Presentation Overview

- The size and scope of public pensions in the US and Connecticut
- Public pension funding conditions
- Perspective on retirement plan design
- Trends and changes in public pension plan design
- Risk-sharing in public pension plan design
Public pensions in the U.S.

- ~$4 trillion in assets
- 14.5 million active (working) participants—employees of states and local government
  - Nearly 10 percent of the nation’s workforce
- 10.7 million public pension retirees and their survivors receive ~$300 billion annually in benefits
- Annual contributions = $200 billion
  - $145 billion from employers; $55 billion from employees
  - Approximately 5.0 percent of all state and local government spending goes to public pensions
- Of 6,000+ public retirement systems, the largest 75 account for 80+ percent of assets and members
Public pensions in Connecticut

• ~$44 billion in assets
• 127,000 active (working) participants—employees of states and local government
• 122,000 public pension retirees and their survivors receive ~$5 billion annually in benefits
• Annual contributions = $4.0 billion
  ▲ $3.4 billion from employers; $600 million from employees
  ▲ Approximately 6.8 percent of all state and local government spending goes to public pensions (FY 15)
• Of 212 public retirement systems, TRB and SERS account for 70+ percent of assets and members
• Slightly fewer than one-half of public employees in CT do not participate in Social Security
Comparison of Retirement Benefits in the U.S.

**Private Sector**

- 60% of full-time private sector workers participate in an employer-sponsored retirement plan; 21% of part-time workers participate
- In total, 49% of all private sector workers participate in an employer-sponsored retirement plan
- Fewer than one in five have a traditional pension (DB) plan
- Social Security coverage is universal

**Public Sector**

- Nearly all full-time workers have access to an employer-sponsored retirement benefit; most have access to a traditional pension (DB plan)
- 87% of full-time employees participate in a pension plan
- 80% of all employees, including part-time workers
- Virtually all others are in a DC plan
- Three-fourths participate in Social Security

US Bureau of Labor Statistics
Change in Aggregate Public Pension Funding Level, FY 01 to FY 17
Median Change From Prior Year in Actuarial Value of Assets and Liabilities

Public Fund Survey Nov-18

Fiscal Year
Distribution of Public Pension Funding Levels, FY 17

Median = 72.9%

Size of bubbles is roughly proportionate to size of plan liabilities

CT TRB
CT SERS
Headwinds Facing Public Pension Plans

- Declining investment return assumptions
- Slow payroll growth as a result of
  - Sluggish hiring rates
  - Tepid salary growth
- Higher required pension plan costs
- Updated mortality assumptions to reflect longer life expectations
- Negative cash flow
Tailwinds Supporting Public Pension Plans

- Stronger employer efforts to pay contributions
- More aggressive liability amortization strategies:
  - More closed periods
  - Shorter periods
- Lower benefit levels = lower long-term costs
- Improving economy
- Slow improvement in hiring and salary growth
The typical public pension funding model is highly reliant on investment earnings.
Investment Return Assumptions, FY 01 to latest

CT TRB: 8.0%
CT SERS: 6.9%

Public Fund Survey, NASRA Jan-19
Relative Change in Employment in Private and Public Sectors, 2007 to present

Data final as of December 2018

U.S. Bureau of Labor Statistics
Change in Actives and Annuitants FY 01 to FY 17

Public Fund Survey Nov-2018
Annualized Quarterly Change in Wage and Salary Costs for Private and State & Local Government Employees, 01-18

Data final as of Q2 2018

U.S. Bureau of Labor Statistics
Median Annual Change in Public Pension Payrolls, FY 02 to FY 17

Public Fund Survey
Jul-18
NASRA’s Position on Pension Plan Design

- Core elements of public pension plan design:
  - Mandatory participation
  - Employee-employer cost sharing
  - Assets that are pooled and professionally managed
  - Targeted income replacement
  - Annuitized benefits
  - Survivor and disability benefits
  - Access to a supplemental retirement savings plan
Perspective on Retirement Plan Design

- The purpose for providing a retirement plan is to meet stakeholder objectives
- Primary retirement plan stakeholders are public employers (school districts, police departments, state agencies, etc.), public employees, and taxpayers
- Stakeholder objectives:
  - Employers seek to attract and retain qualified workers needed to perform essential public services
  - Employees seek a competitive compensation package that includes a retirement benefit
  - Taxpayers seek public services delivered in a cost-effective manner
Perspective on Retirement Plan Design

Q. Why not switch to a defined contribution plan as the primary retirement benefit?

A. A DC plan provides cost certainty and shields taxpayers from certain risks, but introduces new and different types of risk. Sound retirement plan design balances risks and rewards.

Q. What type of risks would a typical DC plan introduce?

▲ Among others:

▲ A DC plan can impair the ability of employers to retain workers, especially those who are older and experienced.

▲ A DC plan can impede the ability of workers to retire in a timely and orderly manner.

▲ A DC plan will result in some employees having no source of assured retirement income, which could mean they will rely on public assistance in their old age.
Perspective on Retirement Plan Design

• Multiple studies have concluded that a traditional pension benefit will deliver the same level of retirement income at a lower cost relative to alternative plan types.

• Generally, this is due to three factors:
  ▲ Pooled assets avoid “over-saving” by saving for the group rather than on an individual basis
  ▲ Lower investment and administrative costs
  ▲ Higher investment returns enabled by assets that are professionally managed and by maintaining a longer investment horizon

• See also
  ▲ “Pension Benefit Design Study, TRS of Texas,” 2018
  ▲ “Study of Colorado PERA Hybrid DB Plan,” 2015
  ▲ Plan Design@NASRA.org
Reforms to pension plans since the 2008-09 market decline and the Great Recession are unprecedented in scope and magnitude

Nearly every state has made changes to pension benefit levels, financing arrangements, or both

Many states have enacted changes more than once

Nearly all states have retained access to a traditional pension plan as employees’ primary retirement benefit
Trends in Plan Design

- Changes to plan design typically are intended to accomplish one or more of the following objectives:
  - Lower employer costs
  - Reduce liabilities
  - Reduce employer risk

- The types of change, the degree of change, and who is affected vary widely among states and plans

- The effect on costs of changes in a pension plan design is heavily reliant on the groups that are affected by the changes
Trends in Plan Design

- Reforms may affect new hires only, current active members, those already retired, or all three.
- Changes that affect new hires only tend to have limited effects on costs and liabilities.
- Changes that affect those already retired can have a significant effect on plan costs and liabilities.
- Public pension legal protections are a primary factor when considering changes to a pension plan.
- Legal protections run a wide range and are not always clearly known.
States Enacting Pension Reforms 2007 to 2018

Significant Reforms to State Retirement Systems, NASRA
Median Employee and Employer Contribution Rates, FY 02 to FY 17

See also NASRA issue briefs on employee and employer contributions
States That Have Made Changes to Cost-of-Living Adjustment Provisions 2009-2018

Significant Reforms to State Retirement Systems, NASRA
Ways Pension Benefit Levels Have Been Reduced

- Lower retirement multiplier
- Longer period for calculating pensionable salary
- Higher required age to qualify for a full retirement benefit
- More required years of service to qualify for a full retirement benefit
- Lower rate of interest accrual on contribution account balances
States That Reduced Pension Benefits, 2009-2018
States That Implemented Automatic Risk-Sharing Features  
2009-2018
States That Created New Hybrid Plans, 2009-2018
Statewide Hybrid Plans and Relative Participation Rates

See also NASRA issue brief on state hybrid retirement plans
Risk-Sharing Conceptually

\[ C + I = B + E \]

- Contributions plus Investment Earnings equals Benefits plus Expenses
- Over time, the revenue into a retirement plan must equal the plan’s expenses
- In a traditional defined benefit plan, when revenues are insufficient to pay for benefits, employer contribution rates rise
- Risk-sharing introduces the possibility that employee contributions or benefit levels will be adjusted
Conceptual Illustration of Typical Risk Distribution, by Plan Type

- DB Plan, EE and ER Contributions Only
- More Employer Risk
- DB Plan, EE and ER Contributions
- Shared Risk
- Cash balance plan, hybrid DB-DC plan, plans in which benefits or employee costs vary on the basis of such factors as investment performance and the financial or actuarial condition of the plan
- More Employee Risk
- DC Plan, EE and ER Contributions
- More Employee Contributions Only

NASRA
Examples of Risk-Sharing Features

- **Hybrid plans**
  - DB-DC: a traditional pension plan combined with a defined contribution plan
  - Cash balance: a retirement benefit like a pension plan except the benefit is affected by investment experience and the employee’s retirement age

- **Variable employee contribution rates**, which can change based on the plan’s actuarial condition

- **Contingent benefits**, in which the size of the basic retirement benefit may be affected by the plan’s actuarial condition

- **Contingent COLAs**, the post-retirement benefit adjustment depends on some external factor, such as investment return or the plan’s funding level
Final Thoughts

• Public pension funding conditions range from strong and healthy to distressed

• In terms of scope and magnitude, an unprecedented number of changes to public pension plans have been enacted in the last decade

• Sound retirement plan design reflects the objectives of all stakeholder groups:
  ▲ Taxpayers, public employers, and public employees

• Most states have retained core features of sound retirement plan design while shifting some risk to employees
Thank you for listening!

With questions or to discuss public pension issues:

keith@nasra.org  alex@nasra.org

202-624-8464  202-624-8461

www.nasra.org