

# *The Current Status of Public Pensions*

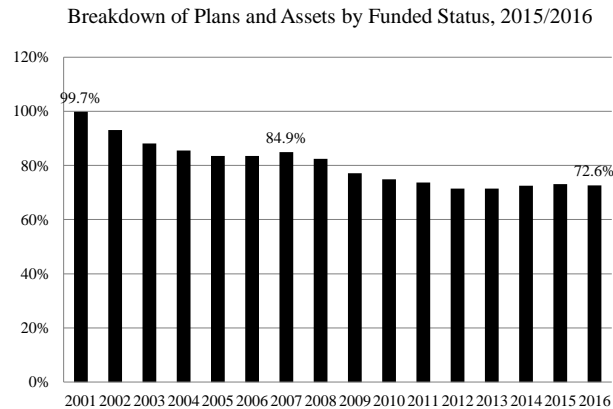
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National Association of State Budget Officers  
Phoenix, MA  
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## Overview

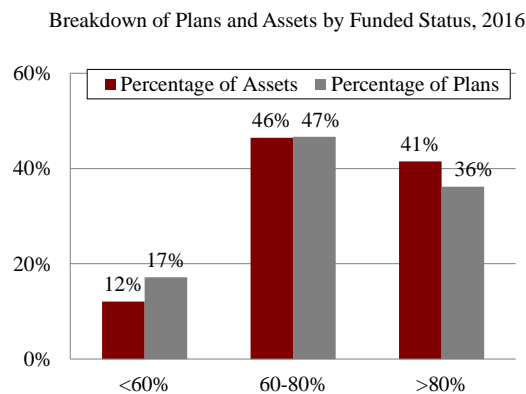
- What is the current status of public pensions?
- What have they done to improve their finances?
- What about the future?

Despite good returns, the funded ratio of public plans has remained flat since the financial crisis.



Source: Public Plans Database (2015-2016).

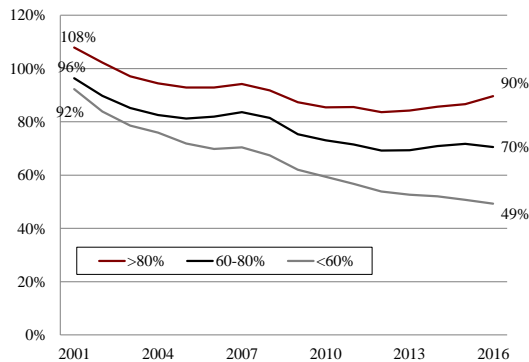
But, public plans are not all in the same position – they can be put into groups by funded status.



Source: Public Plans Database (2016).

Interestingly, all three groups of plans were relatively well funded in 2001.

Aggregate Funded Ratio by 2016 Funded Status, 2001-2016



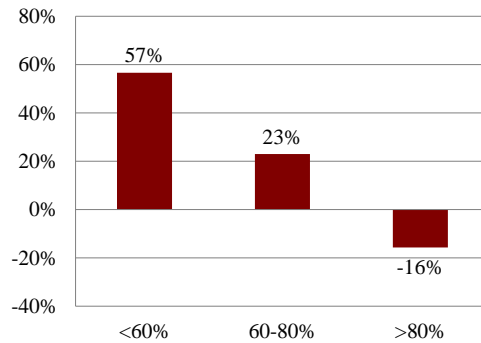
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Source: Public Plans Database (2001-2016).

4

But, even in 2001, good plans were more than fully funded while bad plans had substantial unfunded liabilities.

Unfunded Liability as a Percentage of Payroll by 2016 Funded Status, 2001



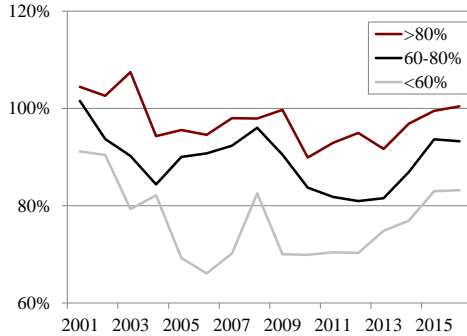
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Source: Public Plans Database (2001, 2015-2016).

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And, since 2001, good plans have paid more of their reported ARC...

Percentage of ARC Paid by 2015/2016 Funded Status, 2001-2016

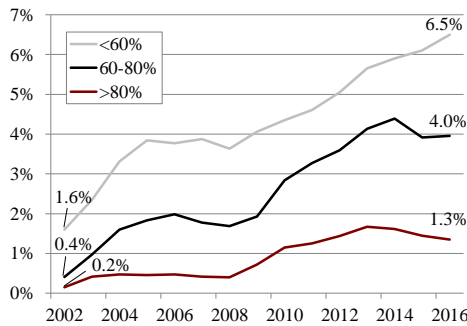


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Source: Public Plans Database (2001-2016).

...and kept their reported ARC closer to the desired measure.

Difference between Level-dollar ARC and Plan-calculated ARC as a Percentage of Payroll, 2002-2016

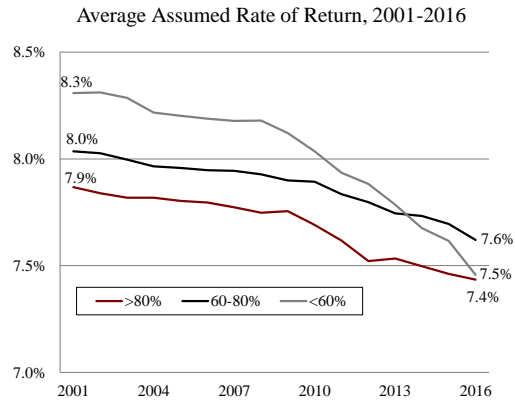


ARC estimates = level-dollar, closed amortization (no changes to plan assumptions).

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Source: Public Plans Database (2002-2016).

## The worst-off plans have lowered their assumed return by almost one percent,...



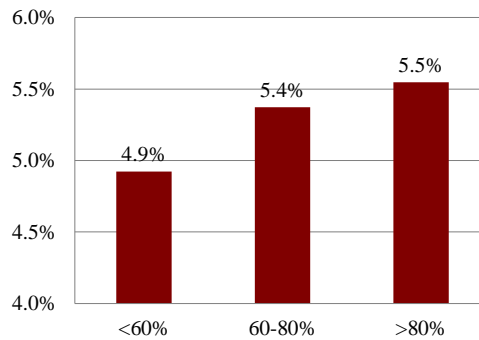
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Source: Public Plans Database (2001-2016).

8

## ...but they have also achieved the lowest returns.

Geometric Returns by 2015/2016 Funded Status, 2001-2016



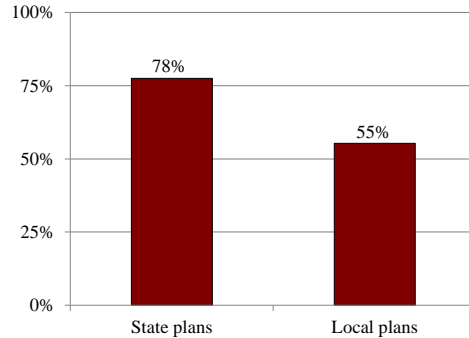
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Source: Public Plans Database (2001-2016).

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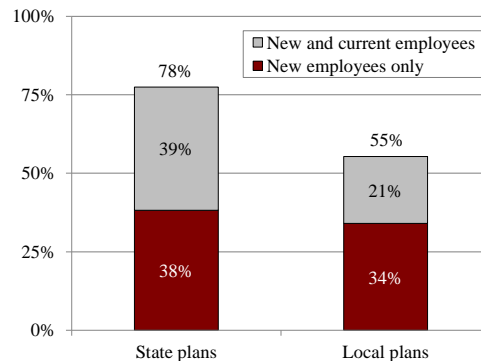
Since the crisis, three-quarters of state plans and half of local plans have made reforms.

Percentage of Plans Making Benefit Changes, 2009-2014



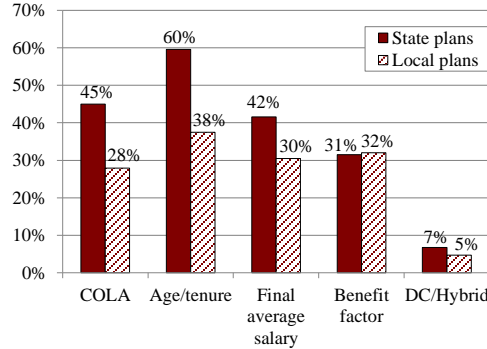
But, because most changes affect new hires only, plans' improvement has not been immediate.

Percentage of Plans Making Benefit Changes, by Type of Employee, 2009-2014



## For new employees, changes to core benefits were common.

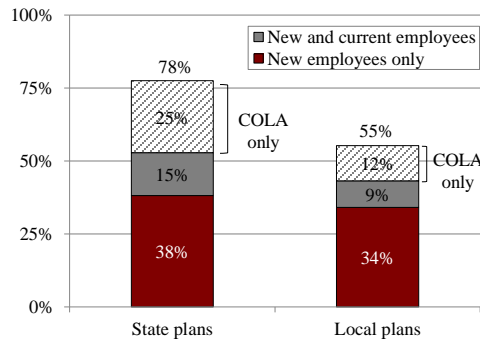
Percentage of Plans Making Benefit Changes to New Employees by Type of Reform, 2009-2014



Source: Author's calculations from various AVs and CAFRs (2009-2014).

## For current employees, cuts to COLAs were most common.

Percentage of Plans Making Benefit Changes, by Type of Employee, 2009-2014



Source: Author's calculations from various AVs and CAFRs (2009-2014).

## Reforms have focused on new hires due to legal protections for current employees.

Legal Basis for Protection of Public Pension Rights under State Laws

Legal basis	Benefit accruals protected			
	Past and future	Past and maybe future	Past only	None
State constitution	AK, IL, NY	AZ	HI, LA, MI	
Contract	CA, GA, KS, MA, NE, NV, NH, OR, PA, TN, VT, WA, WV	CO, ID, MD, MS, NJ, RI, SC	AL, AR, DE, FL, IA, KY, MO, MT, NC, ND, OK, SD, UT, VA	
Property	ME, WY	CT, NM	WI, OH	
Promissory estoppel <sup>a</sup>	MN			
Gratuity				IN, TX <sup>b</sup>

<sup>a</sup> Promissory estoppel is the protection of a promise even where no contract has been explicitly stated.

<sup>b</sup> In Texas, this gratuity approach applies only to state-administered plans. Accruals in many locally-administered plans are protected under the Texas constitution.

Sources: Cloud (2011); Monahan (2010); National Conference on Public Employee Retirement Systems (2007); Mumford and Pareja (1997); Reinke (2011); Staman (2011); Simko (1996); and subsequent communications with plan administrators and legal counsel.

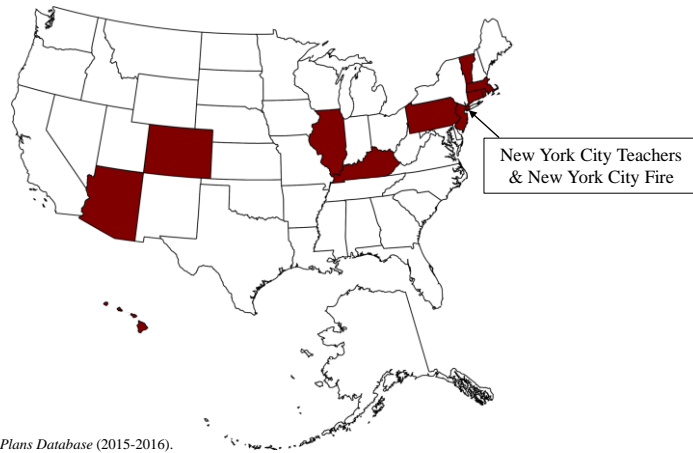
## What can plans do?

- Good plans (>80% funded)
  - Adopt best measure of ARC.
  - Gradually reduce return assumption.
- Middle plans (60-80% funded)
  - Adopt best measure of ARC.
  - Pay full ARC.
  - Gradually reduce return assumption.
  - Model investments after good plans.
- Bad plans (<60% funded): Most need a “grand bargain” that spreads sacrifice among workers, retirees, and taxpayers.



For the worst off, any grand bargain needs to consider historical context.

States with Plans under 60% Funded in 2015/2016

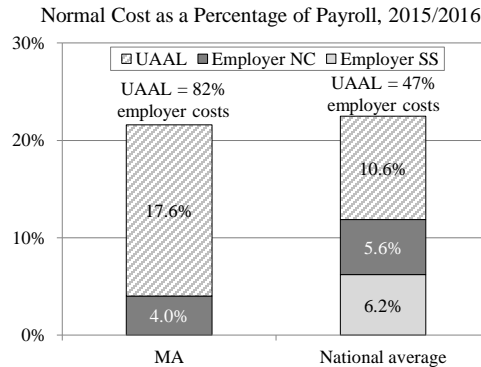


Some bad plans are old and have large legacy costs.

Massachusetts:

- 1910s: Plans created, funded on “pay-as-you-go” basis.
- 1987: Law adopted requiring actuarial funding within 10 years.
- 1998: Payments began based on actuarial funded schedule.

82% of MA retirement contributions go to legacy costs – no Social Security and small employer contribution to normal cost.



Note: For comparability, the MA UAAL amortization cost was recalculated based on a closed, 30-year, level-percent amortization of 2016 UAAL, assuming 3-percent payroll growth.  
Source: Public Plans Database (2015-2016).

So, two items merit consideration in any grand bargain.

- Perhaps remove legacy costs from the plan so that current employees are not burdened by historical underfunding.
- Any new defined benefit plan should have substantial risk-sharing so that we don't end up in the same mess again.

## Conclusion

- The public pension universe has separated into three groups: good, middle, and the bad.
- Plans can do better by:
  - using level-dollar, closed amortization period for ARC;
  - paying the full ARC;
  - gradually reducing assumed returns, and
  - trying to model investment performance after best plans.
- However, some plans can't solve their problem with traditional means and will require a grand bargain in which all parties sacrifice.

Center for Retirement Research at Boston College



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[http://crr.bc.edu/special\\_projects/state\\_and\\_local\\_pension\\_plans.html](http://crr.bc.edu/special_projects/state_and_local_pension_plans.html)

*Public Plans Database (PPD)*



<http://publicplansdata.org/>



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