

RESEARCH ON GOVERNMENT PENSIONS IN RELATIONS TO SOCIAL SECURITY COVERAGE

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The content of this presentation came from multiple sources including GASB, SSA, GAO, Center for Retirement Research at Boston College, Pew Charitable Trusts, NASRA and other research done by speakers

TODAY'S DISCUSSION AGENDA

- **Types of SLG pensions**
- **Status of pensions**
 - State and municipal
 - Employee benefit research
- **Social Security**
 - Present financial status
 - Section 218
- **“What if” scenarios**
 - Who makes up the difference?
 - Where do we go from here?
 - How is GASB 67/68 going to impact financial statements?

TYPES OF PENSIONS

- **Defined Benefit Plan**

- Promises to pay you certain amount of retirement income for life
- Based on formula that takes into account your earnings and years of service
- Risk is on employer
- Employer is responsible for investing contributions to ensure there's enough funds to pay for future pensions

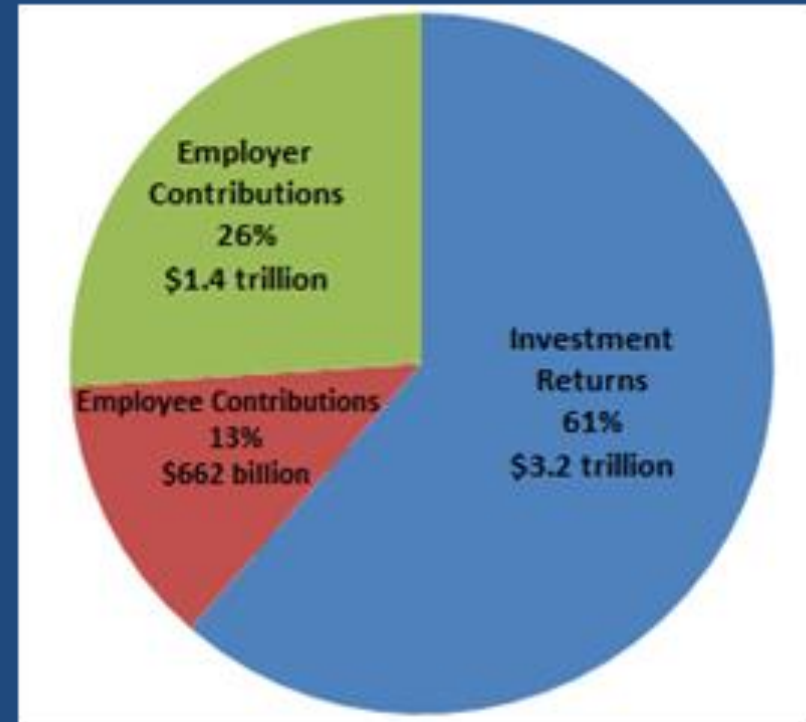
- **Defined Contribution Plan**

- Retirement income is not guaranteed
- Employer normally “matches” contribution to a certain level (6% average)
- Employee is responsible for investing all contributions to grow savings
- Employee will make decisions at end of service on how earnings distributed

- **89% SLG in defined benefit; 2% defined contribution; 7% hybrid; and 2% cash balance**

PENSIONS TODAY

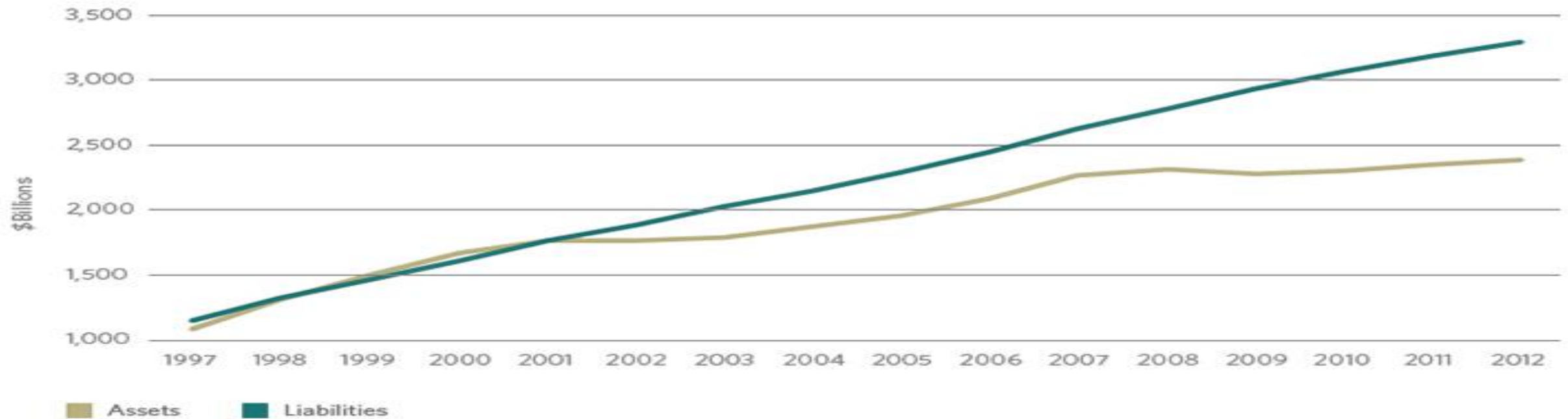
- \$18.9 T in global pension assets at end of 2013 – market value
- \$3.6T in public pension assets at end of March 2014 – market value
 - 15 million working and 8 million retired employees of SLG
 - Chart to right is Public Pensions Based on Revenue from 1982 – 2011 which was compiled by NASRA after compilation of U.S. Census Data.



STATE PENSION FUNDS IN GENERAL TAKEN FROM 235 PENSION PLAN CAFRS FOR FY 2012

The Growing Gap in State Pension Funds

Pension funding has been declining since 2000 as liabilities have grown faster than assets



Source: The Pew Charitable Trusts
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STATE AND LOCAL GOVERNMENT PENSIONS ACTIVITY IN PAST 5 YEARS

- Since 2009, **48 states** have enacted retirement plan changes with bulk of reform focused on making pension plans more **fiscally sustainable**
 - **36 states** have increased required employee contribution rates
- Financial crisis of 2008 generated **two types of responses** from pension sponsors:
 1. Cut back on existing defined benefit plan commitments by raising employee contributions, reducing benefit for new employees and/or suspending cost-of-living adjustments for existing retirees.
 2. Initiate proposals and/or studies to shift some or all of pension system from a defined benefit to defined contribution activity.

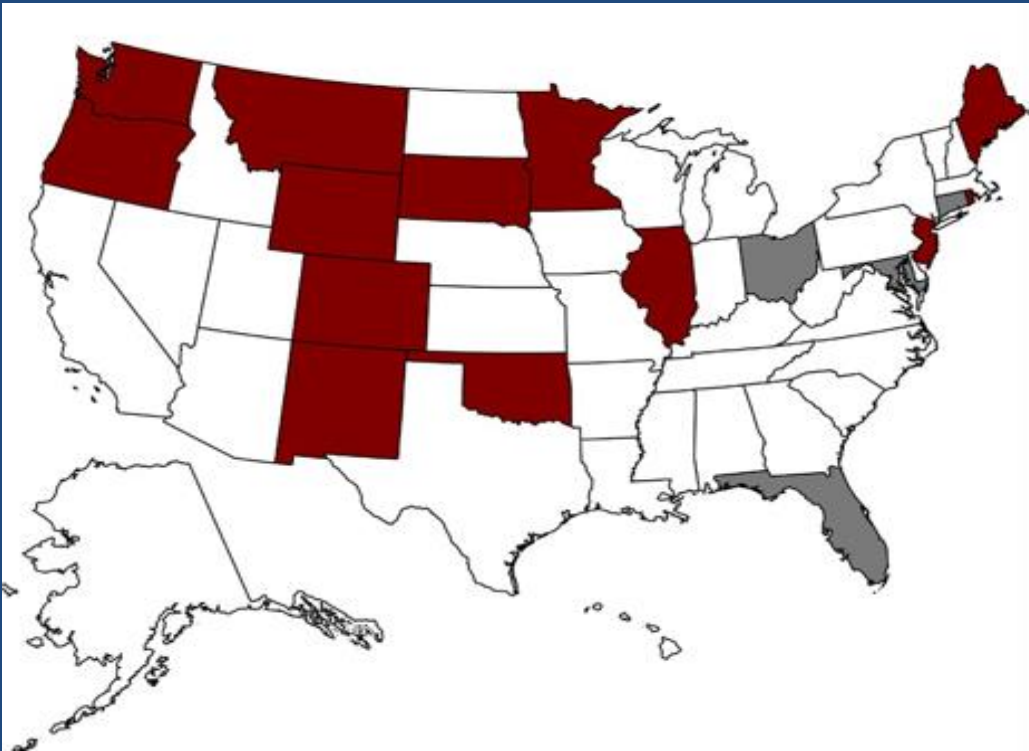
EXAMPLES OF PENSION REFORM IN STATES

- New Contributions – Missouri, Florida, Virginia
- Variable Contributions – Pennsylvania, Arizona, Iowa, Nevada
- Increased Contributions – Alabama, New Mexico, Wyoming, Wisconsin
- Hybrid Plans – Georgia, Michigan, Rhode Island, Utah, Virginia, Tennessee
- Collective Bargaining - California
- Cash Balance Plans – Kansas, Kentucky
- Suspended/Eliminated COLA – New Jersey, Rhode Island, Oklahoma

CHANGES TO CONTRIBUTIONS AND COLAS FOR STATE PENSIONS SINCE 2009

States that have increased employee contributions in at least one public pension plan since 2009

States that have eliminated, suspended, or reduced COLAs for Retirees since 2009



WHAT ABOUT THE BURDEN ON MUNICIPALITIES?

- Detroit's Bankruptcy Court Judge determined that Chapter 9 could cut pension payments for city retirees if not part of bankruptcy plan of adjustment
 - Workers and retirees agreed to cut of 4.5% with reduced OPEB
 - State, private foundations, and Detroit Institute of Arts will make up difference in deficit of pension funds
- Central Falls, Rhode Island pensioners agreed to 25% - 45% cut for five years as part of bankruptcy agreement
- Average cost to U.S. cities for pension costs is 5.6 - 7.9% of city revenues.
- Average costs ranges from 12.3% to 2.7% of taxpayer revenues going to fund pension and OPEB costs.

CITIES WITH HIGHEST PENSION COSTS AS A PERCENT OF REVENUE

City, State	Pension Costs/Revenue
Little Rock City, AR	17.6
Chicago City, IL	17.0
Aurora City, IL	16.1
Charleston City, WV	15.7
Reno City, NV	15.5
Springfield City, MA	15.0
Bakersfield City, CA	14.5
Stockton City, CA	14.1
Saginaw City, MI	13.8
New York City, NY	12.9

NATIONAL COMPENSATION SURVEY

- National Compensation Survey Recent Reports for workers 25-64:
 - 80% of employers sponsor a retirement plan
 - 99% of state-local workers participate in a sponsored plan
 - 50% of private sector workers participate in retirement plan
 - 1/3 of households in United States reach age 60 with **NO RETIREMENT PLAN AT ALL**
 - **54% OF SLG workers say they expect to retire at age 65 or later**
 - **Only 4% said they do NOT EVER expect to fully retire**
- In a 2013 poll of 2,110 SLG workers, over 20% did not know what retirement plan their employers offer with 36% of those respondents in the 18-29 age range.
- 46% of workers younger than 50 said they would prefer a higher salary and lower retirement benefits compared with 33% of older workers.
- Bottom 40% of income distribution almost entirely dependent on Social Security according to recent research by Boston College's Center for Retirement Research.

ACCORDING TO EMPLOYEE BENEFIT RESEARCH INSTITUTE 2014 SURVEY

Figure 17
Total Savings and Investments Reported by Workers
Among Those Providing a Response
 (not including value of primary residence or defined benefit plans)

In total, about how much money would you say you (and your spouse) currently have in savings and investments, not including the value of your primary residence (or value of defined benefit plans)? (2014 Workers n=783)

	<u>2004</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	2014 Has Ret. Plan*	2014 No Ret. Plan
Less Than \$1,000	54%	20%	27%	29%	30%	28%	36%	11%	73%
\$1,000–\$9,999		19	16	17	18	18	16	17	16
\$10,000–\$24,999		13	11	10	12	11	8	10	5
\$25,000–\$49,999	14	11	12	11	10	9	9	14	2
\$50,000–\$99,999	11	12	11	9	10	10	9	14	<0.5
\$100,000–\$249,999	13	12	11	14	11	12	11	16	2
\$250,000 or More	9	12	11	10	10	12	11	17	1

*Has Retirement Plan defined as respondent or spouse having at least one of the following: IRA, DC plan, or DB plan

Source: Employee Benefit Research Institute and Greenwald & Associates, 2004–2014 Retirement Confidence Surveys.

ON THE FLIP SIDE - SOCIAL SECURITY

- Social Security Act of 1935 enacted in response to Great Depression
- Title II of Social Security Act – 1951 – allowed voluntary Social Security coverage to government employees of state and local governments (SLG)
- Social Security Trust Fund is scheduled for exhaustion in 2033
- To boost the Social Security trust fund, Congress is debating making Social Security tax payments mandatory for SLG.
- More than 25% of SLG employees belong to retirement plans that DO NOT PARTICIPATE in Social Security
- Approximately 70% of SLG earnings not covered by Social Security are concentrated in 5 states – California, Texas, Ohio, Illinois and Massachusetts

SOCIAL SECURITY'S FINANCIAL OUTLOOK AS OF 2013 – TRUST FUND OPERATIONS

Table 1. Trust Fund Operations (in billions)

	OASI	<u>DI</u>	HI	SMI
Reserves (end of 2012)	\$2,609.7	<u>\$122.7</u>	\$220.4	\$67.2
Income during 2013	743.8	<u>111.2</u>	251.1	324.6
Cost during 2013	679.5	<u>143.4</u>	266.2	316.7
Net change in Reserves	64.3	<u>-32.2</u>	-15.0	7.9
Reserves (end of 2013)	2,674.0	<u>90.4</u>	205.4	75.1

SOCIAL SECURITY'S FINANCIAL OUTLOOK AS OF 2013 – PROGRAM COSTS

Table 2. Program Cost (in billions)

Category (in billions)	OASI	DI	HI	SMI
Benefit payments	\$672.1	\$140.1	\$261.9	\$313.1
Railroad Retirement financial interchange	3.9	0.6	—	—
Administrative expenses	3.4	2.8	4.3	3.7
Total	679.5	143.4	266.2	316.7

SOCIAL SECURITY'S FINANCIAL OUTLOOK AS OF 2013 – PROGRAM INCOME

Source (in billions)	OASI	DI	HI	SMI
Payroll taxes	\$620.8	\$105.4	\$220.8	—
Taxes on OASDI benefits	20.7	0.4	14.3	—
Beneficiary premiums	—	—	3.4	\$73.3
Transfers from States	—	—	—	8.8
General Fund reimbursements	4.2	0.7	0.9	4.3
General revenues	—	—	—	\$232.5
Interest earnings	98.1	4.7	9.3	2.4
Other	—	—	2.4	3.7
Total	743.8	111.2	251.1	324.6

SECTION 218 OF SOCIAL SECURITY ACT

Title II Section 218 of the Social Security Act

- Tenth Amendment
 - Federal Government cannot tax state government
- Allows voluntary Social Security coverage to government employees through referendum process.
 - Absolute Coverage
 - State and Local Government employees not covered by a Social Security equivalent retirement plan mandatorily covered by Social Security
 - Retirement System Coverage
 - State and Local Government employees covered by a Social Security equivalent retirement plan may vote to adopt Social Security coverage.

WHICH STATES DO NOT PARTICIPATE IN SOCIAL SECURITY (FOR MOST PART)

- 2007 Government Accountability Office (GAO) study states that bulk of uncovered public employees reside in 14 states:

Alaska

Louisiana

California

Maine

Colorado

Massachusetts

Connecticut

Missouri

Georgia

Nevada

Illinois

Ohio

Kentucky

Texas

AUDITS OF GOVERNMENTAL ENTITIES

Internal Revenue Service performs audits of government entities including compliance with 218 agreement

- Non compliance in many situations found evident
 - Missouri teachers should have been paying and were not.
- Government Accountability Office reports to Congress the current situation.
 - Possibly solution to require Social Security coverage for all individuals.
- Mandatory Social Security will have an effect on the fiscal stability of the states' budgets and/or pension systems.

ANNUAL COST TO COVER UNCOVERED EMPLOYEES

Ten States with Most Uncovered Employees

▪ Alaska	\$196 Million
▪ California	\$8.48 Billion
▪ Colorado	\$1.07 Billion
▪ Illinois	\$2.47 Billion
▪ Louisiana	\$1.00 Billion
▪ Maine	\$240 Million
▪ Massachusetts	\$2.11 Billion
▪ Nevada	\$705 Million
▪ Ohio	\$3.37 Billion
▪ Texas	\$3.55 Billion

The total cost to all state and local governments for the coverage of the non Social Security covered employees at the 2007 rate would be in excess of \$28 Billion

GASB STATEMENTS 67 AND 68

Governmental Accounting Standards Board (GASB) Statements No. 67 and No. 68

- Removed the parameters for calculating annual required contributions and changed the funding ratio parameters.
- Plan assets
 - Now valued at market rate instead of actuarial value
 - Pension liabilities covered by these plan assets will use a blended rate instead of the long-term yield rate.
 - Under new GASB reporting method, the aggregate funding ratios for state and local government pension plans in comparison to the old reporting method dropped from 79% to 49% in 2009 and 77% to 53% in 2010 (Alicia H. Munnell, 2011).
- The new standard is a change in valuation and not truly a change in performance making it appear that pension funds are continuing on a downward spiral.

ACCORDING TO ANALYSTS, WHERE ARE PENSIONS HEADED

- **GASB 67/68** enactment after July 1, 2014- governments will have to calculate an estimate of how much they owe for future pension liabilities and put on balance sheet.
 - Doesn't change what they owe – but will bring underfunding to light.
 - Bond ratings will be affected.
 - According to one estimate, state and municipal governments across the country have a total unfunded pension liability of \$4.1 trillion.
- How will local governments be hit?
 - In Chicago alone, the estimate is that each household will need to contribute \$61,000 to fully fund their city employee pensions and OPEB.
 - Approximately 5.6% of local government revenues raised from taxpayers will go towards pension costs for local government employees.