-term survival and its financial well-being. Noted Helen Zell, CSO board chairwoman: "We know the financial facts and challenges, and we know that if a change is not made in retirement benefits, there is risk to sustaining the CSO. We have witnessed other organizations that did not act soon enough to address pension issues, and as a result they suffered devastating consequences."

As of Monday, it looked as if a major shift in bargaining stance by either the musicians or management will be necessary to resolve the pension issue and the resulting strike.

No CSO concerts had been canceled as of Monday morning, but CSO music director Riccardo Muti is due back in Chicago this week for concerts with the orchestra starting Thursday.

Muti, who is not a member of the Chicago Federation of Musicians that represents CSO musicians, previously told the CSO board he sides with the musicians on contract issues that have proved divisive.

While admitting disagreement over the pension plan, CSO management said the deal on the table would guarantee CSO musicians a minimum annual salary of $167,000 in the final year of a new contract. In the 2017-18 season, the minimum salary was $159,000.

The CSO musicians strike represents a setback for CSOA President Alexander, who took over at the group in January 2015. Prior to Sunday's walkout, a spokeswoman for the CSO said Alexander had successfully negotiated orchestra contracts for 35 years without a strike and predicted his track record would not be marred.

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TRENDS IN EMPLOYEE TENURE, 1983-2018

This study examines data on employee tenure -- the amount of time an individual has been with his or her current employer -- of American workers. It uses U.S. Census Bureau data from the Current Population Survey (CPS), including the most recent January CPS data, to examine the tenure with current employers of wage and salary workers from 1983-2018. While some believe current American workers change jobs more frequently than was the case for past generations, the data on employee tenure show that individuals holding only one job for their entire career (career jobs) never actually existed for most workers and continue not to exist for most workers. Furthermore, when the labor market has been the strongest, the tenure of workers has tended to be shorter, as more individuals start new jobs by being newly employed or by changing jobs due to more opportunities from a strong economy.

Here are the key findings:

- Over the past 35 years, the median tenure of all wage and salary workers ages 25 or older has stayed at approximately five years.
- This overall trend masks a small but significant decrease in median tenure among men (which had been increasing until declines in 2016 and 2018) and an offsetting increase in median tenure among women.
- The fact that the gender-distinct trends have generally moved in opposite directions has led to overall constancy in the tenure statistics. However, the median tenures by gender have been moving together in recent years.
- The distribution of tenure levels among workers ages 20 or older had been moving toward longer tenures until the most recent years, where shorter tenures have gained share.
- Compared to 2012, median tenure decreased in all groups. In addition, the distribution of worker tenure showed a sizable increase in the lowest levels (two years or less) of tenure. These results indicate that both more individuals have jobs and individuals who had been working changed jobs -- potentially to better jobs -- as the economy has improved, so that the overall tenure distribution has moved to shorter tenures.
- The difference between private-sector and public-sector workers' tenure distributions is quite striking. While private-sector employers in general have been able to maintain a fairly constant and modest percentage of long-term employees (25 or more years of tenure), public-sector employers have seen this group grow significantly through 2004 before trending down through 2018. Consequently, public-sector employers are facing the retirement of a significant number of their most experienced workers, although this

issue is somewhat abating in the most recent years.

- As for career jobs, the highest median tenure level for any age group (15.3 years in 1983 for males ages 55–64) certainly does not cover an entire lifetime career, since the median worker would not have started his or her current job until after age 40. Furthermore, the percentage of workers in both the 55–59 age group and the 60–64 age group with 25 or more years of tenure has been either just above or just below 20 percent at a time that these workers would be ending their working careers. Consequently, approximately 80 percent of workers at these ages have tenures less than 25 years, which would be less than a full working career.
- These tenure results indicate that, historically, most workers have changed jobs during their working careers, and all evidence suggests that they will continue to do so in the future. This persistence of job changing over working careers has several important implications -- potentially reduced or no defined benefit plan payments due to vesting schedules, reduced defined contribution plan savings, lump-sum distributions that can occur at job change, and public policy issues both through lower retirement incomes of the elderly population and the loss of experienced, public-sector workers likely to be retiring soon.
- Although tenure is not a good measure of job security, it does provide insight into how long workers choose to or are allowed to remain with their current employers. This idea is particularly relevant over the last 10 years, as unemployment remained high in 2009–2012, when tenure was generally increasing. However, with the unemployment rate falling in 2012 and continuing through 2018, the percentage of workers with shorter tenures increased. Therefore, now with the decrease in the unemployment rate, more individuals appeared to have entered the labor force or changed jobs.

CRAIG COPELAND, EMPLOYEE BENEFIT RESEARCH INSTITUTE, FEBRUARY 28, 2019.

Private Sector

IRS Notice 2019-18 Allows for Lump Sum Risk Transferring Programs for Participants in Pay Status

On March 6, 2019, the IRS issued Notice 2019-18, which provides that the Treasury Department and the IRS no longer intend to propose regulations generally prohibiting defined benefit plans from replacing any qualified joint and survivor, single life, or other annuity with a lump-sum payment or other accelerated form of distribution for plan participants in pay status. IRS Notice 2019-18 supersedes Notice 2015-49, which stated the intention of the Treasury Department and IRS to propose regulations generally prohibiting retiree lump-sum windows (see Legal Update, IRS Notice 2015-49 Prohibits Plans from Offering Lump Sum Risk Transferring Programs for Participants in Pay Status).

Required Minimum Distributions (RMDs)

Section 401(a)(9)(A) of the Internal Revenue Code (Code) requires employer-sponsored retirement plans to include required minimum distribution (RMD) rules in their plan documents and comply with those rules to maintain their tax-qualified status under the Code (26 U.S.C. § 401(a)(9)(A)). Under the RMD requirements of Code Section 401(a)(9), plan participants must begin taking distributions from those plans annually, starting with the later of the year in which the participant:

- Reaches age 70½.
- Retires from employment.

(26 U.S.C. § 401(a)(9)(A); see Practice Note, Required Minimum Distributions from Retirement Plans.) However, the actual payment of that first year's RMD may be deferred until the participant's required beginning date (RBD). The RBD for most participants is April 1 of the calendar year following the participant's first distribution calendar year (see Practice Note, Required Minimum Distributions from Retirement Plans: Required Beginning Date (RBD)). Once a participant's RBD is determined, he must take distributions for the first distribution calendar year and every year thereafter, unless there is an applicable exception (for more information, see Practice Note, Required Minimum Distributions from Retirement Plans: Annual Distributions Required).

Once the periodic annuity payments begin:

- Annuity payments generally may not increase over time. However, the Treasury Regulations provide several situations when the payments may increase (see Practice Note, Required

Minimum Distributions from Retirement Plans: Modifying and Increasing Annuity Payments).
- Annuity periods may only be changed if the stream of annuity payments otherwise satisfies the RMD rules and in specific circumstances under the regulations (see Practice Note, Required Minimum Distributions from Retirement Plans: Modifying Annuity Interval Periods).

Code Section 401(a)(9) and the related Treasury Regulations are intended to ensure that:

- The distribution of an employee's benefit will not be unduly tax-deferred.
- The employee's annuity will not be converted to a lump-sum payment or otherwise accelerated, except in cases of retirement, death, or plan termination (26 C.F.R. § 1.401(a)(9)-6, A-13(a), (b)).

Any plan participant who fails to properly receive an RMD is liable for an excise tax equal to 50% of the difference between the actual amount distributed and the RMD for the relevant tax year, though the penalty may be waived in certain situations (see Practice Note, Required Minimum Distributions from Retirement Plans: RMD Requirements and Penalties).

Lump-Sum Windows

Some defined benefit plan sponsors have amended their plans to include lump-sum risk-transferring programs, which provide a limited window of time during which certain retirees receiving joint and survivor, single-life, or other life annuity payments may elect to convert the annuity into a lump sum that is payable immediately (see Practice Note, Defined Benefit Plans: Lump-Sum Windows).
By reducing the number of participants entitled to receive benefits from the plan, lump-sum windows are one option for defined benefit plan sponsors that want to "derisk" their plans. By accelerating the annuity payments, lump-sum windows transfer longevity and investment risk from the plan to the retirees. In some cases, the addition of these programs has been treated as a permissible increase in benefits under Treasury Regulation Section 1.401(a)(9)-6, A-14(a)(4) (26 C.F.R. § 1.401(a)(9)-6, A-14(a)(4)).

Notice 2015-49

In Notice 2015-49, the IRS stated that it intended to amend the regulations under Code Section 401(a)(9) to generally prohibit lump sum risk transferring programs for participants in pay status as of July 9, 2015 (see Legal Update, IRS Notice 2015-49 Prohibits Plans from Offering Lump Sum Risk Transferring Programs for Participants in Pay Status). Specifically, the regulatory changes that the Treasury Department and IRS intended to propose included amendments to Treasury Regulation Section:

- 1.401(a)(9)-6, A-14(a)(4), which would have allowed only limited changes to the annuity payment period under Code Section 401(a)(9).
- 1.401(a)(9)-6, A-13, which would not have permitted acceleration of annuity payments.

These amendments would not have applied to accelerations of ongoing annuity payments under a plan

amendment adopted before July 9, 2015, which was the effective date of Notice 2015-49. Notice 2015-49 also provided that the IRS would not express an opinion in private letter rulings or determination letters regarding the federal tax consequences of a retiree lump-sum window.

Notice 2019-18

Notice 2019-18 states that the Treasury Department and the IRS no longer intend to propose the amendments to the regulations under Code Section 401(a)(9) that were described in Notice 2015-49. The Treasury Department and the IRS will continue to study the issue of retiree lump-sum windows. Until further guidance is issued, the IRS will not:

- Assert that a plan amendment providing for a retiree lump-sum window program causes the plan to violate Code Section 401(a)(9), but the IRS will continue to evaluate whether the plan, as amended, satisfies the requirements of Code Sections 401(a)(4), 411, 415, 417, and 436, among other sections (see Practice Note, Requirements for Qualified Retirement Plans).
- Issue private letter rulings regarding retiree lump-sum windows. However, if a taxpayer is eligible to apply for and receive a determination letter, the IRS will no longer include a caveat in the letter expressing no opinion regarding the tax consequences of a lump-sum window (see Retirement Plan Determination Letters Toolkit).

Practical Implications

Practitioners should be aware that Notice 2019-18 includes a retraction of intent by the Treasury Department and the IRS regarding proposed regulations under Code Section 401(a)(9) that would have limited accelerated forms of distribution to participants in pay status but allowed them for participants who had not yet begun to receive their benefit payments. Under Notice 2019-18, these proposed regulations will not be issued, which means that lump-sum windows may still be available for defined benefit plan sponsors.

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American workers stressed about finances, look to Congress for help

March 25, 2019

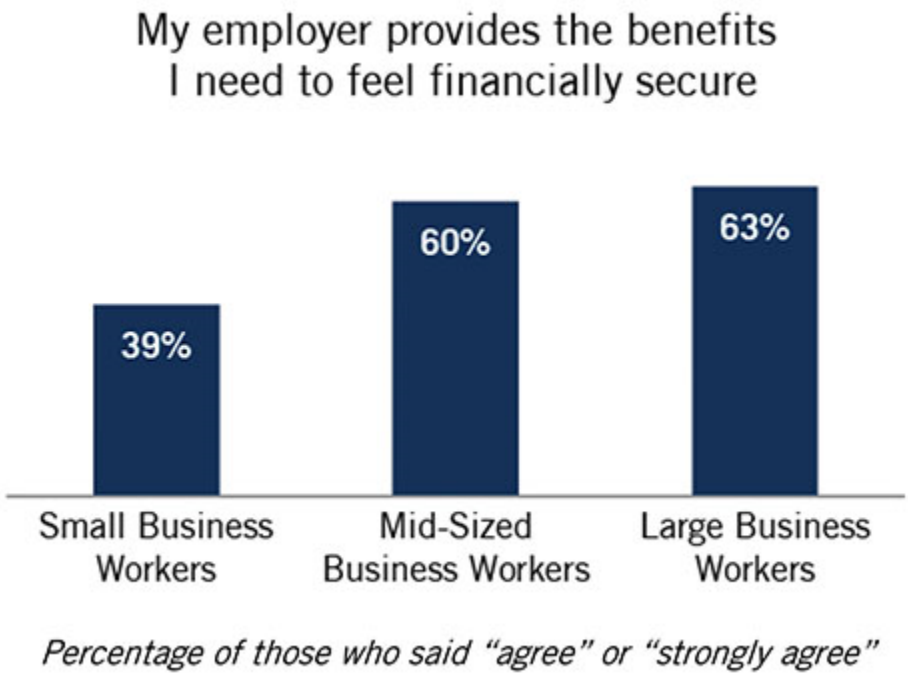
Making it easier to save for retirement is top issue workers want Congress to address, according to new survey results

American workers are gravely concerned about their financial security, particularly in retirement. And they're counting on both Congress and their employers to provide solutions.

The sixth *American Workers Survey*, conducted in February on behalf of Prudential by Morning Consult,

illustrates the depth of their fears.

Seven in 10 respondents say they've felt stressed about their finances in the past year. An even greater number—more than 80 percent of working parents—are concerned about their children's financial security as they grow up. And retirement security remains a primary focus, with nearly seven in 10 respondents saying they are concerned they will not have enough money to live comfortably in retirement.



While the workplace is increasingly one of the primary places in which people access offerings to enhance their financial security, many employees of small businesses lack access to these offerings. Only 39 percent of small business workers say their company provides the benefits they need to feel financially secure, compared to 63 percent of workers at large businesses.

Against this grim backdrop, workers overwhelmingly want Congress to pursue policies that make it easier to save for retirement. Nearly eight in 10 workers say Congress should do more to expand access to retirement plans. Provisions included in the Retirement Enhancement and Savings Act (RESA), which was recently reintroduced, would make it easier for small businesses to join together to offer retirement plans through open multiple employer plans (MEPs). This would expand access to plans, helping to close the retirement savings gap. Additionally, 68 percent believe policymakers should support retirement solutions that convert savings into a stream of lifetime income payments.

"The challenge of saving for retirement, and the concern and stress that it imposes on workers, is a recurring theme in our surveys on barriers to workers' financial security," says **Ann Kappler**, deputy general counsel and head of external affairs for Prudential. "This survey in particular highlights the increasing urgency for Congress to address retirement security."

The survey results also revealed that workers say they're looking to their employers to provide tools that support their financial wellness, particularly saving for retirement. A majority of workers (53 percent) say they would not work for a company that didn't provide a retirement plan. And among employer-provided programs, workers rank retirement plans (74 percent) and life insurance (56 percent) as the most valuable in supporting their financial well-being.

"There is a compelling need—and support—among workers for measures to increase access to retirement plans, especially for small business employees," notes Kappler. "Prudential has long supported policies that would expand Americans' access to retirement savings, such as those that would increase sponsorship and participation in multiple employer plans (MEPs). As a leading provider of financial wellness solutions, we will continue championing much-needed retirement security legislation, to help put financial security within reach for more American workers."

See the sixth *American Workers Survey* Fact Sheet for more of the survey findings. For more information on the results of this survey, contact Andrew Simonelli.

The American Workers Survey is the sixth in a series conducted on behalf of Prudential by Morning Consult from February 8 to 19, 2019, among a national sample of 2,217 self-identified part-time and full-time employed adults (age 18 and over). The interviews were conducted online, and the data was weighted to approximate a target sample of adults based on age, race/ethnicity, and gender. Results from the full survey have a margin of error of ±2 percentage points. In this survey small businesses are defined as companies with less than 100 employees; mid-sized businesses are defined as companies with 100-999 employees and large businesses are defined as companies with over 1,000 employees. Percentages may not total 100 percent due to rounding.

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De-risking in 2019

March 19, 2019

In this article we discuss how changes in interest rates, Pension Benefit Guaranty Corporation premiums and mortality assumptions may affect sponsor decisions to de-risk (or not de-risk) defined benefit plan liabilities in 2019. For purposes of this article, by de-risking we mean paying out a participant's benefit as a lump sum and thereby eliminating the related liability.

We begin with a brief summary of our conclusions, followed by a more detailed analysis.

Summary

We illustrate our analysis of the effect of interest rates and PBGC premiums on the de-risking decision by using a (relatively simple) example: the cost-of-benefit and de-risking gain with respect to a terminated vested 50-year-old individual who is scheduled to receive an annual life annuity of $1,000 beginning at age 65.

We note that IRS recently published Notice 2019-18, which states that it "will not assert that a plan amendment providing for a retiree lump-sum window program causes the plan to violate [the RMD rules]." The analysis provided below would generally apply to lump sum payments to retirees as well.

For our example participant, increases in interest rates (November 2017 vs. November 2018) have reduced the 2019 base cost of paying this participant a lump sum benefit, vs. 2018, by around $1,200. On our assumptions, if a 50-year-old individual with a $1,000 benefit had been paid out in 2018, the cost would have been $7,867; in 2019 the cost would be $6,671.

Most of the savings from de-risking this participant come from reduced PBGC premiums – an (assumed) present value of $1,885 in PBGC flat-rate premiums and $2,578 in PBGC variable-rate premiums (only available to plans subject to the variable-rate premium cap).

In addition, for 2019 lump sum calculations there was an increase in the applicable mortality assumption, which will result in a decrease in lump sum costs. For our example participant that savings would further reduce the cost of paying out the participant in 2019 vs. 2018 by around $30.

The de-risking calculation is, of course, relative and dependent on the sponsor's view of, e.g., future interest rate trends and the cost/savings of paying a participant all benefits this year vs. paying them next year vs. simply paying them when due (e.g., beginning at age 65). In this regard we note that market interest rates (as of February 2019) are down around 40 basis points relative to November 2018. All in all, 2019 looks like a relatively good year (certainly relative to 2018) to de-risk.

What follows is a detailed discussion of these conclusions.

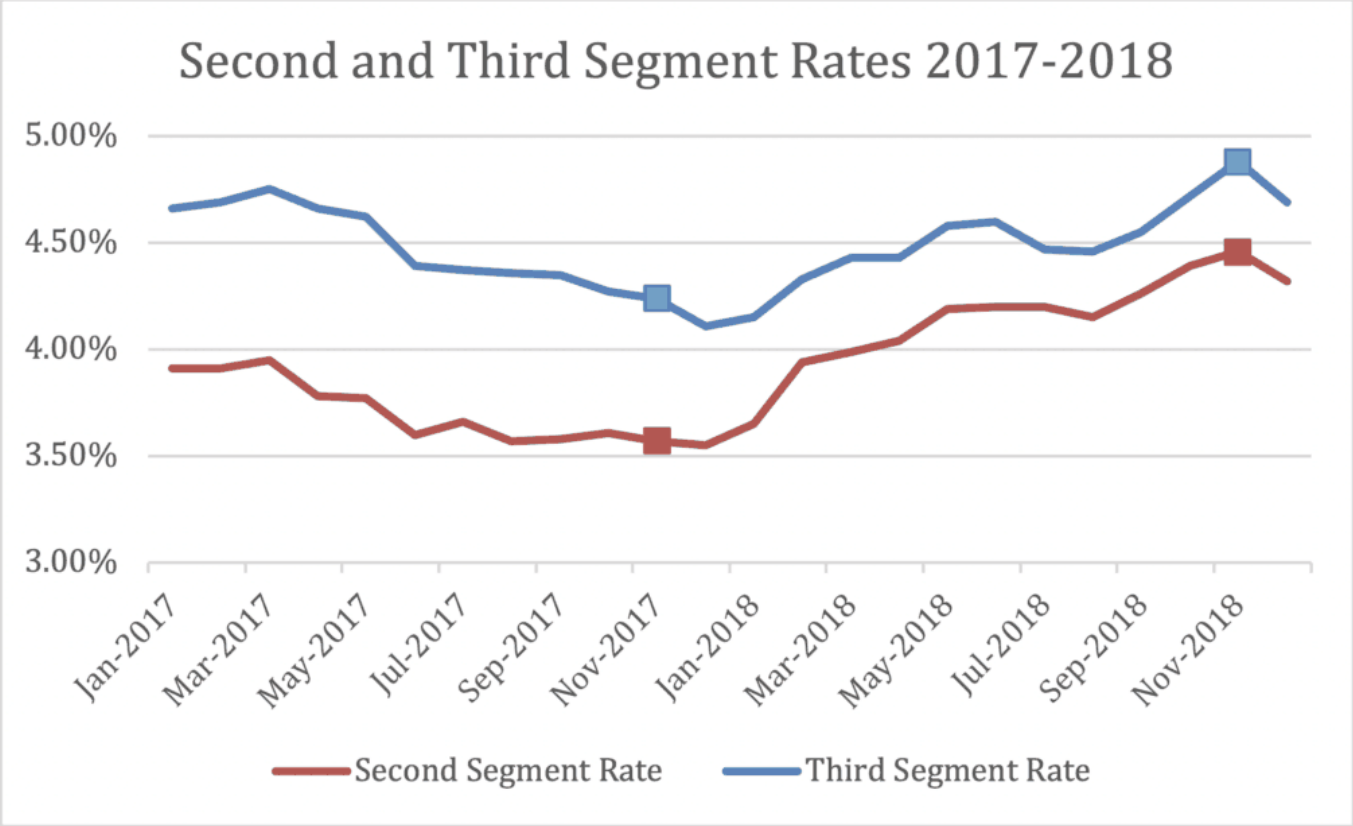
Interest rates

De-risking involves paying out the present value of a participant's benefit as a lump sum. The interest rates used to calculate that present value are the Pension Protection Act (PPA) "spot" first, second and third segment rates for a designated month. Many sponsors set the lump sum rate at the beginning of the calendar year, based on the spot rates in a prior year "lookback" month, so that participants will

know what rate will be used to calculate their lump sum for the entire year. A plurality of plans use a November lookback month, which we use in our example. Under such an approach, for 2019 the lump sum rates would be the November 2018 PPA spot rates.

The following chart shows PPA spot second and third segment rates for the period 2017-2018 (with November rates highlighted).

PPA monthly average interest rates



As this data indicates, November 2018 interest rates were up significantly vs. November 2017 rates. (We note that the increase in 2018 rates was significant across all lookback months; the November 2017-November 2018 increase was, however, the greatest.)

As noted, based on these rates, the cost of de-risking our example participant decreased from $7,867 in 2018 to $6,671 in 2019.

(For purposes of this calculation, rather than doing a strict Tax Code 417(e) calculation, we simply

assume the participant has a 21-year life expectancy at age 65.)

PBGC premiums

Reducing participant headcount, e.g., by paying out lump sums to terminated vested participants, reduces the PBGC flat-rate premium and may, depending on plan funding and demographics, reduce the variable-rate premium. Premiums for the current year are based on headcount for the *prior* year. So de-risking in 2019 will reduce premiums beginning in 2020.

PBGC flat-rate premiums

We are estimating the 2020 PBGC flat-rate premium to be $82 (the 2019 rate of $80 adjusted for one year of wage inflation).

For purposes of our analysis we assume no inflation-related increases in PBGC premiums. We use a discount rate of 2.5%, which generally assumes low or no inflation.

Discounting annual premiums for 36 years (assuming our example 50-year-old participant lives to age 86) yields a present value of the savings from the elimination of PBGC flat-rate premiums for our example participant of around $1,885.

Variable-rate premiums

In our article Reducing pension plan headcount reduces risk and PBGC premiums we discuss how de-risking can, in some cases, dramatically reduce the variable-rate premium. The logic of that is not especially intuitive. The gains come from the headcount-based cap on variable-rate premiums. We estimate (again, based on one year wage inflation) the 2020 headcount cap to be $555. Oversimplifying (and again ignoring any future inflation adjustment to the cap), depending on plan funding and demographics, de-risking (that is, lump summing-out) one participant in 2019 may save a sponsor $555 *per year* in PBGC premiums beginning in 2020.

As plan funding improves, however, these savings will go away. For purposes of our example we assume the plan "funds its way out" of the per participant variable-rate premium cap after 5 years. Discounting annual premiums of $555 for 5 years yields a present value of around $2,578.

Effect of changing mortality improvement scales

On October 20, 2017, the Society of Actuaries adopted a new mortality improvement scale (MP-2017),

showing an *increase* in mortality over MP-2016. Quoting the SOA: "most 2017 pension obligations calculated using Scale MP-2017 (with a discount rate of 4.0%) are anticipated to be approximately 0.7% to 1.0% lower than those calculated using Scale MP-2016." On December 15, 2017, IRS updated applicable mortality tables for 2019, to reflect the SOA's new scale. As noted, based on the new mortality improvement scale, we estimate that the cost of de-risking our example participant decreased by around $30in 2019.

* * *

Increases in lump sum valuation interest rates have made de-risking in 2019 significantly less expensive than it was in 2018. It is also less expensive vs. a lump sum valuation made using current (first quarter 2019) interest rates. Changes in mortality assumptions in 2019, vs. 2018, have also reduced the cost of lump sums. Sponsors will want to consider these factors in making their 2019 de-risking decision.

We will continue to follow this issue.

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Payment of Defined Benefit Plan Benefits After Normal Retirement Age

By Elizabeth G. Kennedy and Brian J. Dougherty
March 18, 2019

It is apparent from the extensive investigation of defined benefit plans on the part of the US Department of Labor (DOL) that the DOL is quite focused on timely payment of plan benefits to participants. The DOL is interested not only in when benefits begin, but in how a participant is made whole when benefits begin after normal retirement age. A defined benefit plan must generally increase a normal retirement benefit actuarially where payment begins after a participant's normal retirement age. The Internal Revenue Code (Code) and underlying regulations, however, allow a plan to pay instead the normal retirement benefit amount plus make-up payments in some instances. In light of the DOL's scrutiny in this area, it may be wise for plan sponsors to review pertinent plan provisions and operation to make sure they comply with applicable rules.

Section 411(c)(3) of the Code provides that where a participant's benefit under a defined benefit plan is to be determined as an amount beginning on a date later than the participant's normal retirement age, the benefit must be actuarially increased.

There is an exception to this rule where a participant remains employed after his normal retirement age, and the plan contains and properly administers a suspension of benefits provision under Section 411(a)(3)(B) of the Code and Section 203(a)(3)(B) of ERISA and its underlying regulations. A suspension of benefits provision allows a plan to refrain from paying normal retirement benefits during certain

periods of employment (called "Section 203(a)(3)(B) Service") and/or to discontinue payment of normal retirement benefits to retirees who return to Section 203(a)(3)(B) Service. Section 203(a)(3)(B) Service is, under a single employer plan, any month or four- or five-week payroll period after normal retirement age during which an employee completes 40 or more hours of service or receives payment for hours of service performed on eight or more days in such month or payroll period. Treasury Regulations § 1.411(c)-1(f)(1) provides that no actuarial increase is required for periods of suspension of benefits.

Treasury Regulations § 1.401(a)-14(d) provides some relief from the Section 411(c)(3) actuarial increase requirement where benefit payment is unavoidably delayed. If a participant's benefit is to be paid by default under Section 401(a)(14) of the Code or in accordance with the participant's election, and the benefit cannot be ascertained by the payment date or the participant cannot be located by the payment date after reasonable attempts to locate him, the plan may make a retroactive payment (to the date payment should have begun) within 60 days after the date the participant's benefit can be ascertained or the date the participant is located. Since the benefit would be calculated as of the retroactive date, there is no actuarial increase (however, the retroactive payments should be calculated with interest).

In addition, a defined benefit plan is permitted under Treasury Regulations § 1.417(e)-1(b)(3)(iv) to specifically base benefits on a retroactive annuity starting date if certain requirements are met. A retroactive annuity starting date (RASD) is a date that occurs before a participant is provided with a written qualified joint and survivor annuity but on which he would otherwise be able to begin receiving benefits under the plan. A plan that contains a RASD provision may, for example, permit a terminated vested participant to elect his employment termination date as his retroactive annuity starting date. The plan would then begin paying a benefit calculated as of the participant's employment termination date and provide make-up payments (plus interest) for the period from his employment termination date to the current date. If the RASD is the participant's normal retirement date, the RASD provision would serve to eliminate the Section 411(c)(3) actuarial increase for the participant because the benefit would be calculated as though it had begun on the participant's normal retirement age. The participant would, however, be made whole through the make-up payments.

It is always important to administer a plan according to its terms, as well as Code provisions and pertinent regulations. The DOL's current audit campaign has served to identify which areas it deems particularly significant. Now is a good time for plan sponsors to thoroughly review how their plans handle post–normal retirement age benefit payments, and put in place new practices if they will align better with plan sponsor objectives.

If you have questions about how to address post–normal retirement age benefits, please reach out to the authors or your Morgan Lewis contact.

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404(a)(5) Participant Fee Disclosures: Rules & Requirements

When it comes to 401(k)s, transparency is crucial - especially when it comes to fees.

After all, over 35 years, even an innocent-sounding 2% fee can consume up to half of the returns from the retirement savings you worked so hard for.

That's why the government requires plan sponsors to disclose ALL the fees participants are paying. Of course, doing this yourself would be a nightmare (both from a fiduciary standpoint, and with all the work it'd take). Luckily, your 401(k) providers should do all of the work for you by sending their 404(a)(5) participant fee disclosures!

But wait... what the heck is a 404(a)(5) participant fee disclosure? And what are the requirements around sending them? Don't worry we'll demystify this important document, breaking down what it is, why it's important, and everything else you need to know about sending it. Ready to get started?

What is a 404(a)(5) Participant Fee Disclosure?

Quick Definition:

Department of Labor (DoL) regulations require that a retirement plan's participants are provided with timely and comprehensive information about their investment fees. This is fulfilled in the form of a 404(a)(5) participant fee disclosure.

Important note: A fee disclosure has to show all the fees that participants face - from custodial and recordkeeping fees to investment expenses.

All About the Participant Fee Disclosure Process

How It's Made:

All jokes aside, quite a bit of information (i.e work) goes into a typical fee disclosure, so it's a good thing you (the plan sponsor or administrator) don't have to do that part.

The 404(a)(5) fee disclosure is typically put together by the recordkeeper. It's then sent along to the plan sponsor, who then distributes it to the plan participants.

Important Note: Do NOT change anything. If any of the information is incorrect or throws up other types of red flags, this is something to mention to your recordkeeper or TPA. Just don't try to amend a fee disclosure - doing so could create fiduciary risk.

404(a)(5) Participant Fee Disclosure Distribution Methods

Bad news: Even though the recordkeeper does the hard work, plan sponsors still have the duty to get the fee disclosures to participants.

Good news: Electronic distribution methods are allowed, so often that duty is actually really easy and/or almost automatic. However, it won't come as a surprise that there are some rules you have to follow for electronic sending. These are:

- The recipient must have access to the document on a work computer
- OR must have been given a computer for work
- OR must have opted in for electronic delivery.

If none of these methods are available (or if your company likes tradition) then you can send hard copies to your employees via the mail.

In essence, you just have to make sure that participants have the easiest possible access to the fee disclosure information. It's all about transparency, after all.

Who's Responsible for Sending These?

The plan sponsor has the duty to distribute the fee disclosure to all participants and account holders with control of their accounts (this includes other beneficiaries with direct management of the funds).

Sounds simple, but there a few different things to keep track of...

Different Participant Fee Disclosures, What's Required, and When

Types of Fee Disclosures	Purpose and Contents	When is This Sent?
Initial and Annual Fee and Investment Disclosure Notification	General plan info, admin fees, participant-level fees, investment fees, and related expenses.	On or before the participant gains access to and control of their retirement account assets. Every 14 months (due to a recent 2-month extension).
New Participant Fee Disclosure	This disclosure informs new employees - it's got the same information as the Annual Fee Disclosure.	Provided prior to eligibility or as part of the automatic enrollment/new-hire paperwork.
Fee Change Disclosure	This is a disclosure to update plan participants on any fees that have recently been changed	No less than 30 (but not more than 90) days BEFORE any changes are due to take effect. Be preemptive with the notification, but not so early that it's actually inconvenient to plan for (like a wedding invitation 3 years in advance).
Quarterly Fee Disclosure	Information on the quarterly statement - including the dollar amount they actually paid for general administrative fees.	Pretty simple - every quarter.

How Participant Fee Disclosures Impact Employee Benefits

Fee disclosures are all about transparency - and that's because transparent fees help participants pick the best options and save more money - the whole point of retirement savings.

In fact, the DoL has estimated $14 billion in savings to participants in 10 years as a result of fee disclosure rules. The vast majority of the savings, according to the DoL, come from the access to information and increased ability to choose lower cost investments. Information is power (or in this case, money)!

Remember, as plan sponsor, you have the fiduciary responsibility to act in the participant's best financial interest. That means asking yourself the all-important question... "Are my plan participants paying reasonable fees?"

Conclusion

Fee disclosure rules may be relatively new - but they're in place because of a greater need for transparency.

Transparent fees show employees exactly what they're taking home, and ultimately help plan sponsors fulfill their fiduciary duty to act in the financial best interests of their plan participants. That means, first and foremost, reasonable fees for 401(k) services.

If you'd like to check whether or not your 401(k) fees are reasonable, try our 401(k) fee calculator! Just answer two quick questions and instantly receive estimates for a low-cost plan tailored to your business on three major providers!

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