



Bill Introduced to Fix Public Safety Tax Issue

On September 9, Sen. Bill Nelson (D-FL) introduced a bill to fix certain tax issues related to passage of the Pension Protection Act of 2006. The bill, S. 1657, amends the Internal Revenue Code to fix unintended changes to Section 828 of the PPA. Section 828 of the Pension Protection Act of 2006 amended 26 U.S.C. 72(t) to allow retired public safety employees beginning at age 50 to take distributions from their defined benefit pension plans without paying the 10 percent early distribution tax. Section 828 recognized that—due to the nature of the profession and in many cases mandatory retirement ages—public safety employees typically retire earlier than the general population, and therefore should have access to their retirement benefits without penalty.

Unfortunately, since implementation of the PPA, two issues have arisen that need to be fixed. First, public safety employees between the ages of 50 and 55 who chose to rollover their distributions into a 457 plan and then take distributions from the 457 plan are subjected to the 10 percent early distribution tax until age 59 1/2. Second, public safety employees who retired before age 55 and before enactment of Section 828 and opted

to annuitize their benefit to avoid the 10 percent early distribution tax—and who after the enactment of Section 828 decide to take a modified distribution from their plans—are subjected to a 10 percent recapture tax on the previous annuitized distributions.

At issue here is the wording of the Pension Protection Act at Section 828, which was written such that the exemption on the 10 percent tax penalty was available only if the distribution was made from a defined benefit plan. Senator Nelson's bill removes the requirement that disbursements be made from a defined benefit plan, and further exempts from the 10 percent recapture tax qualified retired public safety employees who opted for annuitized benefits prior to enactment, but now want to modify their distribution.

NCPERS, IAFF, the Miami Police & Fire Pension Fund, the Houston Fire Fighters Relief & Retirement Fund and the Dallas Police & Fire Pension Fund all have been working to bring the issue to the attention of Members of Congress and urging them to help provide relief on the unintended consequences of Section 828.

The bill, which is a companion bill to one introduced earlier this year by Representative Kendrick Meeks (D-FL), was referred to the Senate Committee on Finance. NCPERS continues to advocate for this legislation on Capitol Hill. In concert with the coalition, NCPERS is leading the effort to find legislative vehicles to pass this important bill.

GASB Hearings on Public Pension Accounting and Reporting

This summer, the Governmental Accounting Standards Board heard testimony on whether it is necessary or appropriate to change financial reporting and pension accounting requirements for public pension. Proponents of an overhaul argued that transparency and comparability were key issues that would result from new standards for public pension disclosure. State officials and others testified that broad changes were unnecessary and would prove disruptive to the governmental budgeting process by introducing increased market volatility into pension accounting.

The hearings were held in conjunction with the GASB's

Invitation to Comment (ITC) on Pension Accounting and Financial Reporting. Written comments on the ITC were due by July 31, with an initial hearing set for August 26 in Connecticut. In order to accommodate the high level of interest in testifying on the ITC, GASB convened a second hearing in Washington, DC. NCPERS provided written comments and was present at the hearings in Washington.

At the Connecticut hearings, Robert A. Wylie, executive director of the South Dakota Retirement System, said that pension funding issues seen in funds across the nation were largely absent in his state and that his plan had a well-established, flexible funding policy. He argued that changing the procedures for accounting and reporting are unnecessary and that the current standards are appropriate and “very workable.”

Many feel that based on the questions the board members asked that it was not likely they would move toward making wholesale changes to the existing rules. Instead, it seems more likely that the GASB may vote to make narrower changes to the Standards, such as shortening amortization schedules or reducing the number of actuarial methods that plans may use.

On the largest point of contention—whether a specific discount rate, such as the Treasury rate, should be used—the Board seemed disinclined

to take up the matter head-on. Linda Kopp, Treasurer of the State of Maryland and Chair of the Board of Trustees of the Maryland State Retirement and Pension Systems, testified in the Washington hearing that the basis for the discount rate should be the long term yield of the plan, and not an arbitrary “risk-free” which saddles the fund with a termination liability, as opposed to a rate that reflects a pension plan that is ongoing. She noted that while corporate plans are far riskier because the plan sponsor may go out of business, that isn’t the case with governmental plans, pointing out that the State of Maryland was established before the United States was created.

The task at hand for GASB now is to review the written and oral comments before determining whether it will make any changes and, if so, to what extent. The Board’s next step likely will be to issue a Preliminary Views document, stating the Board’s position on various aspects of the ongoing project. Lastly, if the Board does decide to make changes, it would issue an Exposure Draft, which indicates the changes to standards expected to be made and provides one last opportunity for the public to comment before the changes are made. It is not likely that an Exposure Draft would appear before the summer of 2010.

NCPERS has been and will continue to be involved in the process as

GASB determines whether the pension funds require new accounting and reporting standards, and will continue to provide coverage of the issue as developments occur.

Public Funds Meet with Treasury Officials

On Friday, September 11, NCPERS and others representing the public pension fund community in Washington, DC met with Mark Iwry, a senior advisor to Treasury Secretary Timothy Geithner and Deputy Assistant Treasury Secretary for Retirement and Health Policy. Also representing the Treasury were Bill Bortz, Associate Benefits Tax Counsel, and Harlan Weller, a Treasury Department actuary. The meeting was requested to discuss ways that the Treasury, IRS and the public plan community could better work together.

In addition to NCPERS, representatives from NASRA, NCTR, AFSCME, IAFF, Government Finance Officers Association, National Education Association, National Conference of State Legislatures, National League of Cities, National Association of Counties, National Association of Police Organizations, CalPERS, CalSTRS, and the District of Columbia Retirement Board attended the meeting.

Foremost on the agenda was the IRS compliance survey project embarked

upon by that agency more than 18 months ago. In early 2008, IRS convened a roundtable with representatives of public funds to discuss the traditionally “underserved” public plan community. At the time, IRS suggested that it wanted to work in a cooperative effort. At that meeting, IRS also announced its intent to create a survey on tax qualification that it wanted to send to public plans. The survey, however, was developed without any input from the public plan community, and was delivered to NCPERS, NASRA, and NCTR who were told to keep the survey secret and provide comments within 24 hours. The survey, with some modifications, has since been sent to 25 public plans around the country.

During discussion, the group reiterated its contention that IRS was asking for information out of its purview, that it was seeking to keep the public fund community at arm’s length through the process, and was taking enforcement action through the compliance survey before guidance had been provided. And despite the community’s many offers to help in formulating the survey as well as providing correct mailing addresses for intended recipients of the survey, the IRS chose to not avail itself of the offers. As such, the Service likely received erroneous information from those that completed the survey, and in more than one instance, sent the survey to recipients unrelated to the pension fund targeted.

Other issues discussed included concerns about implementation of the Normal Retirement Age regulation, which has been delayed; concerns about the recently implemented Report of Foreign Bank and Financial Accounts (FBAR), which would require pension funds to report to IRS any foreign holdings to IRS; and the definition of government plans, which the agency has been working on for more than four years.

Iwry indicated that the stated concerns were valid and pledged to be both more cooperative and more responsive to the community’s needs. He also pointed out that President Obama and Treasury Secretary Geithner were both strong proponents of secure retirement, noting the introduction a week prior of the Administration’s initiatives to help citizens save more for retirement. He said that those initiatives were only the beginning of and that the administration expected to embark on a more comprehensive review of retirement policy—and that suggestions from the public fund community were not only welcomed, but encouraged.

To show that Treasury and the Service are serious about working cooperatively, Iwry suggested a follow-up meeting, which will include representatives from Treasury and the Employers & Plans division of IRS, to discuss in-depth some of the concerning issues presented by the plan community.

That meeting is expected to take place later this month.

New Survey on Health and OPEB Funding Strategies

According to a new survey partially funded by NCPERS, approximately 49 percent of the nations’ cities, counties and townships expect less revenue in 2010, 21 percent expect fewer employees, and about 26 expect increased consolidation of local services. With shrinking budgets and fewer staff, local officials are taking several approaches to contain long-term costs associated with employee and retiree health care.

The *Health and OPEB Funding Strategies: 2009 National Survey of Local Governments* report is based on responses from more than 1,500 city, county, township and special district governments across the country. The study was conducted by Cobalt Community Research, a leading nonprofit research organization based in Lansing, Michigan.

“There are significant changes from last year’s study,” said William SaintAmour, executive director of Cobalt Community Research, which conducted the survey. “We’re seeing belt tightening and growing awareness of benefit costs.”

The report examines local governments’ awareness of and responses to growing health costs

and liabilities. It also helps inform public employers about national OPEB accounting requirements and current practices used by local governments to control health care costs.

According to the Cobalt study, approximately 78 percent of the survey respondents provide health care to their employees, with 30 percent also providing health care to retirees. Larger local governments are more likely to provide such benefits.

The study found many local governments are considering one or more health care cost-containment

strategies, including increasing health insurance deductibles and co-pays, increasing employees' share of premium costs, implementing wellness programs, expanding use of generic drugs, and implementing health savings accounts (HSAs) and health reimbursement arrangements (HRAs)

Few respondents plan to eliminate benefits.

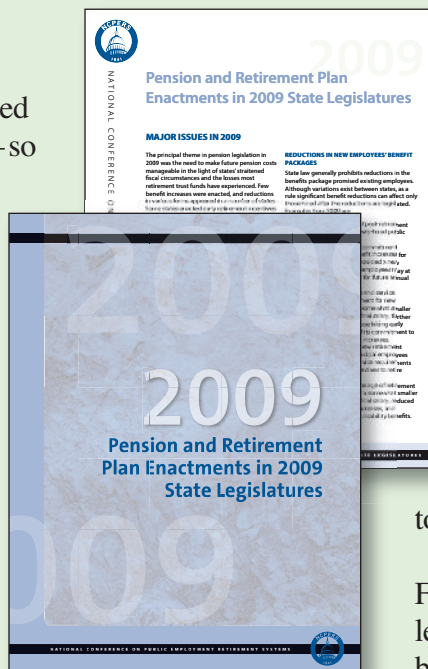
“Clearly, the study shows activity, but many cost-reduction strategies are still untapped,” said SaintAmour. “For example, only 27 percent of respondents increased deductibles

over the past two years, only 19 percent implemented wellness programs and only 15 percent expanded the use of generic drugs.” Others sponsoring the survey included Gabriel Roeder Smith & Company, Government Finance Officers Association, Employee Benefit Research Institute, International Foundation of Employee Benefit Plans, Municipal Employees’ Retirement System of Michigan, and Tegrit Financial Group.

To view a copy of the study, please visit www.NCPERS.org/files/OPEB_2009.pdf.

State Legislative Report Available

NCPERS produces a compendium of state legislative initiatives—updated three times during the year—so that NCPERS members are aware of the retirement-related bills other state legislatures are considering or have passed. We recently published *Pension and Retirement Plan Enactments in 2009 State Legislatures*, which has information on the retirement and employee benefits legislation that has been enacted through the middle of the year. For example, Texas initiated an




employee contribution in the previously non-contributory plan for law enforcement personnel and the Illinois legislature voted to issue \$3.5 billion to cover employer costs for pension plans. The states of Georgia, Louisiana, Nevada, New Mexico, Rhode Island and Texas all have reduced, to some degree or other, benefits for new hires. And 10 states and Puerto Rico created study commissions to report on public DB issues such as solvency of funds, funding levels, and conversion of DB to DC plans.

For more information on state pension legislation this year, the report can be found on the NCPERS website by visiting


www.NCPERS.org/files/Legis_Enact2009.pdf.

Arkansas




The head of the Arkansas Teacher Retirement System wants an attorney general's opinion on whether the system can legally collect millions of dollars from some retirees. The retirees returned to work but failed to report their earnings as required under state law. The law was changed July 1. Until the change was made, teacher system retirees were required to have \$1 of their pension withheld for every \$2 they earned above a limit set by state law. That limit was \$27,120 last year. ATRS director George Hopkins says many of the retirees didn't know they were subject to the income limit.

Florida




Pension assets overseen by Florida's State Board of Administration now stand at approximately \$111 billion—the amount managers forecast earlier this year would be enough to cover the forecasted costs of pensions for future retirees. As of late September, the SBA pension funding ratio was 100 percent, compared with 93 percent on June 30 and 106 percent at the end of June 2008. Assets in the fund, one of the largest public pension systems in the United States, touched a low of \$83 billion on March 9. Actuaries are now preparing a formal report based on the June 30 asset values and projected payouts that should be released in November.

Kansas



Gov. Mark Parkinson has indicated that he opposes moving Kansas toward 401(k)-style pension plans for teachers and government employees. Parkinson's administration is studying ways to deal with long-term funding problems faced by the Kansas Public Employees Retirement System. Parkinson, though, dismissed the idea of getting away from guaranteeing benefits based on employees' salaries and years of service, regardless of KPERS investment earnings. The Democratic governor's comment puts him at odds with GOP House leaders who want to consider 401(k)-style plans, at least for new teachers and government employees. At the end of 2008, the gap between income and benefit payments over the next 25 years was projected to be \$8.3 billion, according to KPERS.


Iowa



Senate Democratic Leader Mike Gronstal of Council Bluffs says legislators will consider a variety of options to address the shortfall in the Iowa Public Employees Retirement System, which saw a reduction of four-billion dollars in 2008. "While I understand people being nervous, we want to assure them we're going to go through a deliberative process. We're going to listen to folks," Gronstal said. "We're going to listen to the

recommendations of IPERS and try, just as we have always, to maintain the long-term solvency of our system." Two years ago the legislature increased the amount working public employees contribute into IPERS toward their own retirement. Gronstal says legislators may consider another increase in pension contributions for those who are at least 15 years away from retirement. Earlier, Governor Culver said there was "no need for alarm" or for immediate action to address the shortfall in the IPERS fund.

Virginia



Both candidates for Virginia governor—Democrat Creigh Deeds and Republican Bob McDonnell—said that they would not reduce the state's current level of contribution to the retirement benefits of state employees. Gov. Tim Kaine recently said the state would defer its quarterly employer contribution to workers' pensions in the Virginia Retirement System for the last quarter of fiscal year 2010 in an effort to close an anticipated \$1.35 billion revenue shortfall in the state's spending plan. But Kaine and administration officials also indicated they were considering a change that could require the state's 100,000 employees to contribute a portion of their salaries toward their pensions. Such a shift could be incorporated into the budget for the 2011-2012 fiscal years, which Kaine will submit in December before his term expires.

A year ago at this time, the economic situation looked bleak at best. The Dow had fallen from a high of 14,093 in October of 2007 to 8,451 in just a year. Lehman Brothers disappeared almost overnight, and Bank of America took over Merrill Lynch. And what was dubbed as “the greatest financial crisis since the Great Depression” was only getting worse.

The markets bottomed out in March of this year, and as a result, public funds found themselves in a defensive position with the media, legislators and the general public. But—and I don’t want to sound too optimistic—it seems we’ve turned a corner, and the future, while not exactly bright, does seem to offer a glimmer of hope. The market trend seems to be generally positive with much less volatility than what we saw from October 2007 to March of 2009, and public funds are again seeing positive returns, which are finally offsetting some of the recent losses.

That said, I think we still must remain vigilant. Public funds are still in the crosshairs, and many state and local

legislators are using the opportunity to again make their attacks on defined benefit pension systems. We must continue to educate the public, the media, and our state and local legislators, letting them know that the public pension community is a driving economic engine that brought some stability to the markets at a time when others could not. We need to continue letting them know that our funding models take into account both losses and gains, and while our funds were hit hard—as were all who invested in the markets—we are resilient and are already working to recoup the losses. Lastly, we need to continue hammering home the point that retirees’ benefits are safe, and America’s public pension systems have the money to continue paying benefits well into the future.

Again, we aren’t out of trouble yet, and I think we will still have to confront many challenges. But, the clouds seem to be parting and the sun is beginning to shine through. And with stimulus money finally coursing through the economy, coupled with the American spirit of optimism and hard work, this may just be the formula for a real recovery.

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Website: www.NCPERS.org • E-mail: legislative@NCPERS.org



The Voice for Public Pensions

444 North Capitol Street, NW, Suite 630 • Washington, DC 20001 • 1-877-202-5706 • (202) 624-1439 (fax)