

# The Case for Public Pensions



**TMRS Seminar  
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# Overview

- **Snapshot of the nation's retirement condition**
- **Primary concerns:**
  - **Financial illiteracy**
  - **Defined contribution plans**
  - **Social Security**
- **The case for public pensions: a stakeholder perspective**

# Retirement Benefits Comparison

## Private Sector

- One-third have no access to an employer-sponsored retirement benefit
- One-fourth of those eligible do not participate
- Barely one-half are in an employer-sponsored plan
- Fewer than one in five have a traditional pension (DB) plan
- Universal Social Security

## Public Sector

- Nearly all have access to an employer-sponsored retirement benefit
- Ninety percent have access to a traditional pension (DB plan)
- Three-fourths participate in Social Security

# Financial Illiteracy is Widespread

- Studies show:
  - A large percentage of Americans lack understanding of basic financial concepts, such as:
    - compound interest
    - balancing a checkbook
    - the costs of not paying off a credit card balance
    - the importance of maintaining a savings buffer
    - amounts necessary to replace income in retirement

# Defined contribution plans are unreliable vehicles for delivering retirement income

- Defined contribution plans, like 401(k) plans, are characterized by:
  - leakage via loans and pre-retirement withdrawals
  - insufficient savings rates
  - high fees
  - longevity risk
  - poor asset allocations
  - poor returns

# Americans are poorly prepared for retirement

- Twenty-seven percent of American adults say they have less than \$1,000 in savings
- Median value of 401(k) plans in 2009 for workers aged 55-64: \$56,212
- More than half of workers (54 percent) report that the total value of their household's savings and investments, excluding the value of their primary home and any defined benefit plans, is less than \$25,000

# Americans are poorly prepared for retirement

- Fewer than half (46%) of working Americans have calculated how much they'll need in retirement
- The percentage of workers who expect to retire after age 65 has increased, from 11 percent in 1991 to 14 percent in 1995, 19 percent in 2000, 24 percent in 2005, and 33 percent in 2010
- Estimated medical costs for a couple age 65 are \$250,000

# Retirement insecurity in a nutshell

“The biggest, but most underreported, financial story in America is the looming retirement disaster. Eighty million baby boomers are approaching retirement, and most have absolutely no idea what's going to hit them. For them the financial crisis isn't over. It's just about to begin.”

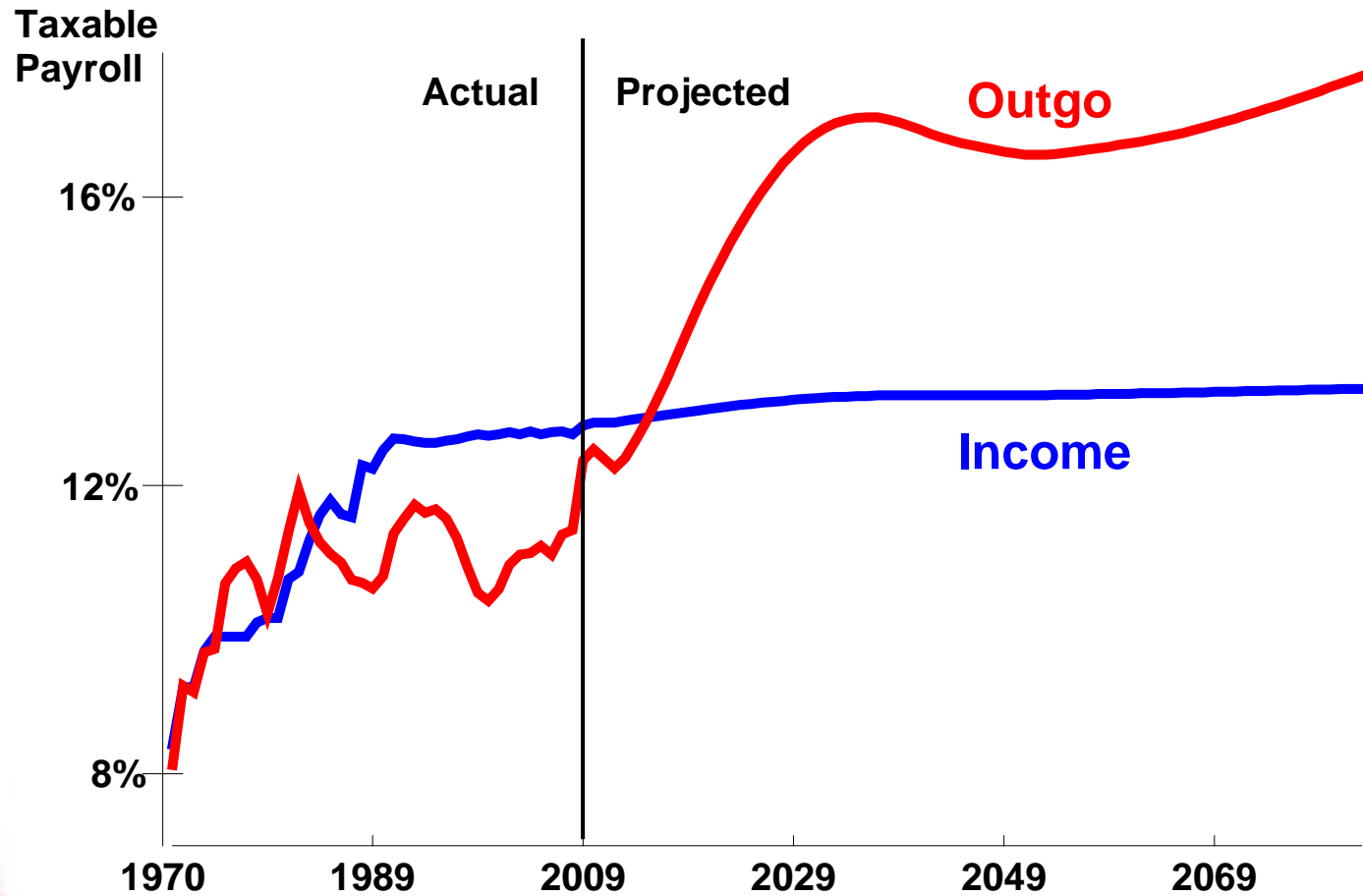
Wall Street Journal, June 11, 2010

# Americans rely heavily on Social Security

- More than half (56 percent) of those on Social Security rely on it for more than half of their income.
- For 30 percent of Social Security recipients, Social Security accounts for 90 percent of retirement income.
- For almost one of every five Social Security recipients, (19 percent) Social Security is the sole source of income.

**Source: Social Security Administration**

# Social Security Income and Outgo



Social Security Administration

# Distinguishing elements of a defined benefit plan

- Mandatory participation
- A benefit that reflects the worker's salary and length of service
- Assets that are pooled and professionally invested
- A benefit that cannot be outlived
- *TMRS is a defined benefit plan*

# The basic retirement equation

$$C + I = B + E$$

Contributions plus Investment earnings

equals

Benefits plus Expenses

# The case for public pensions: a stakeholder perspective

- Who are public pension stakeholders, and what do they want?
  - **Public employees** – reliable income in retirement
  - **Public employers** – to attract and retain qualified workers needed to perform essential public services
  - **Taxpayers** – a tax burden that is fair and predictable
  - **Recipients of public services** – reliable delivery of public services
- *These groups are not mutually exclusive*

# Public employees as public pension stakeholders

- What do public employees want in a retirement plan?
  - A reliable income in retirement
  - Pooled assets invested by professionals
  - Lower costs and higher returns
  - A benefit that cannot be outlived
  - Poverty prevention

# Public employers as public pension stakeholders

Compared to the private sector, public employees are more likely to

- Have a college degree:
  - *One-half v. one-fourth*
- Work in a position that involves physical risk:
  - *law enforcement, hazardous waste, firefighting*
- Stay on the job longer:
  - *median tenure: 7.2 v. 3.6 years*
- Be older:
  - *50% of public sector is age 45 and older, compared to 40% of the private sector*

# Public employers as public pension stakeholders

- What do public employers want in a retirement plan?
  - Attract and retain qualified workers needed to perform essential public services
    - Especially retain
    - A large portion of public sector positions are career or long-term: teachers, public safety
  - Promote an orderly turnover of personnel
    - Retire employees at an appropriate age
  - Employers have a moral interest in employees' retirement readiness

# Taxpayers as public pension stakeholders

- What do taxpayers want in a public employee retirement plan?
  - Costs that are reasonable and predictable
- Taxpayers also benefit from the economic effects of public pensions
  - Substantial economic benefits in the form of increased output and job creation

# Recipients of public services as public pension stakeholders

- Seek the reliable, cost-efficient delivery of public services
- Include taxpayers, public employees, and public employers and have many of the same objectives:
  - Poverty prevention
  - A moral interest in retirement security for all
  - Economic benefits
  - Orderly turnover of personnel

# Retirement security benefits everyone

- **Pensions work**

- When they're allowed to work: properly designed and funded
- They are the most effective and economical method for delivering retirement income
- Pensions are especially important for non-Social Security participants

- **Pension policies have long-term impacts**

- Minor adjustments to benefit levels can have major effects later on
- Retirement security is at stake
- Pension plans are flexible and can be modified

- **Pensions support our local economy**

- Pension benefits are spent in our cities and this state
- Pension benefits produce sizable economic effects

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