



# **An Overview of Public Pension Issues**

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# Keith Brainard Bio




- Research director for NASRA since 2002
- Previous service: Arizona State Retirement System, Arizona and Texas Legislatures
- Appointed member, Texas Pension Review Board
- Elected member, Georgetown, Texas city council
- M.P.A and B.A., The University of Texas at Austin
- Regular speaker on public pension issues before congressional and legislative committees and pension boards

# Keith Brainard Publications

Author or co-author of the following:

- ▲ “Governmental Plans Answer Book, Third Edition”
- ▲ NASRA Issue Brief: Employee Contributions to Public Pension Plans, February 2015 (Committee Notebook, Funding 173-182).
- ▲ Pension Funding: A Guide for Elected Officials, Report from the Pension Funding Task Force, 2013 (Committee Notebook, Funding 183-190)
- ▲ Effects of Pension Plan Changes on Retirement Security, April 2014 (Committee Notebook, Pension Reform 9-28)
- ▲ NASRA Issue Brief: State Hybrid Retirement Plans, September 2013 (Committee Notebook, Pension Reform 41-44)
- ▲ NASRA Issue Brief: Cost-of-Living Adjustments, July 2015 (Committee Notebook, Pension Reform 45-58)
- ▲ Selected Approved Changes to State Public Pensions to Restore or Preserve Plan Sustainability, December 2014 (Committee Notebook, Pension Reform 89-111).
- ▲ The “Annual Required Contribution Experience of Statewide Retirement Plans, 2001 to 2013”

# Presentation Overview

-  An overview of public pensions
-  Use of alternative retirement plan designs
-  The choice facing Alabama policymakers

# A 50,000-foot view of public pensions in the U.S.

- ▲ ~\$3.7 trillion in assets
- ▲ ~14 million active (working) participants
  - ▲ 13 percent of the nation's workforce
- ▲ 9 million retirees and their survivors receive ~\$240 billion annually in benefits
- ▲ Of 4,000 public retirement systems, the largest 75 account for 80+ percent of assets and members
- ▲ Aggregate funding level = ~75%

# Public pensions in Alabama

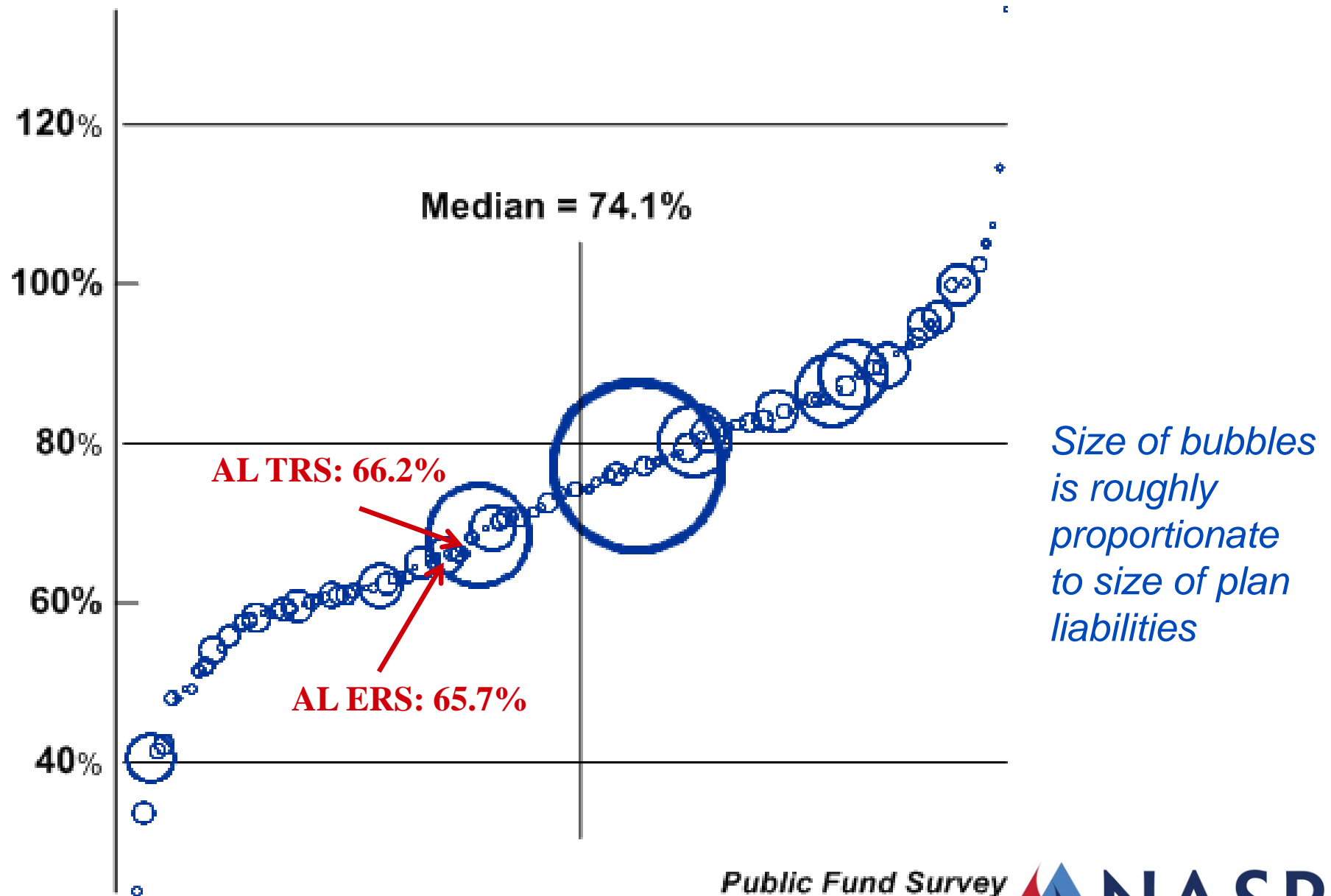
As of 2014:

- ▲ \$36 billion in assets
- ▲ 260,000 active (working) participants
  - ▲ ~12 percent of the state's workforce
- ▲ Systems received \$2.0 billion in contributions:
  - ▲ \$1.2 billion from public employers
  - ▲ \$800 million from public employees
- ▲ 134,000 retirees and their survivors receive \$3.1 billion annually in benefits

# Key public pension trends


- ▲ From 2009 to 2014, there was an unprecedented
  - ▲ number of reductions in public pension benefit levels
  - ▲ number of increases to employee contribution rates
  - ▲ number of legal challenges—and rulings—in response to pension changes
  - ▲ reduction in state and local government employment
- ▲ New pension accounting standards are changing the way pension liabilities are calculated and reported
- ▲ Investment return assumptions are under scrutiny and challenge, and are being reduced
- ▲ Funding levels are improving in most places
- ▲ Some states have yet to resolve their pension problems

# Latest Public Pension Funding Levels





# Retirement Plan Design and Policy

 The retirement plan *type* is less important than the retirement plan *design*







 Plan types:

- ▲ defined benefit
- ▲ defined contribution
- ▲ hybrid

 Plan design:

- ▲ participation requirement
- ▲ vesting period
- ▲ benefit level
- ▲ cost
- ▲ timing of benefits eligibility
- ▲ assignment of risks, esp. inflation, investment and longevity
- ▲ assignment of costs

# Distinguishing elements of public pension plan designs

-  Mandatory participation
-  Employee-employer cost sharing
-  Targeted income replacement
-  Assets that are pooled and professionally invested
-  Death & disability protection
-  A benefit that cannot be outlived



## Overview of Primary Retirement Benefit Plan Type, by State

*The information listed below reflects the prevailing plan type provided to all or most members of broad employee groups in each state: state employees, public school teachers, public safety personnel, and other employees of local government. Plan designs vary; many DB plans contain hybrid features.*

|                             |  |
|-----------------------------|--|
| <b>Alaska</b>               | DC for all new hires since 7/1/06; DB for those hired previously   |
| <b>Alabama</b>              | DB   |
| <b>Arkansas</b>             | DB   |
| <b>Arizona</b>              | DB   |
| <b>California</b>           | DB except CB for employees of community colleges that have elected to participate and some part-time school employees  |
| <b>Colorado</b>             | DB for state employees, teachers, and local government employees; CB for most local public safety personnel  |
| <b>Connecticut</b>          | DB   |
| <b>District of Columbia</b> | DB for teachers and public safety personnel; DC for general employees  |
| <b>Delaware</b>             | DB   |
| <b>Florida</b>              | Optional DB or DC; approximately 85 percent elect the DB   |
| <b>Georgia</b>              | DB for teachers and most local government workers; DB-DC hybrid for state workers hired since 2008   |
| <b>Hawaii</b>               | DB   |
| <b>Iowa</b>                 | DB   |
| <b>Idaho</b>                | DB   |
| <b>Illinois</b>             | DB   |
| <b>Indiana</b>              | DB-DC hybrid   |
| <b>Kansas</b>               | DB except CB for new hires since 1/1/15  |
| <b>Kentucky</b>             | DB for teachers; DB-DC hybrid or CB for those hired since 2008   |
| <b>Louisiana</b>            | DB   |
| <b>Massachusetts</b>        | DB   |
| <b>Maryland</b>             | DB   |
| <b>Maine</b>                | DB   |
| <b>Michigan</b>             | DC for state workers hired since 1997; DB-DC hybrid for teachers hired since 2010 and for those hired previously who have elected to participate; DB or DB-DC hybrid for most local government workers |
| <b>Minnesota</b>            | DB   |
| <b>Missouri</b>             | DB   |

|                       |  |
|-----------------------|--|
| <b>Mississippi</b>    | DB   |
| <b>Montana</b>        | DB except optional DC for state and local government workers hired since 2002, who may choose between DB and DC. Approximately three percent of participants are in the DC plan.   |
| <b>North Carolina</b> | DB   |
| <b>North Dakota</b>   | DB   |
| <b>Nebraska</b>       | DB for teachers and public safety personnel; CB for state and county workers   |
| <b>New Hampshire</b>  | DB   |
| <b>New Jersey</b>     | DB   |
| <b>New Mexico</b>     | DB   |
| <b>Nevada</b>         | DB   |
| <b>New York</b>       | DB   |
| <b>Ohio</b>           | Most teachers, state employees, and employees of local government hired since 2001 or 2002, depending on the plan, may choose between DB, DC, or a DB-DC hybrid. Approximately 95 percent of those offered a choice have elected the DB plan. Public safety personnel have a DB. |
| <b>Oklahoma</b>       | DB except new state hires as of 11/1/15 will have only a DC.   |
| <b>Oregon</b>         | DB-DC hybrid   |
| <b>Pennsylvania</b>   | DB   |
| <b>Rhode Island</b>   | DB-DC hybrid   |
| <b>South Carolina</b> | DB; state and school workers may choose between a DB and DC plan; roughly 80 percent of those offered a choice have elected the DB plan  |
| <b>South Dakota</b>   | DB   |
| <b>Tennessee</b>      | DB; DB-DC hybrid for teachers and state employees hired since 7/1/14; local governments may elect to participate in the hybrid plan  |
| <b>Texas</b>          | DB for teachers, state employees, and most employees of the largest cities; CB for employees of counties, most smaller cities and special districts  |
| <b>Utah</b>           | DB; those hired since 7/1/11 may choose between a DB-DC hybrid and a DC plan, each of which feature a maximum employer contribution rate of 10 percent of pay.   |
| <b>Virginia</b>       | DB for those hired before 2014; those hired since 1/1/14 participate in a DB-DC hybrid   |
| <b>Vermont</b>        | DB   |
| <b>Washington</b>     | Most participants may choose a DB or a DB-DC hybrid; roughly two-thirds have elected the DB plan   |
| <b>Wisconsin</b>      | DB   |
| <b>West Virginia</b>  | DB; teachers hired between 1991 and 2005 were enrolled only in a DC plan, and most of them have elected since to switch to a DB plan   |
| <b>Wyoming</b>        | DB   |

**Legend: DB = defined benefit DC = defined contribution CB = cash balance**

***See also***

- Selected Approved Changes to State Public Pensions to Restore or Preserve Plan Sustainability, NASRA
- Decisions, Decisions: Retirement Plan Choices for Public Employees and Employers, NIRS
- Issue Brief: State Hybrid Retirement Plans, NASRA
- Plan Design @NASRA.org

# Is there a “public pension crisis” ?

- ▲ The experience and condition of public pensions are unique to each state and plan
- ▲ Broad generalizations about the entire public pension community gloss over important details specific to individual plans:
  - ▲ Actuarial funding condition
  - ▲ Actuarial methods and assumptions
  - ▲ Demographics of each pension plan and plan sponsor (state, cities, etc.)
  - ▲ Plan sponsor(s) fiscal and economic conditions
  - ▲ Pension legal protections
  - ▲ Benefit levels
- ▲ Some states and cities face formidable pension funding challenges; most do not

# Is there a “public pension crisis” ?

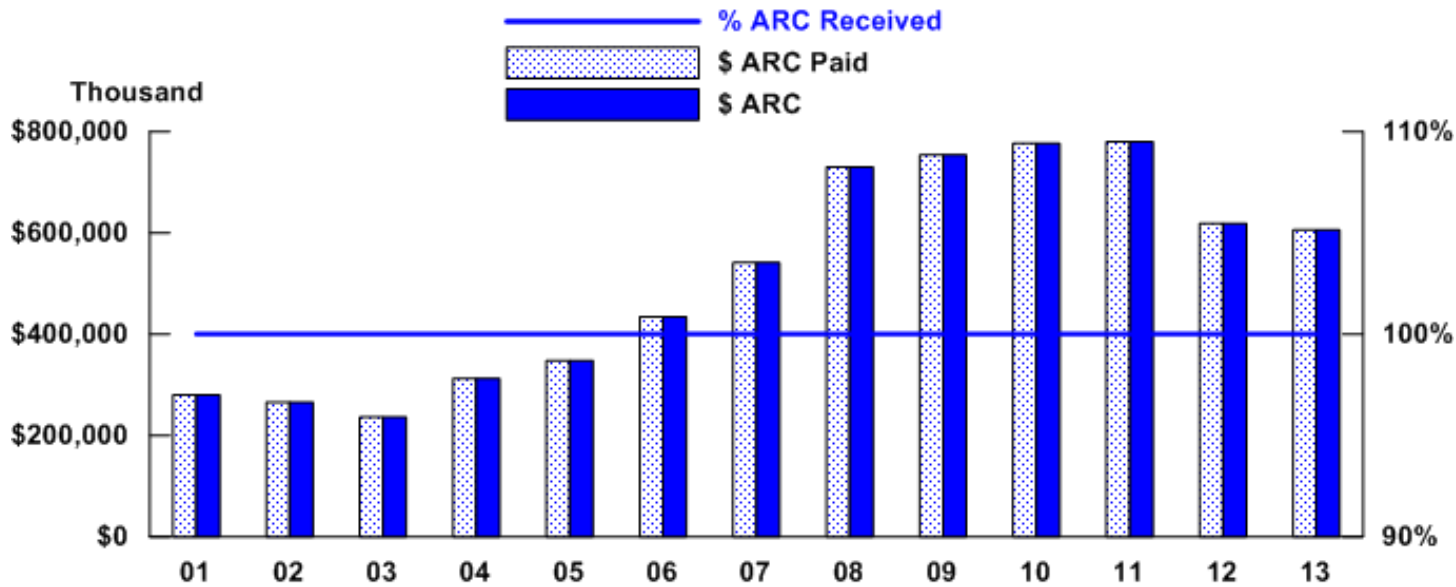
## Webster’s definition of “crisis:”

- ▲ *An unstable or crucial time or state of affairs in which a decisive change is impending; especially: one with the distinct possibility of a highly undesirable outcome <e.g., a financial crisis>*

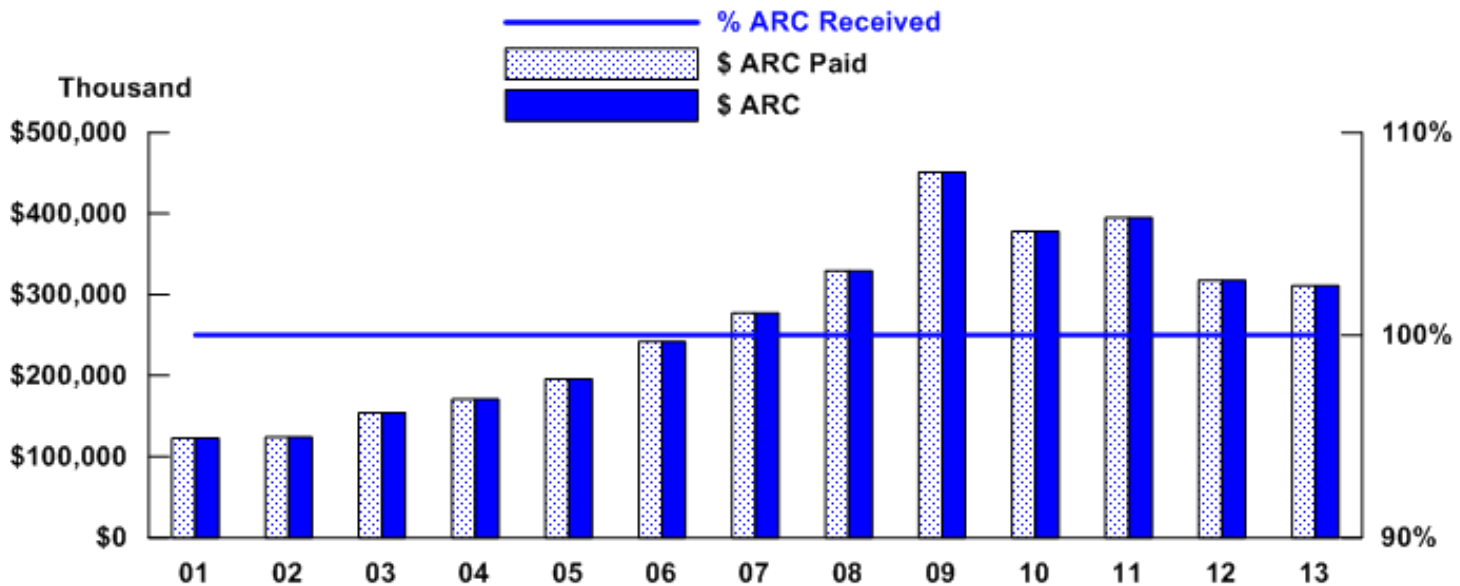
# Does Alabama face a pension crisis ?

- ▲ Are Alabama pensions “unstable”?
  - ▲ Pensions in Alabama appear to be stable: costs are well-known, fairly predictable, and, measured as a percentage of all state and local government spending, are relatively low.
- ▲ Is “decisive change impending with the distinct possibility of a highly undesirable outcome <a financial crisis>”?
  - ▲ By enacting substantial reforms in 2012, Alabama appears already to have made a “decisive change.”
  - ▲ Barring an unforeseen national economic collapse, current conditions in Alabama do not appear poised to result in a materially negative outcome.

# AL TRS



# AL ERS

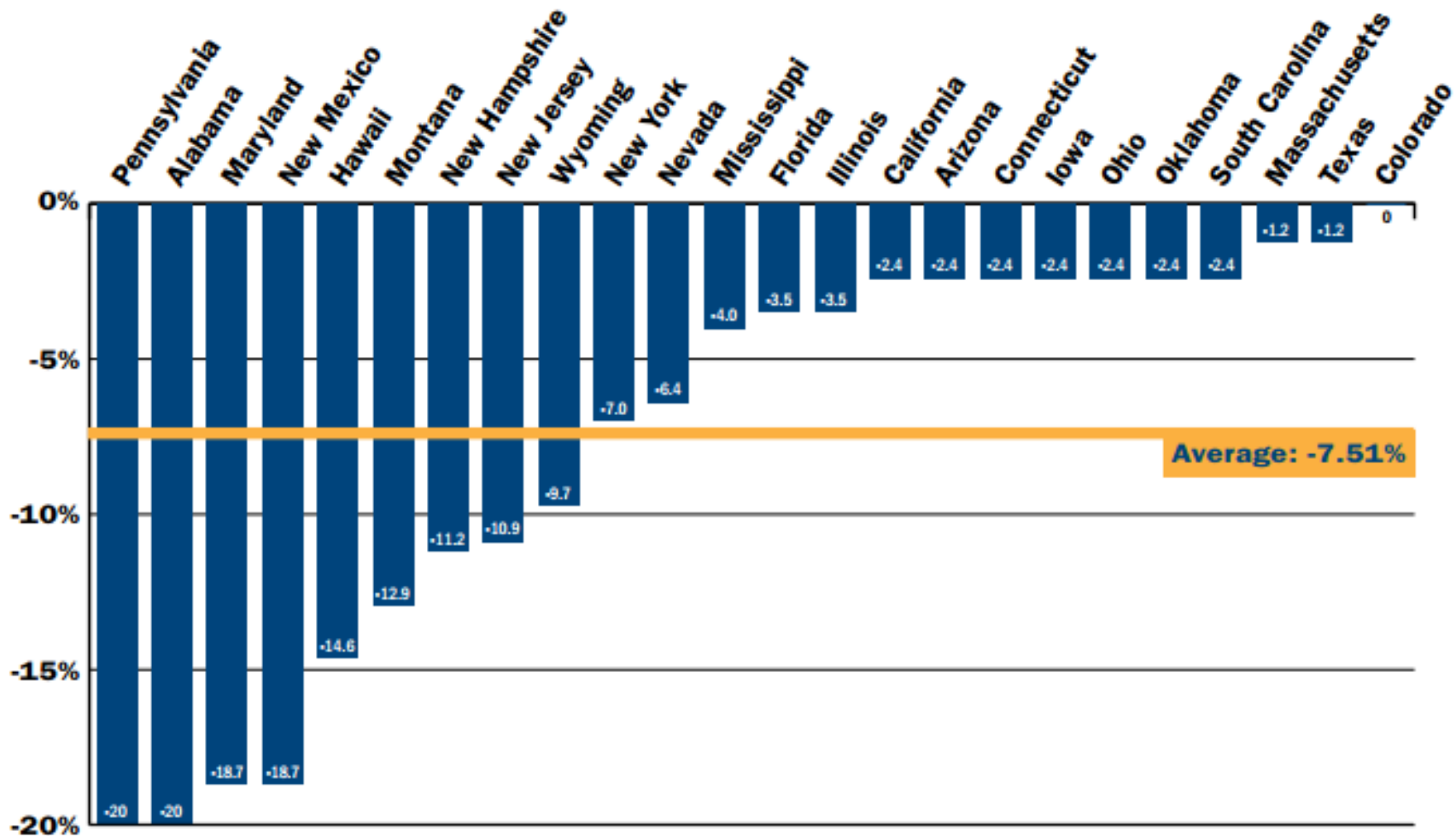


**Alabama has a commendable record of paying required pension contributions**



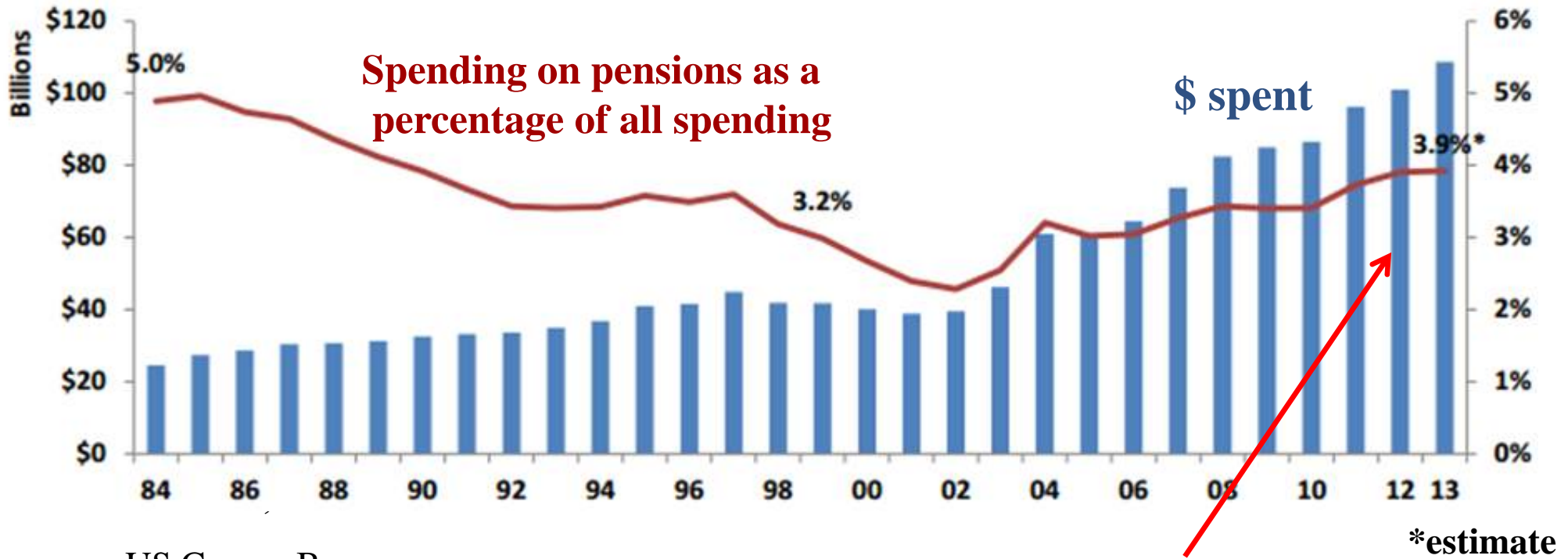


# Percentage change in pension benefit based on recently enacted reforms affecting general state employees



Source: NASRA, SLGE, *Effects of Pension Plan Changes on Retirement Security*, April 2014

# Employer (taxpayer) spending on public pensions, U.S., 1984 to 2013



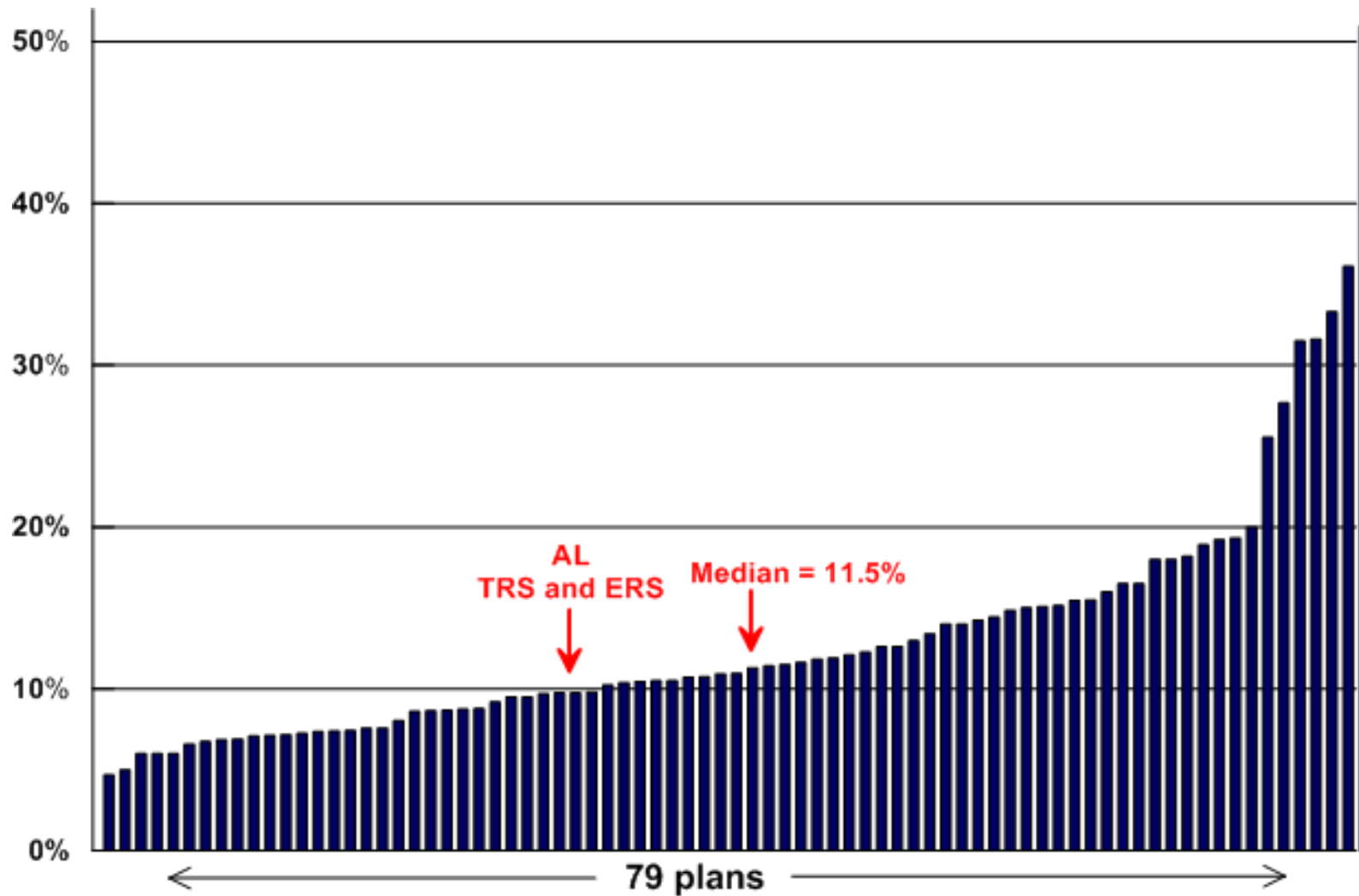
US Census Bureau

**Alabama FY 12 = 2.87 percent**

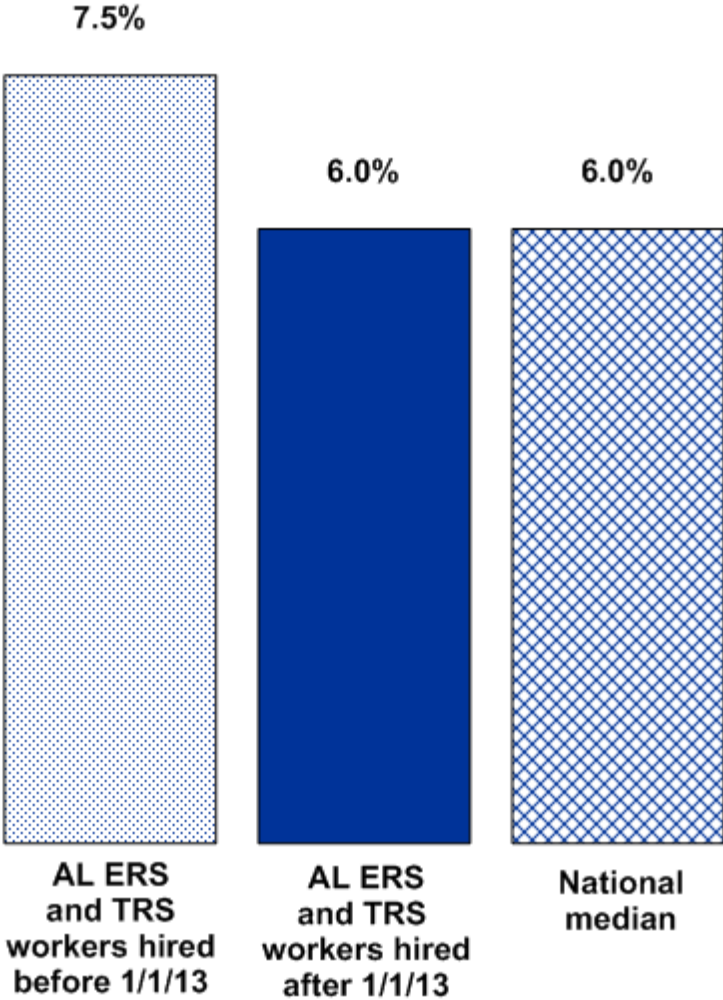
# Legislative pension enactments in recent years

- ▲ Nearly every state, including Alabama, has modified public pension benefits, raised employee contributions, or both, since 2009
- ▲ Lower benefits:
  - ▲ higher retirement age
  - ▲ more required years of service
  - ▲ longer vesting period
  - ▲ reduced or eliminated COLAs
- ▲ Increased use of hybrid retirement plans
- ▲ Two new defined contribution plans:
  - ▲ Oklahoma new hires as of 11/1/15
  - ▲ Elected officials in Arizona since 2013

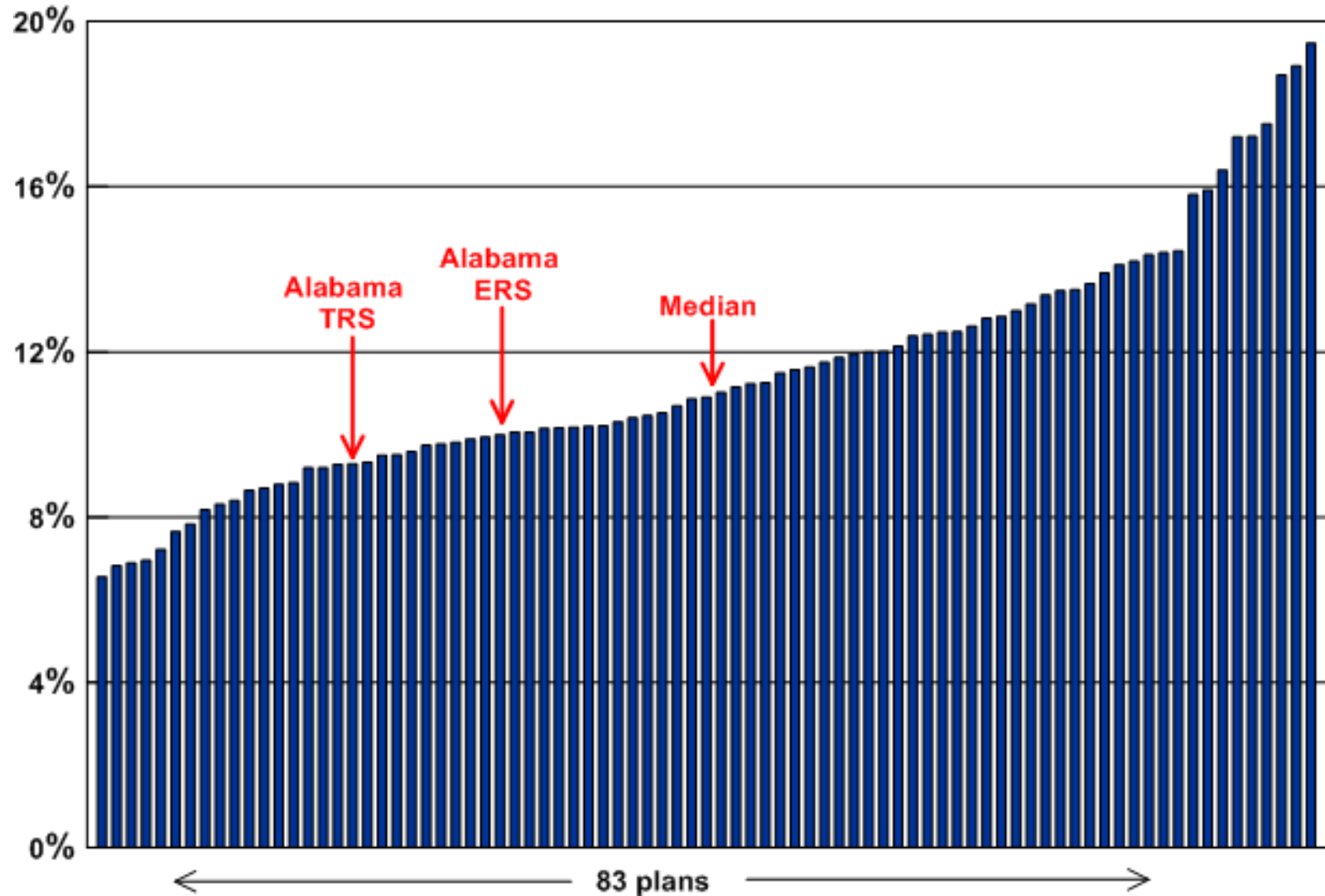
# Employer contribution rates as a percentage of payroll, FY 13, general employees and teachers, Social Security-eligible



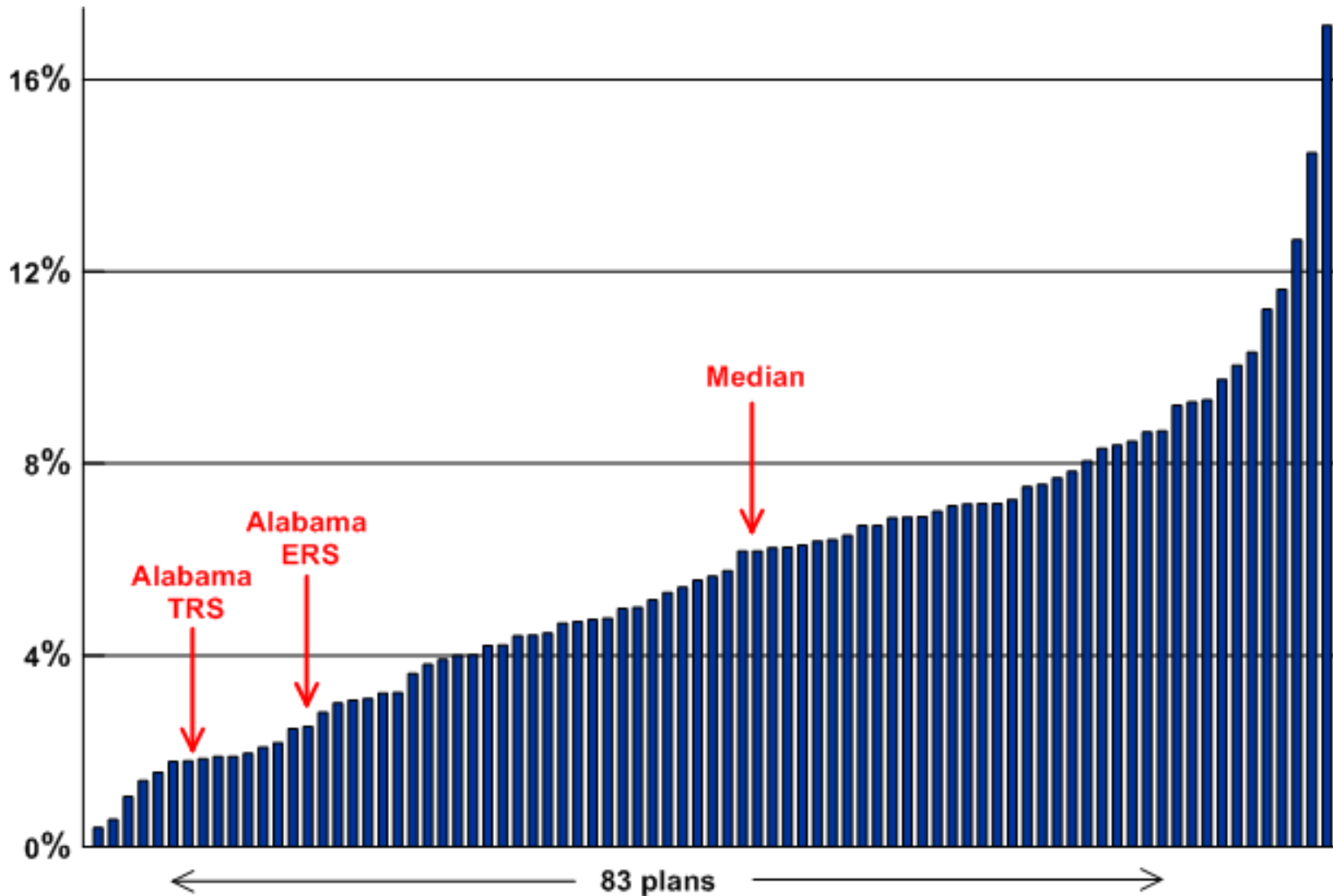
# Comparison of employee contribution rates FY 13, Social Security-eligible, general employees and teachers



# Normal cost as a percentage of payroll, FY 13 Social Security-eligible, general employees and teachers



# Employer normal cost paid as a percentage of payroll, FY 13, Social Security-eligible, general employees and teachers

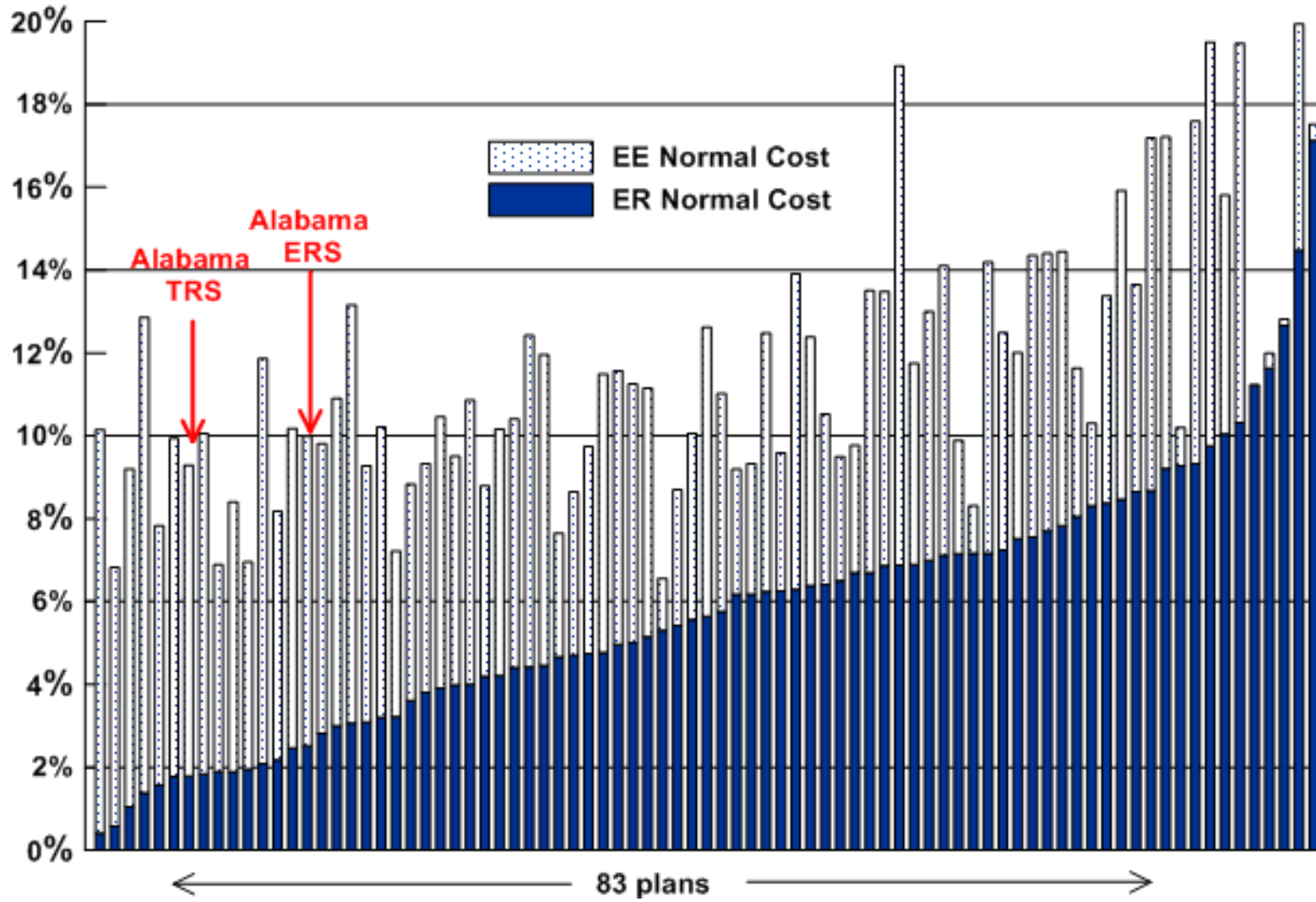


The employer normal cost for Tier II is below one percent of pay.

Compiled by NASRA based on data from the Public Plans Database



# Employee and employer normal cost paid as a percentage of payroll, FY 13, Social Security-eligible, general employees and teachers



Compiled by NASRA based on data from the Public Plans Database





# The Choice for Alabama Policymakers

- Considering that the cost to the state and its political subdivisions of the retirement plan for current hires is less than one percent of employee pay, what changes, if any, should be made?