

Presentation to the Pennsylvania House Subcommittee on Public Pensions, Benefits and Risk Management

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Anna Petrini, senior policy specialist, Employment, Labor & Retirement Program

- 1. What are the key characteristics of public employee pension plans?
- 2. How have states altered their plans in recent years?
 - Funding basics and contribution rates
 - Higher age and service requirements
 - COLA Changes
- 3. Which states have replaced traditional DB plans with alternative designs?
- 4. What are alternative structures (DC, Hybrid, Cash Balance) and how do states vary?
- 5. Other recent trends? How are post-recession reforms playing out?



Legislative Trends in Plan Design and Funding: 5 Key Questions

Session Overview





Q1: What are key characteristics of public employee pension plans?

Why? The value of retirement security for employers, employees, and the broader economy.







Who participates and do they have Social Security coverage?



Where?

What's the geography of pension plan coverage?



What?

What are typical benefits and asset levels?



When?

What are historical trends affecting pensions?

Tracking Major Pension Legislation in the States





2020-2021

- NCSL tracks legislation changing state retirement plans for general employees and teachers.
- This session, retirement system legislation is being or has been considered in 44 states.
- NCSL's Pension Legislation Database has
 732 pieces of legislation so far for 2021.
- At least 175 bills were enacted in 2020 in
 40 different states.



Since 2009

- 2009 10 states
- 2010 21 states
- 2011 32 states
- 2012 10 states
- 2013 6 states and Puerto Rico
- 2014 8 states
- 2015 4 states
- 2016 2 states
- 2017 8 states
- 2018 5 states
- 2019 5 states
- 2020 1 state
- 2021 at least 6 states



How Pensions Work











Participation

Mandatory or optional

Contributions

Employer and Employee

Age and Service Requirements

Normal and early retirement; vesting period

Benefits

Benefit levels, caps and formulas

Distribution

Methods











Compounded Investment Earnings



Age and Service Requirements

Increased Ages for Normal Retirement



Contribution Rates

Rate Increases for Current and Future Employees



COLA Changes

Cost of Living Adjustments

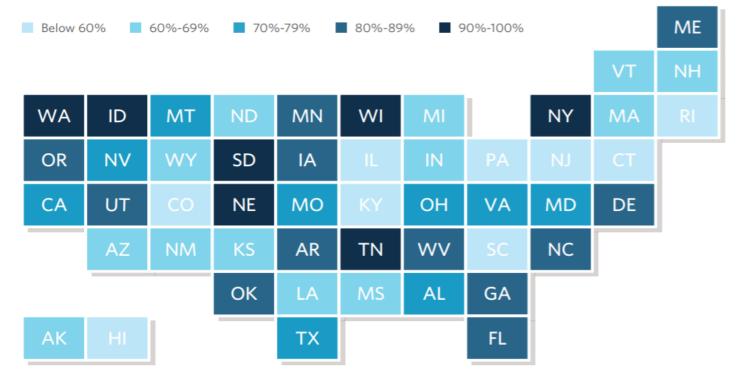
Pension Funding Levels

"Simple as it may sound, the path to improving the fiscal health of public pension plans starts with making contributions that are sufficient to reduce unfunded pension liabilities over time."

The Pew Charitable Trusts, The State Pension Funding Gap: 2018

State Pension Funding in 2018

Just seven states were 90% funded, while nine states were less than 60% funded



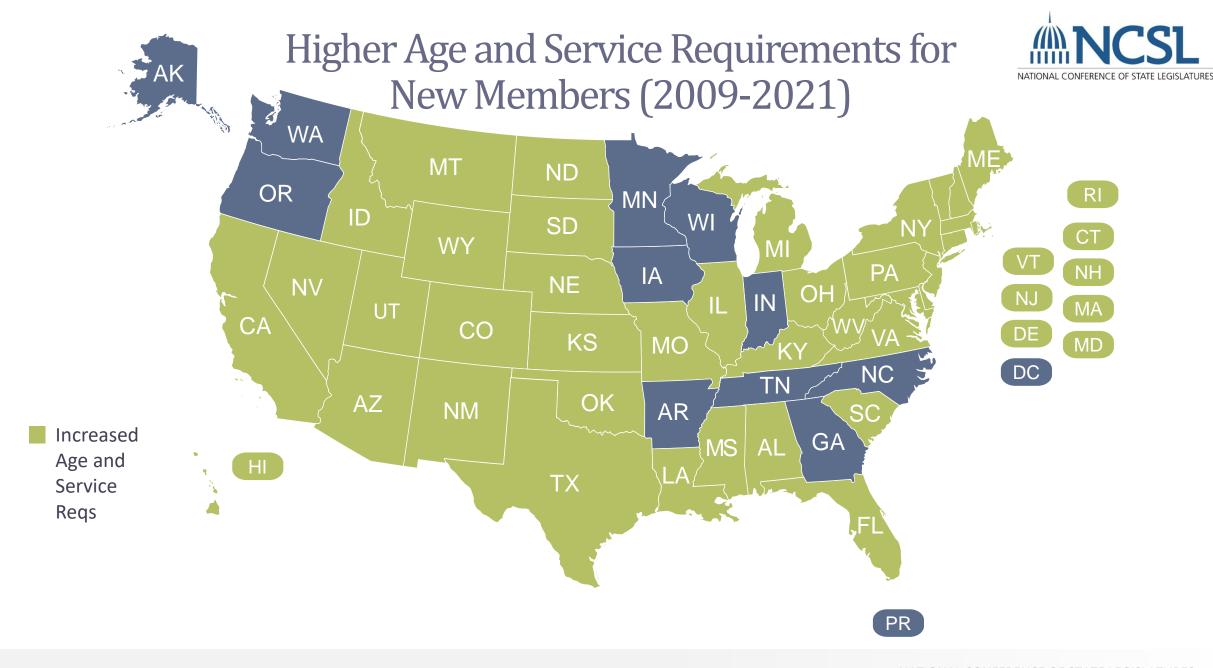
Note: Numbers reflect the Governmental Accounting Standards Board reporting standards as of 2018.

Sources: Comprehensive annual financial reports, actuarial reports and valuations, other public documents, or as provided by plan officials

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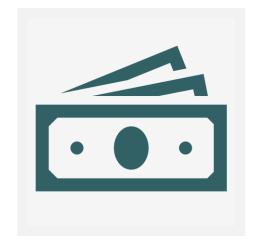






Other Key Design Features Cost-of-Living Adjustments (COLAs)













What

Two broad categories: ad hoc and automatic.

Who

Critical for state and local workers outside Social Security.

Where

Most state and local pension plans have COLAs, but more than 30 states have reduced, suspended or eliminated since 2009.

When

Can fluctuate with inflation, be linked to plan funding levels, investment returns, etc.

Why

Help insulate retirees from inflation.

Reductions in Post-Retirement Benefit Increases



2009-2021



10

At least some actives

Future hires only



Retirees and actives





Q3: Which states have replaced traditional DB plans with alternative designs?

Q4: What are alternative structures and how do states vary?







Final Average Salary X Years of Service X Multiplier



Hybrid DB-DC

Combines DB and DC features; side-by-side or stacked



Defined Contribution

Savings account; risk shifting



Cash Balance

Individual Accounts; Guaranteed ROR



Defined Benefit (DB) Plan Design

- Employer sponsored retirement benefit
- **Eligibility requirements**: workers must reach age and service thresholds
- Monthly benefit based on salary and length of service

Sample Calculation

- \$100,000 final average salary x 30 years of service x 2% retirement multiplier = \$60,000 annually
- Final Average Salary: often the average of several highest years of compensation
- Years of service or service credit refers to an employee's length of employment
- Multiplier: a factor that is applied to determine the amount of a retired employee's annuity

Statewide Retirement Plan Designs



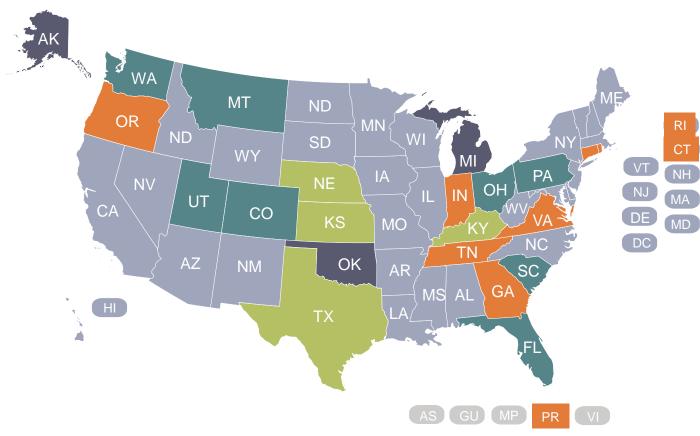
(Non-Defined Benefit)

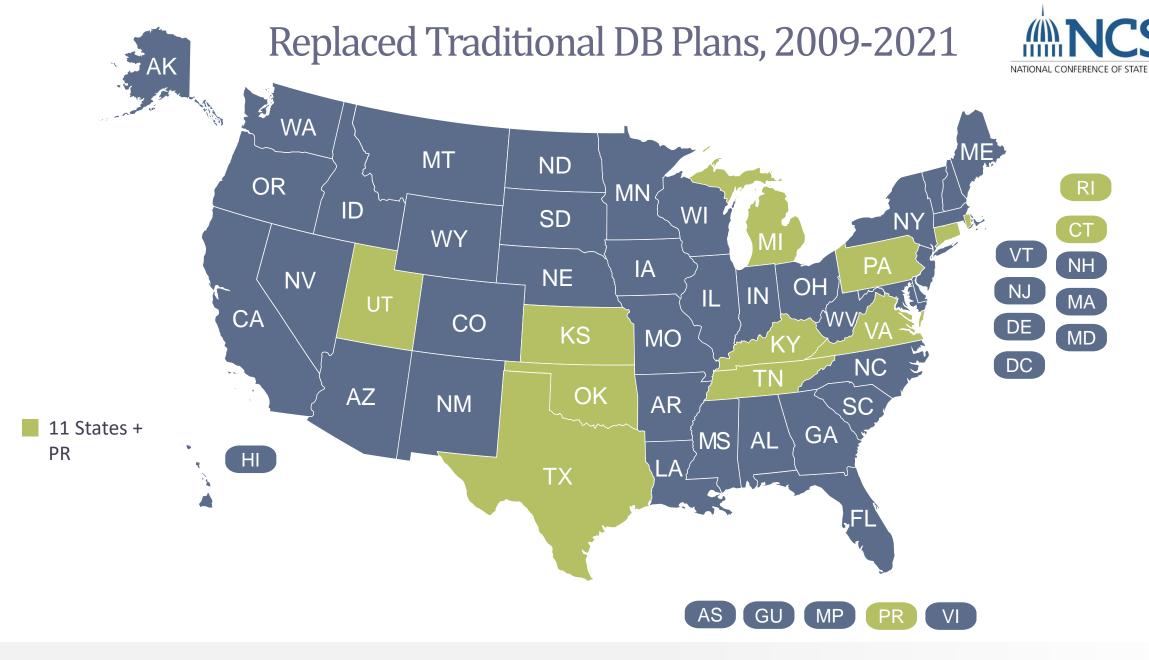
Choice of Primary Plan (8

states)







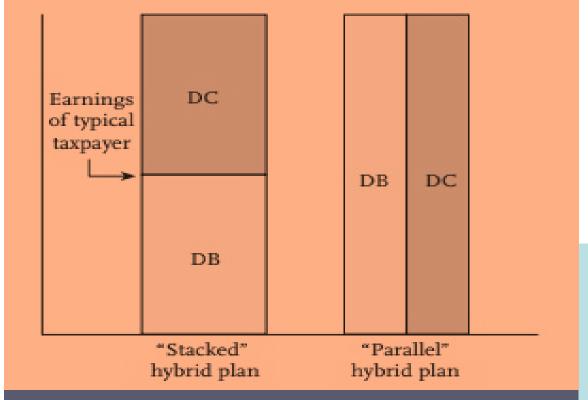


Defined Contribution (DC) Plan Design

- Function like savings accounts.
- ❖ Funds are more portable.
- Stabilizes states' costs for new hires.
- Risks and responsibilities shifted to employee:
 - Risk of losing funds with investment fluctuations.
 - ❖No guaranteed rate of return.
 - Employee must (usually) choose:
 - ❖Their contribution amount (risk saving too little);
 - Among investment options.
- *Administrative & investment costs are generally higher than with DB plans.









Investment Gains or Losses

Hybrid DB-DC Plan Design

Cash Balance Plan Design

- Provides each member with an individual account.
- **Employees** and employers contribute.
- ❖The member cannot choose how the money is invested.
- Members' accounts are managed in one trust fund, and members are guaranteed a return on investment.
- ❖ If investment return makes it possible, member accounts can receive additional returns.
- In public plans, upon retirement, the member receives an annuity based on the account balance.

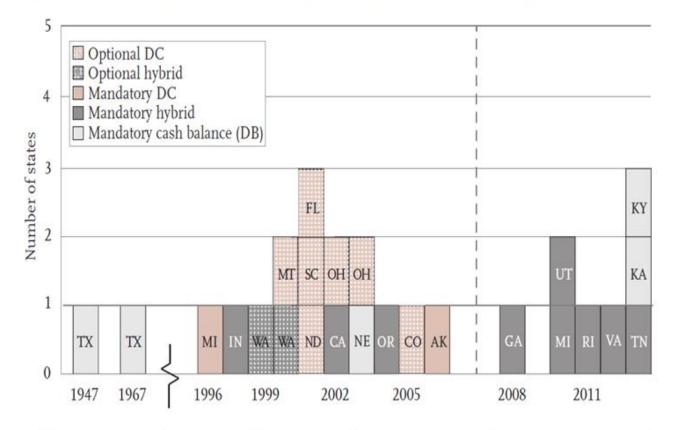






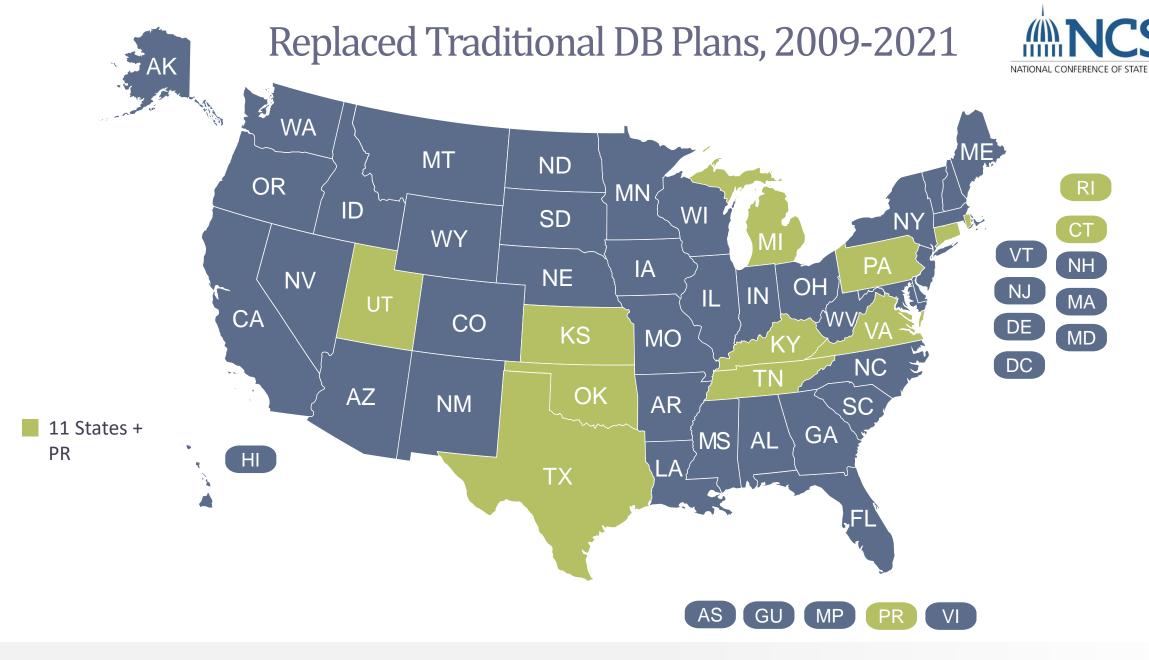
When Were Non-DB Plans Adopted?

Figure 1. Introduction of State Defined Contribution Plans, by Year, 1947-2013⁴



Sources: Actuarial reports; state websites; National Association of State Retirement Administrators (2013); and Munnell (2012).

Source: Center for Retirement Research at Boston College, A Role for Defined Contribution Plans in the Public Sector: An Update, 2014



Why Have Non-DB Plans Been Adopted?





Before the Great Recession



After the Great Recession

 Offer employees the opportunity to manage their own money and participate directly in a rapidly rising stock market.

- Avoid high costs associated with large unfunded liabilities;
- Unload some investment and mortality risk associated with DB;
- Have a less back-loaded benefit structure to aid short-term employees when they leave.











Small number of participants, but this will change over time





Certain classes of employees

Retirement Plan Choices for Public Employees

Source: Decisions, Decisions: Retirement Plan Choices for Public Employees and Employers, Milliman, National Institute on Retirement Security, August 2017.

Table 2. New Hire Elections in Most Recent Complete Year*

System	DB Plan Enrollments	DC Plan Enrollments	Combined Plan Enrollments
Colorado Public Employees' Retirement Association	88%	12%	Not offered
Florida Retirement System	75%	25%	Not offered
Montana Public Employee Retirement Administration	97%	3%	Not offered
North Dakota Public Employees Retirement System**	98%	2%	Not offered
Ohio Public Employees Retirement System	95%	4%	1%
State Teachers Retirement System of Ohio	89%	9%	2%
South Carolina Retirement Systems	82%	18%	Not offered

[&]quot;Not offered" means enrollment in a combined DB/DC plan is not offered.



^{*}Data for Colorado, North Dakota, and Ohio PERS are for January 2010 through December 2010. Data for Florida, Montana, STRS Ohio, and South Carolina are for July 2010 through June 2011.

^{**} One new employee out of the 63 eligible joined the North Dakota DC plan in 2010.





How are post-recession reforms playing out?







Risk Assessment



New Jersey

Dedicated Funding Sources



Maine

Revised Investment Strategies



North Carolina

OPEB Reform

Evaluating Features of Different Benefit Designs

Source: The Hybrid Handbook |Not All Hybrids Are Created Equal, Cheiron; National Institute on Retirement Security, May 2021.

Table 1: Evaluating Key Features of Various Retirement Benefits

Key Features and Goals	Final Pay Pension	Cash Balance	Parallel DB/DC	Stacked DB/DC	Contribution Rate Risk Sharing DB	Variable Benefit DB	DC
Adequacy and provision of lifetime income to those who:							
Worked a full career and retire from the plan		1	1			1	
Mid-career hire, retire from plan			1	-		1	
Hired young, but terminated before retirement							•
Purchasing power preservation in retirement	•			•	•		
Funding predictability						•	
Funding flexibility				•			
Benefit predictability and transparency							
Workforce management effectiveness				•	1	•	



Anna Petrini Anna.Petrini@ncsl.org (303) 856-1527



Thank You!

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