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MENDOCINO COUNTY
EMPLOYEES' RETIREMENT ASSOCIATION
625-B KINGS COURT
UKIAH, CALIFORNIA 95482-5027

Date: May 8, 2013
To: Board of Retirement
From: Richard White, Retirement Administrator
Subject: Administrator Report

Meetings attended since the last Board of Retirement meeting:

- I attended the SACRS Symposium on April 23, 2013 in San Francisco. The symposium covered the issues confronted by a public pension fund in the event a plan sponsor enters bankruptcy or refuses to pay contributions into the system.
- I attended the County of Mendocino Department Head meeting on May 1, 2013.

Board Agenda:

At a recent Board of Retirement meeting, a member asked about adding a consent calendar to the regular Board agenda. Due to time constraints, the Board was not able to have a full discussion regarding the merits in the use of a consent agenda.

Future meeting attendance:

- I will be attending the SACRS Spring 2013 conference in Napa during the week of May 13th.
- I will be attending the Government Finance Officers Association 107th Annual Conference in San Francisco on June 2-5, 2013.

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1. Article entitled <u>False Sense of Security</u> from Plan Sponsor Magazine is included for your reading.

False Sense of Security

A DB pension may not cover all retirement living expenses

Employees who are offered the increasingly rare defined benefit (DB) pension plan—there were as few as 47,000 of the plans in 2012, according to the Department of Labor (DOL)—may think they will simply put in their years at work and, once they reach the required age, count on their companies to provide retirement income. But industry experts caution that pensions should only be thought of as one part of the retirement readiness package, and simply having a pension does not mean one should neglect to plan for retirement expenses or lifestyle. In fact, without planning ahead for health care and emergencies, among other expenses, experts say, those with DB pension plans may actually fare worse in retirement than those with defined contribution (DC) plans.

Baby Boomers—defined by the Census Bureau as those born between 1946 and 1964—are particularly in danger of having insufficient savings to live off comfortably in retirement. In fact, Fidelity Investments recommends that individuals aim to replace 85% of their preretirement income. This generation, historically deemed the "consumption" generation, is the first to see both pensions and 401(k) plans in the workplace. According to a recent Fidelity survey, one in five retirees with pensions acknowledged that they did no planning before retirement, with half (51%) indicating that they only began planning one to five years before retirement.

Having a pension plan could potentially "lull" employees into not supplementing their savings, because they wrongly assume that their company's retirement plan, coupled with Social Security, will cover their living expenses in retirement, says Wendy Foster, senior vice president of product management at Fidelity in Smithfield, Rhode Island. However, retirees with defined benefit and defined contribution plans alike may be unprepared for retirement. Even when retired Boomers have access to pension payments, Fidelity found that seven out of 10 of them wish they had done more to save for retirement during their working years.

According to Fidelity's survey, nearly half (48%) of Baby Boomers—regardless of whether they expect to retire with a pension—anticipate retiring with debt from some of life's typical demands. The debts reported, from largest to smallest, were mortgages, credit card balances, car payments and student loans, for themselves, a spouse or their children.

A greater number of working Boomers with DB pensions (56%) indicated they are more likely to retire at or before the traditional age of 65 than are those without pensions (39%), yet almost half of them still expect to retire with debt.

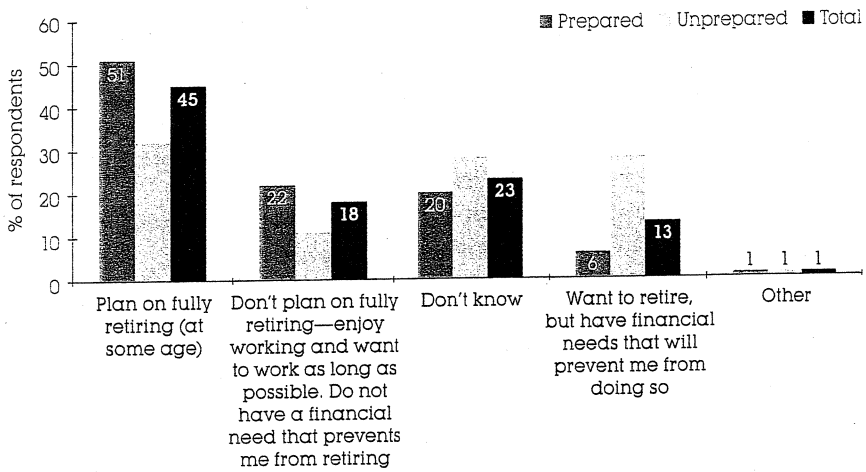
Though DC plans may be no better vehicles than DBs to prepare employees for retirement, DC plans can make employees more active in their financial futures, says Bill Keen, managing director of investments at The Keen Wealth Management Group of Wells Fargo

Percentage of households at risk of not maintaining current standards of living at retirement

AGE GROUP	2007	2010
All	44%	53%
30 to 39 years old	53%	62%
40 to 49 years old	47%	55%
50 to 59 years old	32%	44%

Source: Center for Retirement Research at Boston College National Retirement Risk Index; Analysis: Manning & Napier.

Retirement Timing



Source: TD Ameritrade.

Advisors in Kansas City, Missouri. While he says generalizations about DC versus DB success cannot be made, he cautions that those with defined benefit plans may rely too heavily on their company to take care of them—they may lack perspective on the long-term wealth-building approach that comes from taking on their own retirement preparation—for example, by contributing to a DC plan.

Defined contribution plans, in comparison with pension plans, make employees "active" in their retirement planning because the responsibility to save falls on the individuals rather than the company, says Robin Pellish, CEO at Rocaton Investment Advisors LLC in Norwalk, Connecticut.

That said, research indicates that defined contribution participants are just as "uninvolved" in their savings as defined benefit participants. According to data from Charles Schwab in "Bridging the Gap Between 401(k) Sponsors and Participants," more than half (52%) of participants do not have the time, interest or knowledge to manage their 401(k) plans, suggesting that the problem may not be the type of plan but, rather, the participants' level of engagement in the plan.

In addition, research has found that defined benefit plans—at least in the eyes of plan sponsors—increase the likelihood that participants will meet their retirement goals. The 2012 PLANSPONSOR Defined Contribution survey found that 28% of sponsors with DB plans (traditional or cash balance) either agree or somewhat agree that employees will reach their retirement goals, compared with 19% of sponsors who said the same about DC plans.

Robert Stammers, director of investor education at CFA Institute in New York City, says the retirement success of individuals—whether they have defined benefit or defined contribution plans—depends on many factors, so he agrees with Keen that generalizations about future success cannot be made. However, planning for retirement is equally as important with a DB plan as with a DC plan, and pensioners may overlook this. "There is a sense of, 'No matter what happens, at least I'm going to have some money,'" he says, cautioning that employees may fail to plan for inflation or for changes in the pension's funded status. "Pension plans aren't necessarily made to fund 100% of a person's retirement."

Educating Pension Participants

To help employees maintain their standard of living in retirement, financial education must start early in life and include lessons about compound interest, volatility, market history and future costs, Keen says. "You don't need to have a Ph.D. in economics to [understand] these things," he stresses. "If you're educated and engaged, you can actually make a change." He says employees must also realize early that health care, long-term care, home ownership and emergencies are all part of retirement readiness. Without some reserve for the unexpected, retirement funds can deplete quickly.

Many seniors spend the bulk of their assets in the last three to five years of life because of health care and nursing home costs, says Paul Saganey, president of Integrated Financial Partners Inc. (IFP) in Boston. The housing crisis has also made it very challenging to profit from home sales, so he cautions people against assuming they will make money from downgrading to a smaller house when they retire.

Health care remains a costly burden for retirees. According to the December 2012 research paper "Potential Macroeconomic Consequences of an Aging Population With Insufficient Savings" from Manning & Napier, as of 2009, Medicare covered only 59% of health care costs for beneficiaries ages 65 and older. Out-of-pocket covered 13%, private insurance covered 14%, and a mix of Medicaid, Tricare and other sources made up the remaining 14%.

Preparing for future costs is especially crucial now, with the longevity crisis—according to the U.S. Census, life expectancy by 2020 is predicted to be 79.5, up from 70.8 in 1970. A married couple aged 65 has a 50% chance of at least one of them living to age 89, according to the National Vital Statistics Reports, Vol. 58, No. 21, United States Life Tables 2006. "Longevity is posing a challenge, and health care costs have been outpacing inflation," says Mary Moglia-Cannon, senior analyst and portfolio strategist at Manning & Napier in Rochester, New York.

Longevity is the biggest challenge employees face—fairly healthy people have a good chance of living into their 90s, Saganey says. "I think it's a fallacy that you'll need less money when you're older."

Coupled with longevity risk is inflation. Saganey notes that many pension plans neglect to adjust for cost-of-living increases. If retirees are not careful, inflation can "far eclipse" their savings, he warns.

Before retiring, employees must determine whether they are actually ready for retirement or just eligible for their pension benefit.

Those with debt should consider delaying retirement until the debt is paid, Keen says, whether that means continuing work at a current job or picking up part-time employment. Fidelity's research revealed that 15% of employees with 401(k)s plan to work in retirement, compared with 7% of employees with pension plans.

Employees approaching retirement should also consider the type of debt they have. Those with high-interest credit card debt, for example, should think about different savings strategies, such as delaying retirement to help pay the debt off, Moglia-Cannon says.

Whether employees have a defined benefit plan, a defined contribution plan or both, plan sponsors and advisers should help them understand the unexpected costs in retirement. "At the end of the day, we really think it's important to have people aware of the fact that they cannot be complacent about their retirement savings," Moglia-Cannon says.

—Corie Russell

DEPLETION ALLOWANCE

Largest cities face $217B retirement system shortfall

SIXTY-ONE cities across America have emerged from the recession with a pension and retiree health care funding shortfall totaling more than $217 billion, according to a report from The Pew Charitable Trusts.

The new report, "A widening gap in Cities," covers the most populous city in each state plus all others with populations of more than 500,000. For pensions, these cities combined a shortfall of $99 billion in fiscal year 2009, the most recent year with complete data. The rest of the shortfall—$118 billion—was for retiree health care and other benefits.

While investment losses during the recession depleted cities' pension funds nearly across the board, the Pew report found that another factor made the difference between the best- and worst-funded pension systems. "Having studied 61 cities and the 50 states, the better-funded plans all share one characteristic: They have the discipline to pay their annual pension bills," says David Draine, senior researcher at the Pew Center on the States in Washington, D.C.

Nearly six out of 10 cities made at least 90% of their annual payments in all three years studied. Among those jurisdictions, pension funds weathered the recession better than in cities with poor funding habits, and their funding levels dropped only half as much.

The National Public Pension Coalition (NPPC) issued a statement that agrees with conclusions regarding the factors contributing to the underfunding but criticizes Pew's suggested remedies: "While Pew acknowledges the factors behind the underfunded pension systems, to suggest modifications that punish public employees is irresponsible and uncalled for."

The retirement systems' funding statuses ranged from 113% in Milwaukee to 24% in Charleston, West Virginia. For pensions, the 16 best-performing cities, as noted in the Pew study, are: Albuquerque, New Mexico; Baltimore; Charlotte, North Carolina; Dallas; Denver; Des Moines, Iowa; Los Angeles; Milwaukee; Salt Lake City; San Antonio; San Francisco; Seattle; Sioux Falls, South Dakota; Virginia Beach, Virginia; Washington, D.C.; and Wichita, Kansas.

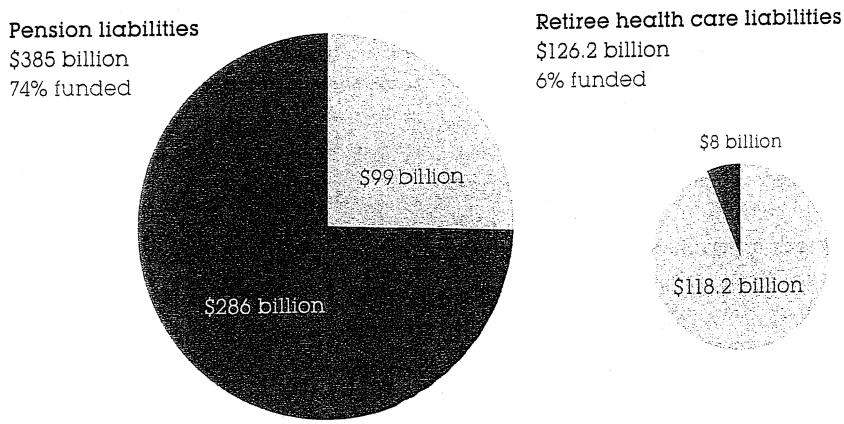
The nine worst-performing cities, according to the study, are: Charleston, West Virginia; Chicago; Fargo, North Dakota; Jackson, Mississippi; Little Rock, Arkansas; New Orleans; Omaha, Nebraska; Philadelphia; and Portland, Oregon.

Many cities have commitments to health care, life insurance and other nonpension benefits for their retirees and preretirees. Unfortunately, as of 2009, only Los Angeles and Denver had even half of the necessary funds to meet those commitments, and 33 cities had not set aside any funds at all for these future retiree benefit expenses. —*Rebecca Moore*

61 Cities' Retiree Bills

FISCAL YEAR 2009 ■ *Funded* ▒ *Unfunded*

The unfunded share of retirement benefits promised to city employees totaled $217.2 billion.



Note: Retiree health care is the primary component of other postemployment benefits, which also include other nonpension benefits such as life insurance.

Source: The Pew Charitable Trusts analysis 2012.

> "While Pew acknowledges the factors behind the underfunded pension systems, to suggest modifications that punish public employees is irresponsible and uncalled for."