A National Perspective of State and Local Pensions

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TMRS Board and Joint Advisory Committee
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Comparison of Retirement Benefits in the U.S.

Private Sector

- 60% of full-time private sector workers participate in an employer-sponsored retirement plan; 21% of part-time workers participate
- In total, 49% of all private sector workers participate in an employer-sponsored retirement plan
- Fewer than one in five have a traditional pension (DB) plan
- Social Security coverage is universal

Public Sector

- Nearly all full-time workers have access to an employer-sponsored retirement benefit; most have access to a traditional pension (DB plan)
- 87% of full-time employees participate in a pension plan, as do 80% of all, including part-time workers; virtually all others are in a DC plan
- Three-fourths participate in Social Security

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Public pensions in the U.S.

- ~$4.33 trillion in assets
- ~14 million active (working) participants
  - 10 percent of the nation's workforce
- 10.3 million retirees and their survivors receive ~$280 billion annually in benefits
- Annual contributions = $192 billion
  - $141 billion from employers; $51 billion from employees
  - Approximately 5.0 percent of all state and local government spending goes to public pensions
- Of 6,000+ public retirement systems, the largest 75 account for 80+ percent of assets and members
- Aggregate funding level = ~72%

US Census Bureau, Public Fund Survey

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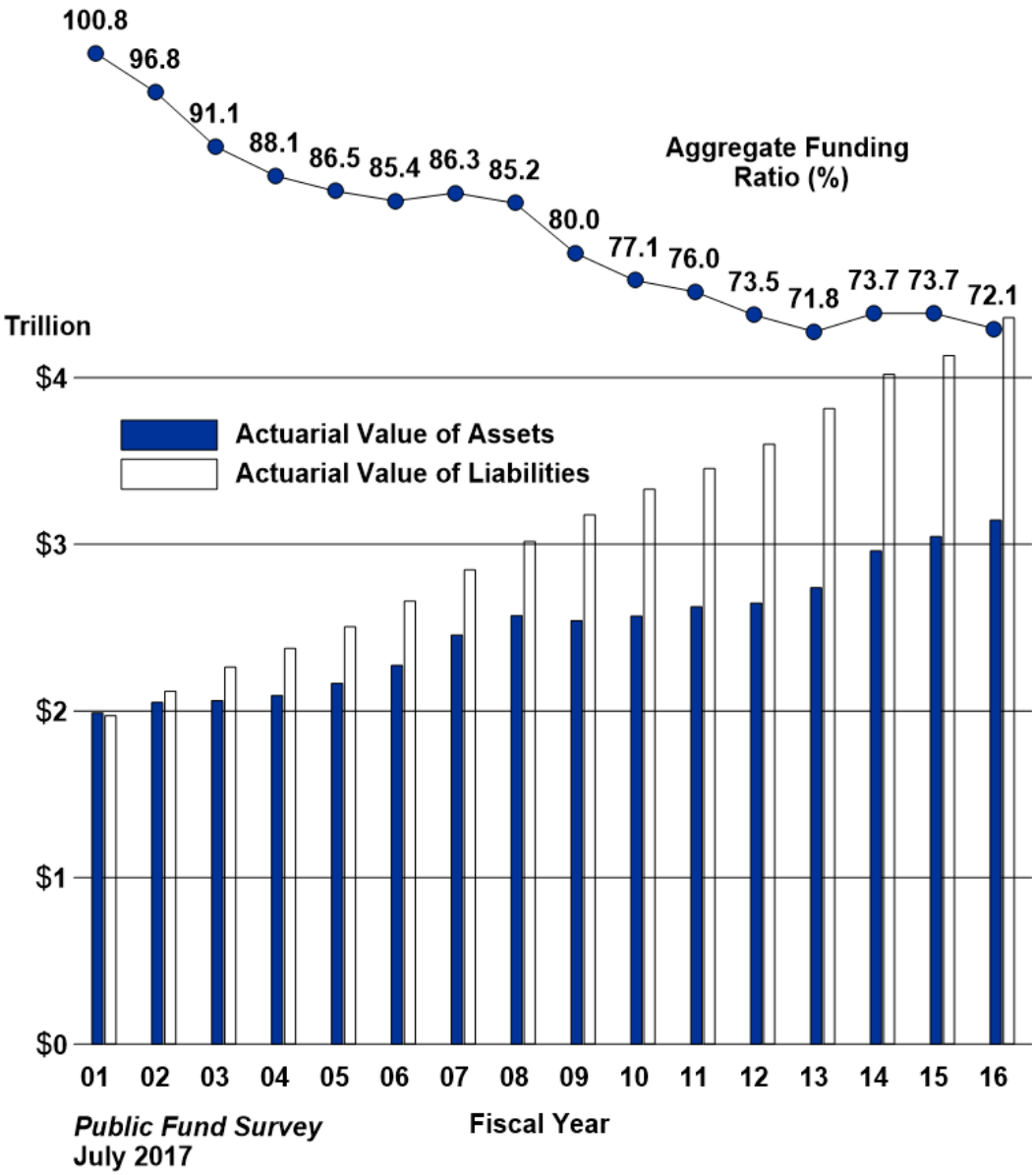

Change in aggregate actuarial funding level and actuarial values of assets and liabilities, FY 01 to FY 16

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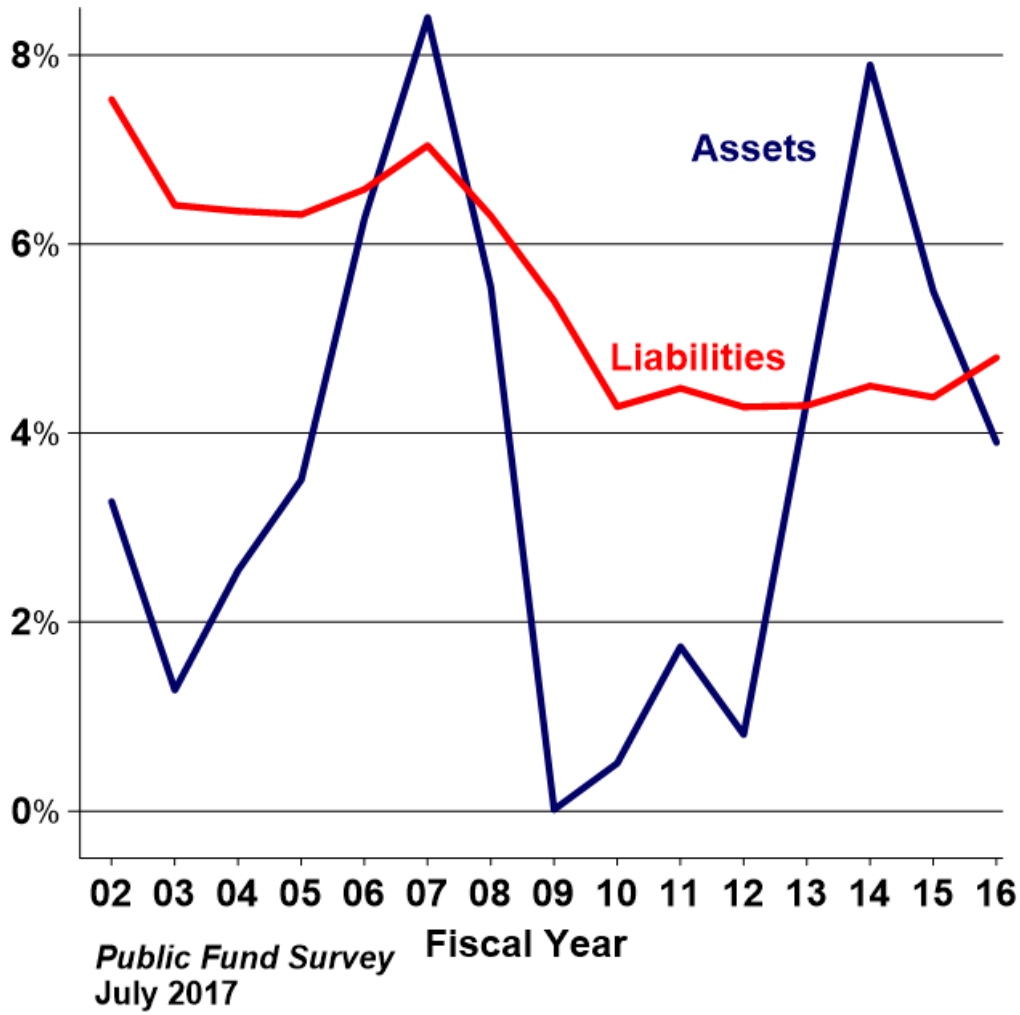

Median change from prior year in actuarial value of assets and liabilities, FY 02 to FY 16

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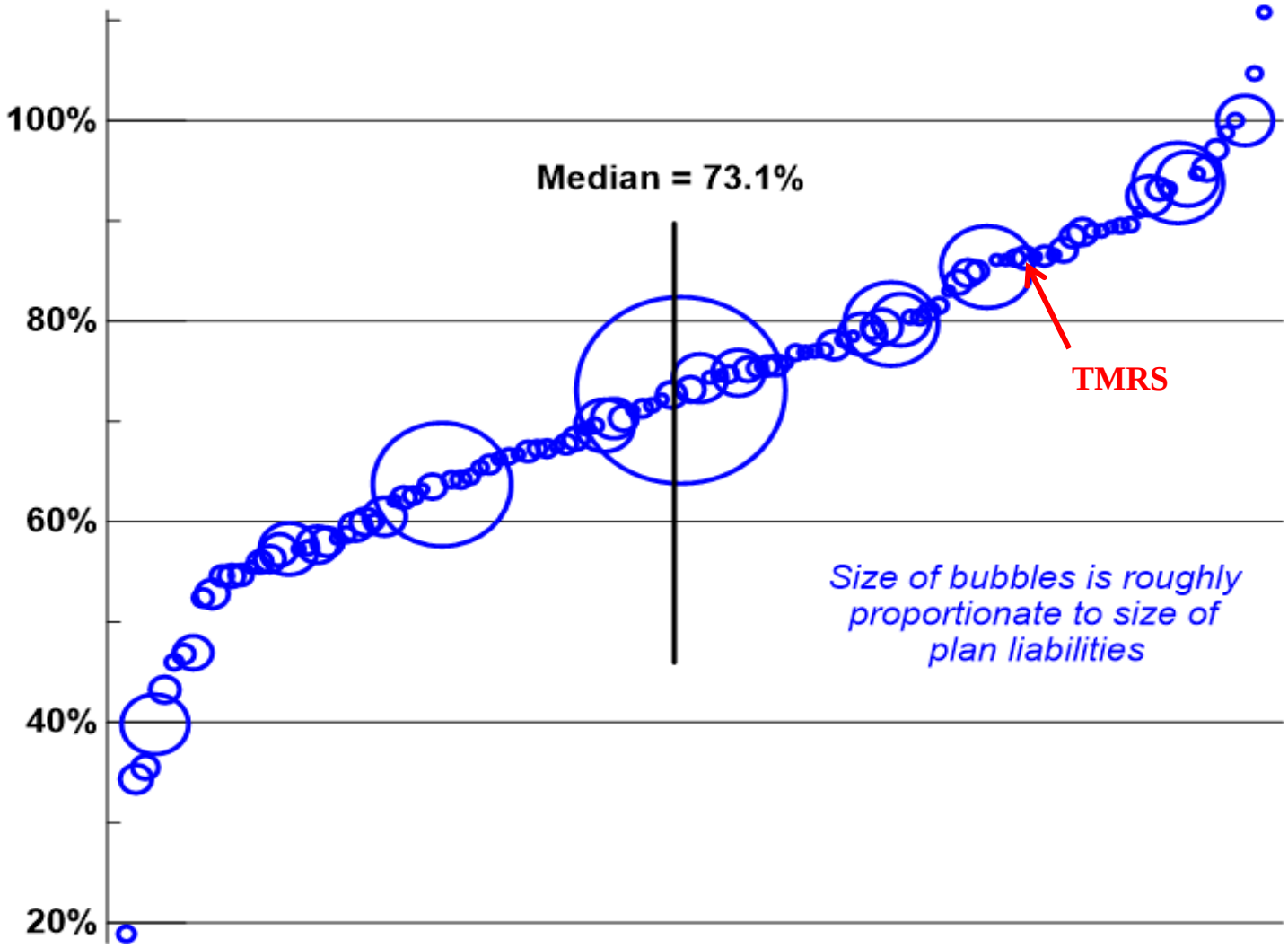
Distribution of public pension funding levels, FY 16



Public Plan Database, Public Fund Survey

Hybrid Plans

- New hybrid plans are being created by legislatures nearly every year
- Mostly DB-DC, some cash balance plans
- Usually apply to new hires only
- DB-DC plans maintain a DB component, with a lower benefit accrual rate
- Cash balance plans contain key features of DB plans, but also transfer some investment risk to workers

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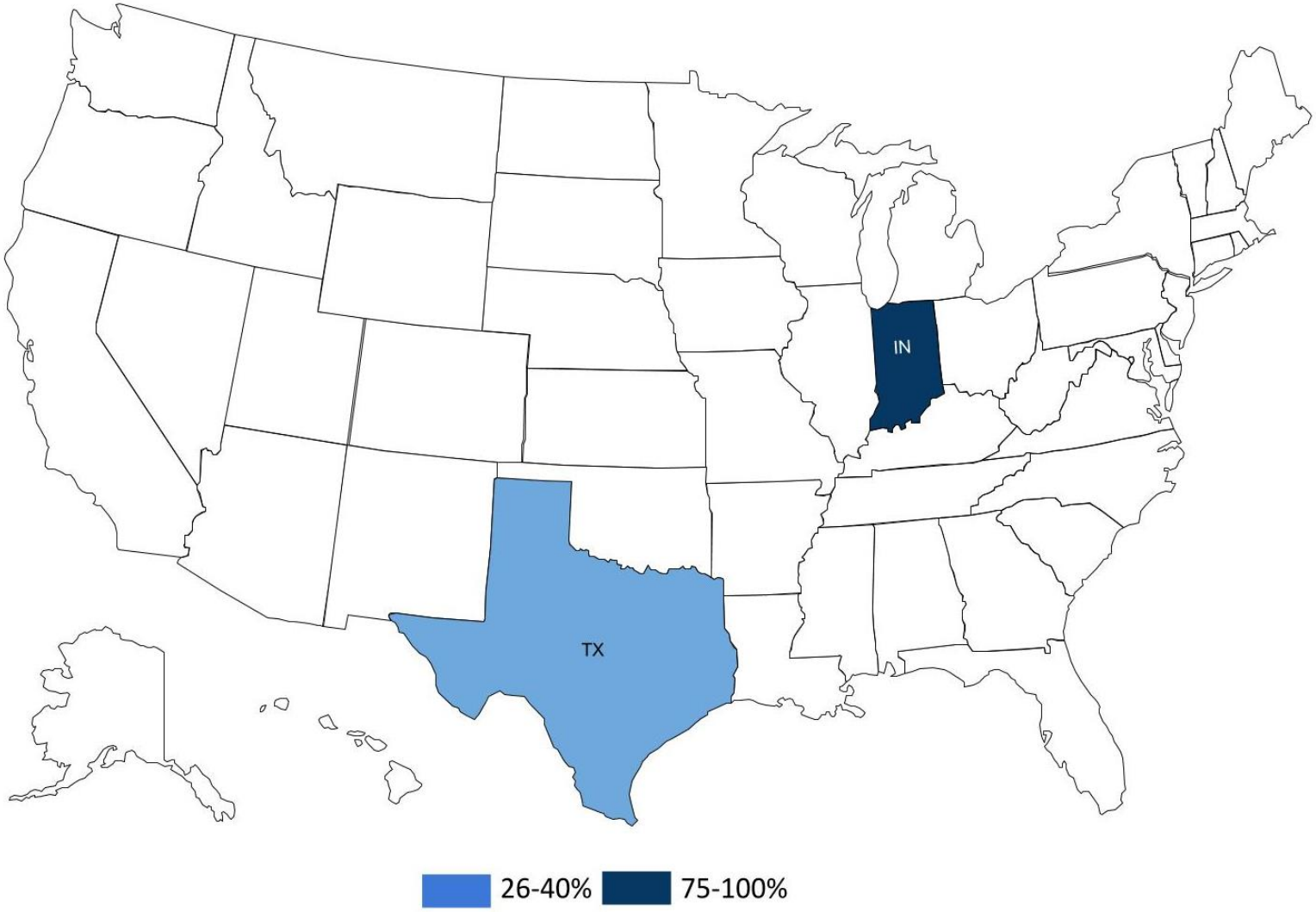
Statewide Hybrid Plans, 1995

(portion of public employees in each state participating)



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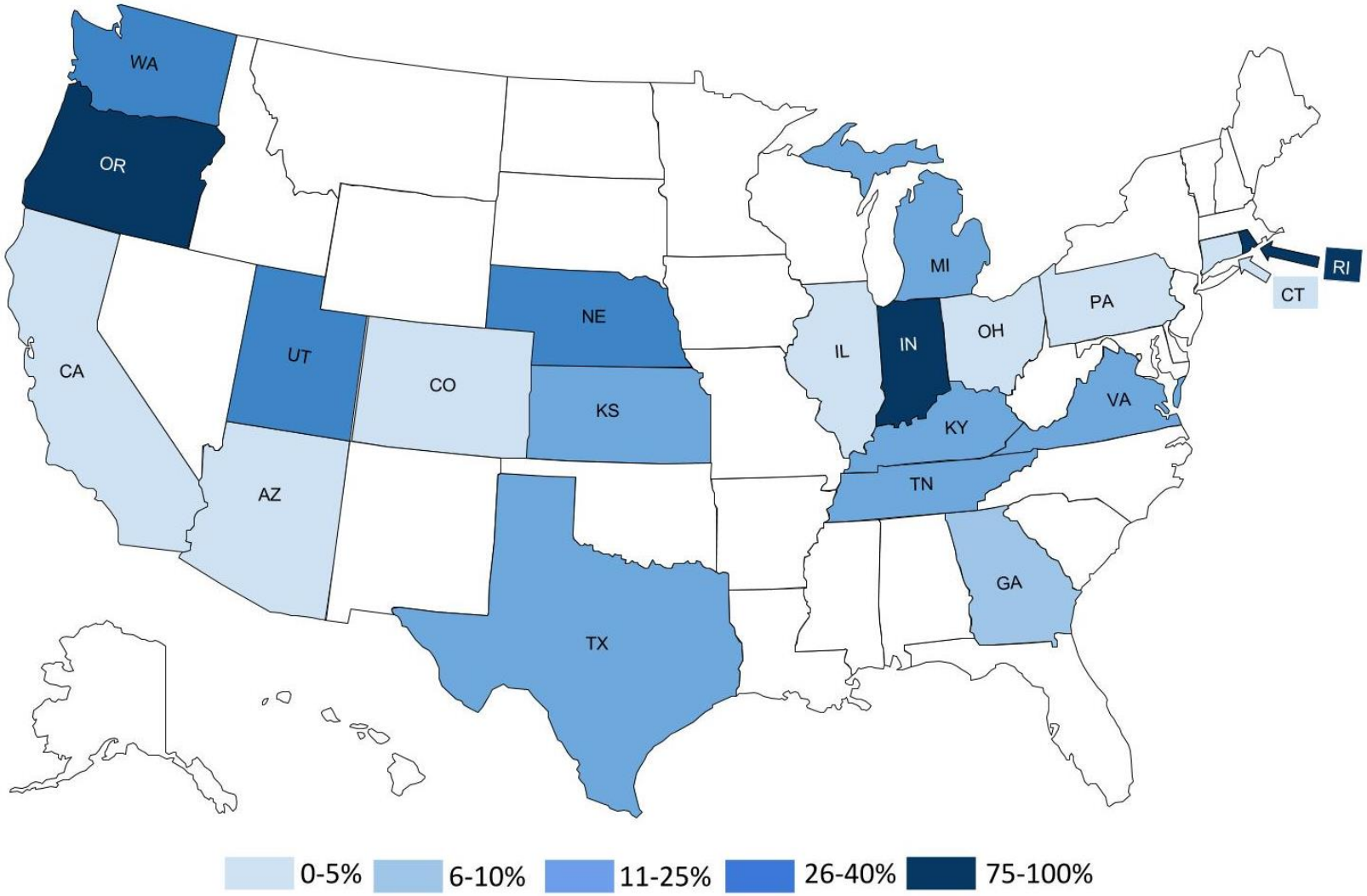
Statewide Hybrid Plans, 2017
(portion of public employees in each state participating)



"State Hybrid Retirement Plans," NASRA 2016

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Defined Contribution Plans

- The number of mandatory and optional DC plans as workers' primary retirement benefit has grown
- Mandatory:
  - District of Columbia for general employees
  - Michigan for state employees hired since 3/1/97
  - Alaska for all hires since 7/1/06
  - Oklahoma for state employees hired since 11/1/15
- Alaska has a DC plan as the primary retirement benefit, combined with non-Social Security participation
- Two states—Nebraska and West Virginia—moved away from DC plans as the primary retirement benefit

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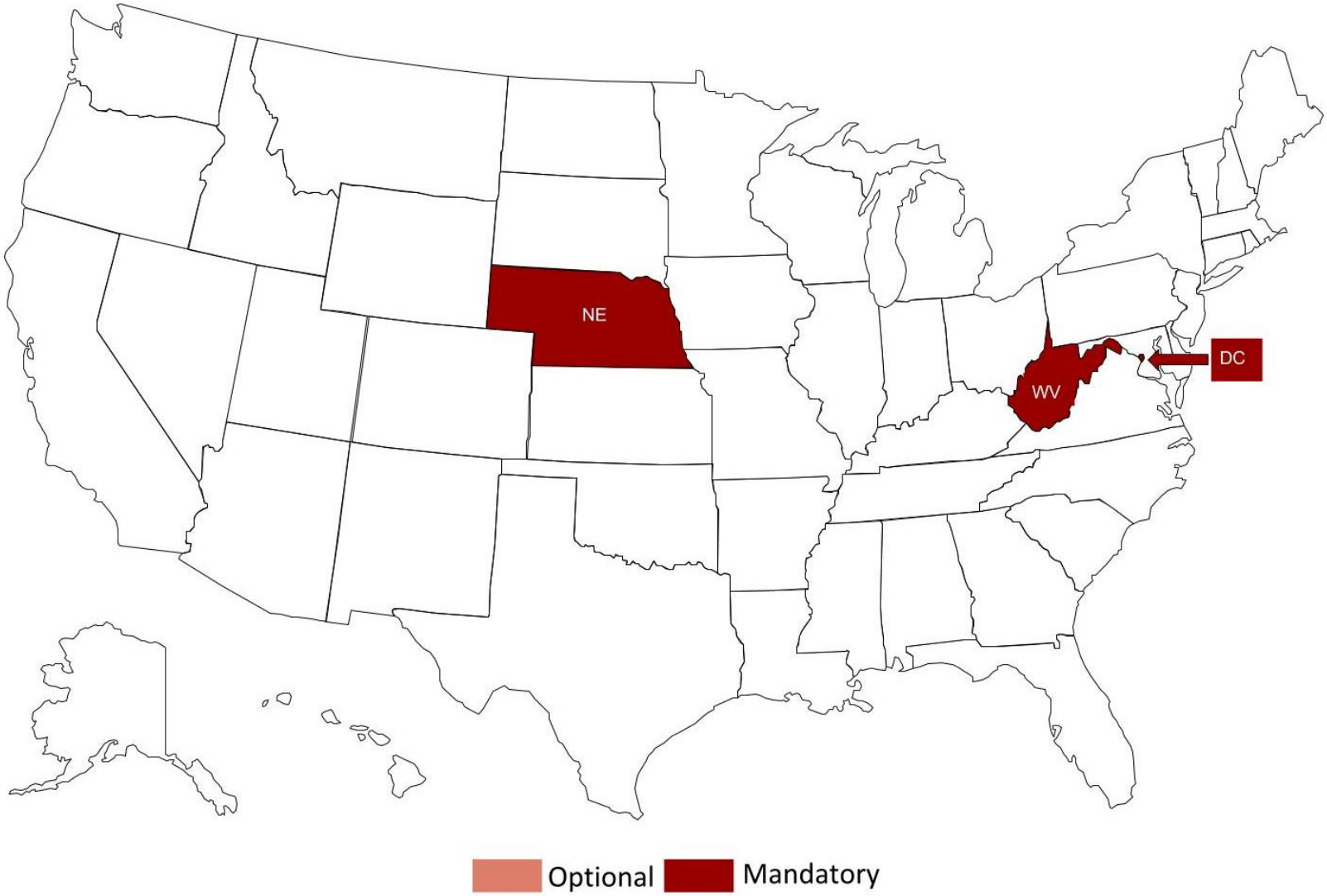
Statewide Defined Contribution Plans, 1995



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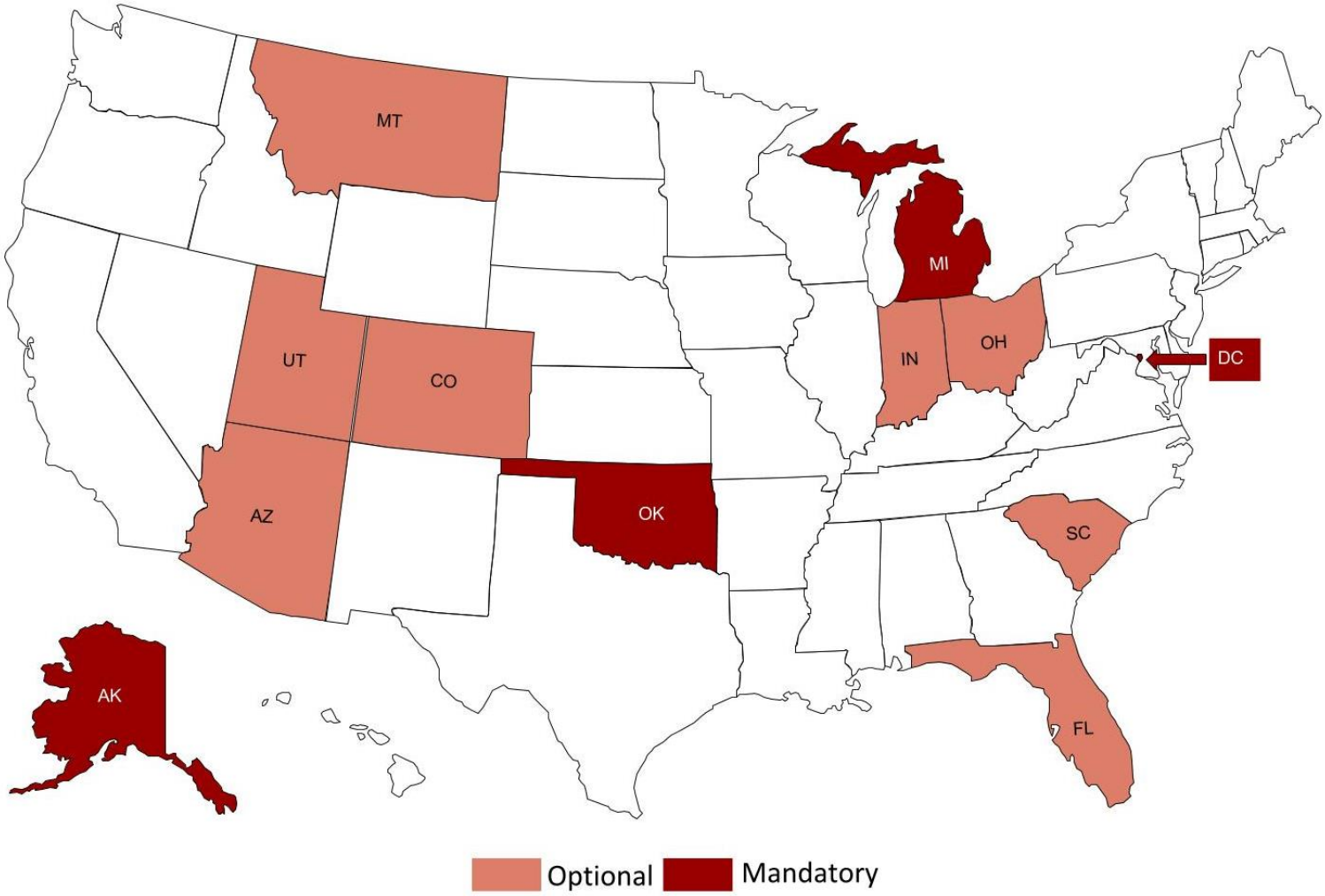
For broad employee groups: teachers, general employees, and public safety personnel

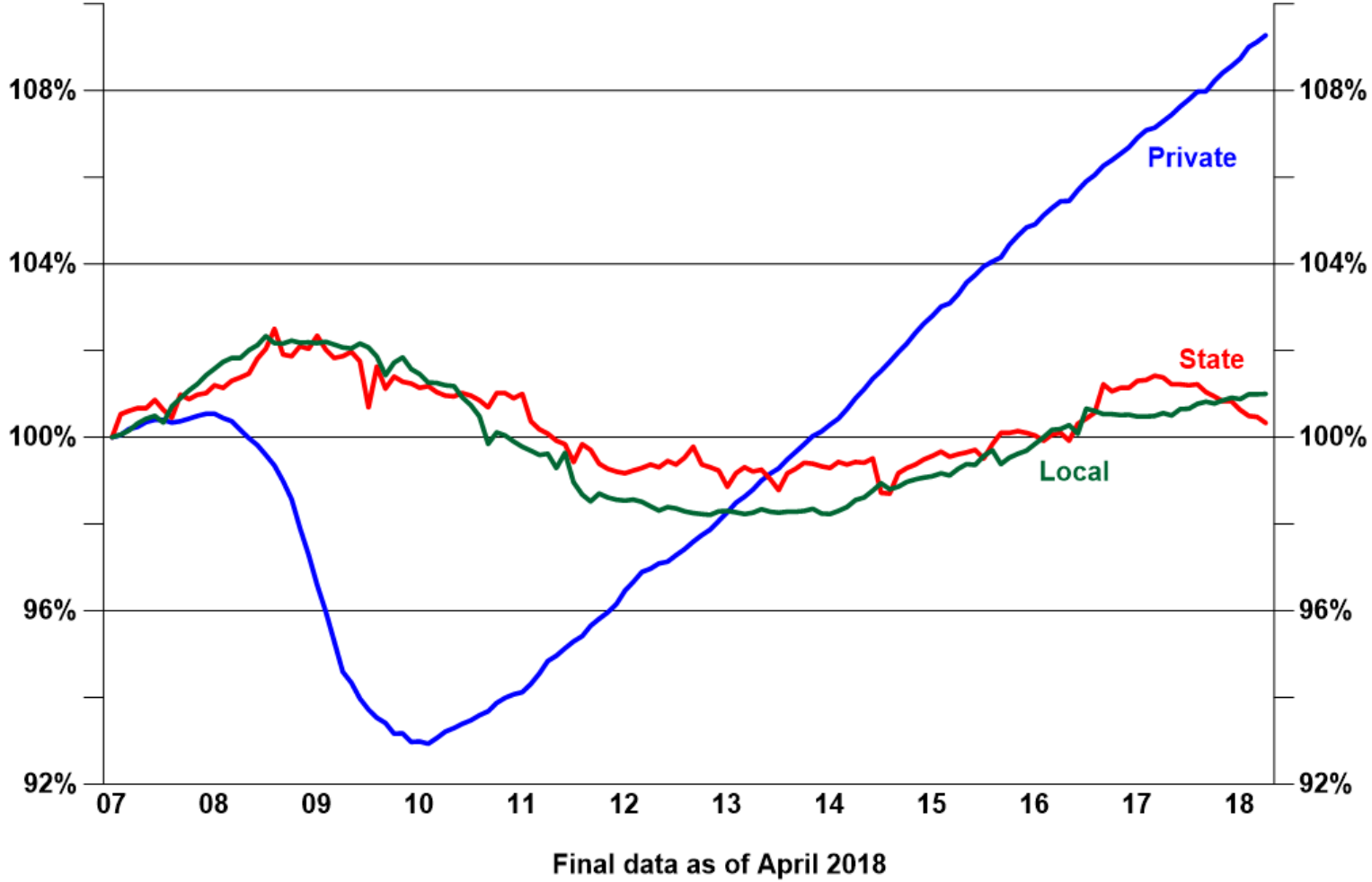
Statewide Defined Contribution Plans, 2017



NASRA

For broad employee groups: teachers, general employees, and public safety personnel

Cumulative change in employment, private sector and state and local government, 2007-present



US Bureau of Labor Statistics

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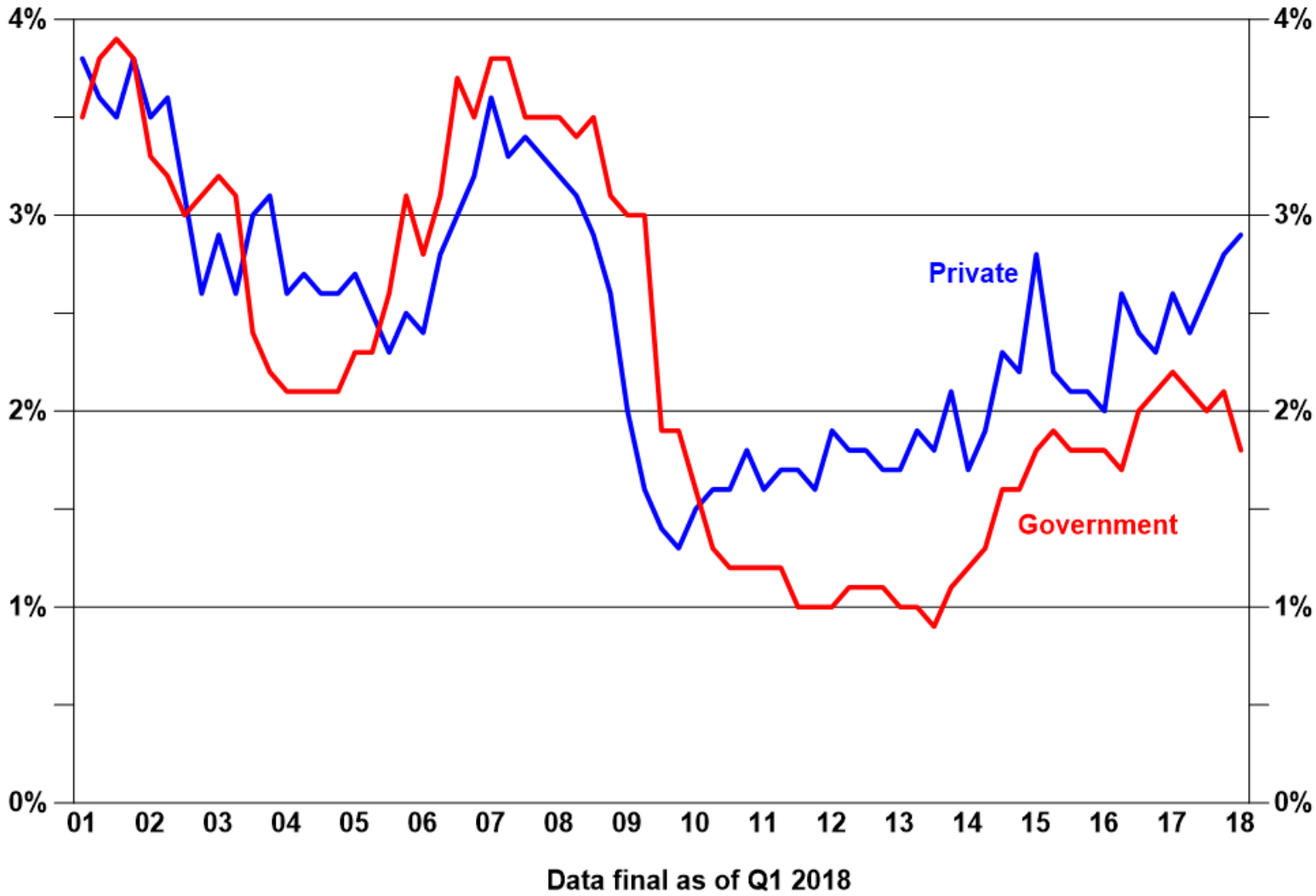
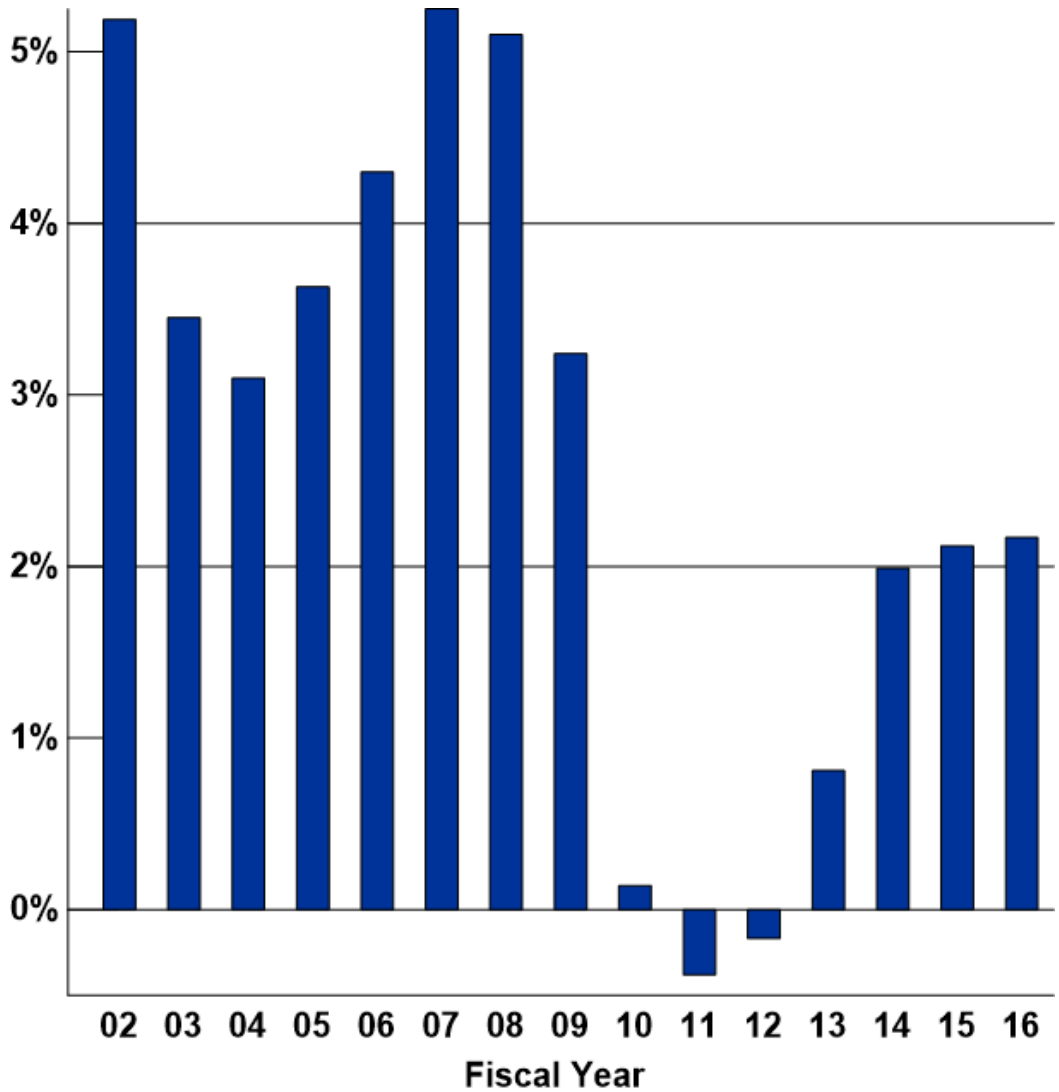
Annualized quarterly change in wage and salary costs for private and state and local government employees, 01-1Q18



US Bureau of Labor Statistics

Median annual change in payroll, FY 02 to FY 16



Public Plan Database, Public Fund Survey

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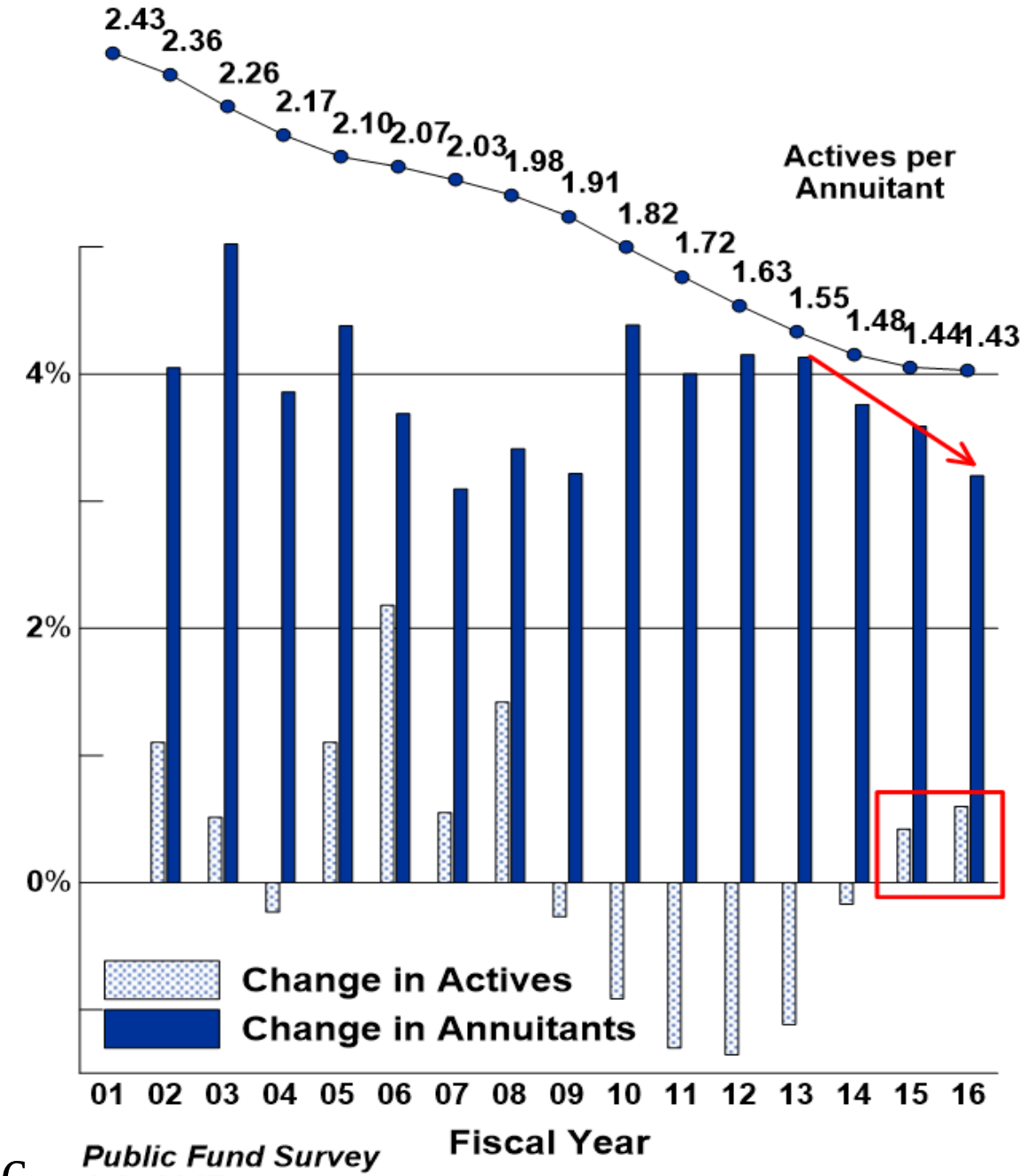

Public Fund Survey
July 2017

Median change in number of actives and annuitants, FY 01 to FY 16

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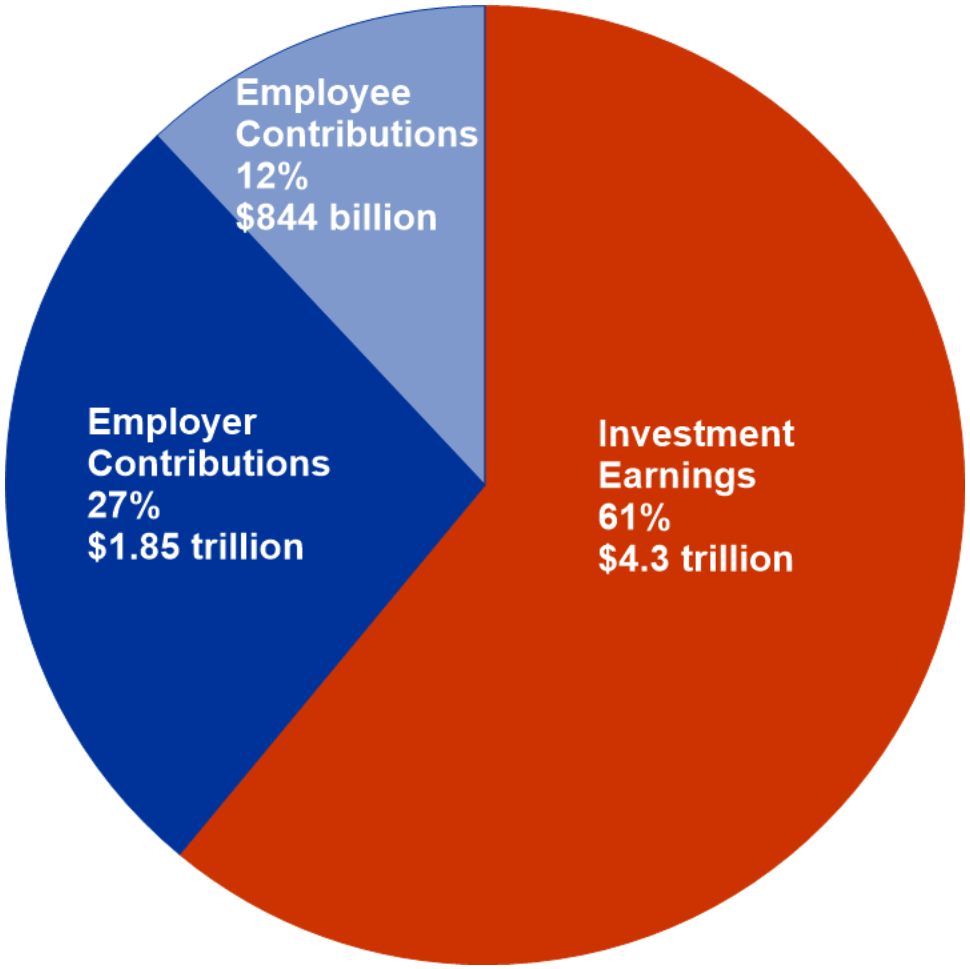

Sources of public pension revenue, 1987-2016

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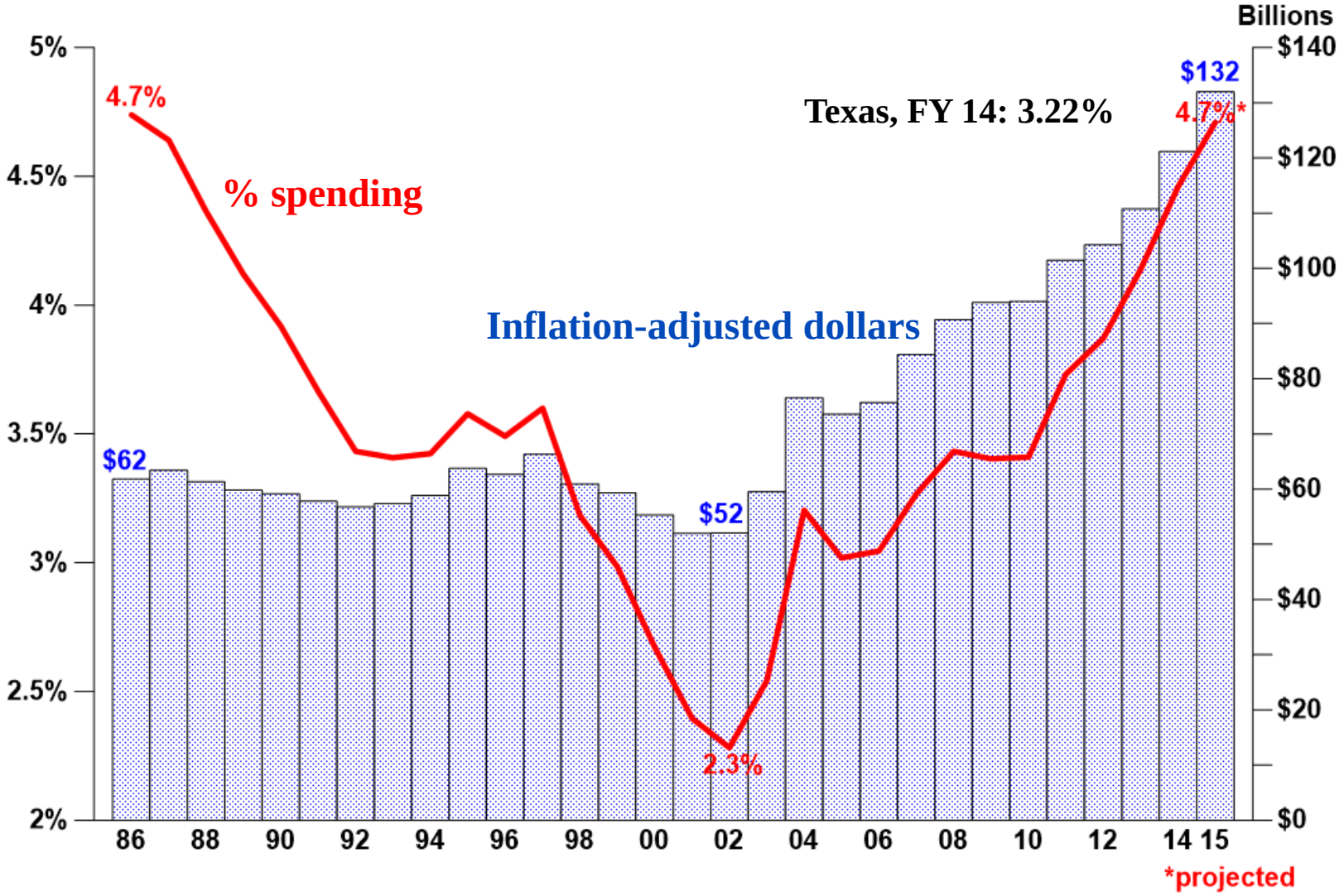
Taxpayer spending on pensions

- Spending varies widely among states
- Pension benefit levels affect the spending number
- Social Security participation is an important factor
- Not all states contribute as much as they should
- Spending is higher for cities than for states
  - A larger portion of city budgets is spent on personnel
  - A larger percentage of municipal employees serve as public safety officers, whose retirement benefits are more expensive due to shorter careers

Employer (taxpayer) spending on public pensions, 1986 to 2015



"State and Local Government Spending on Public Employee Retirement Systems," NASRA 2016

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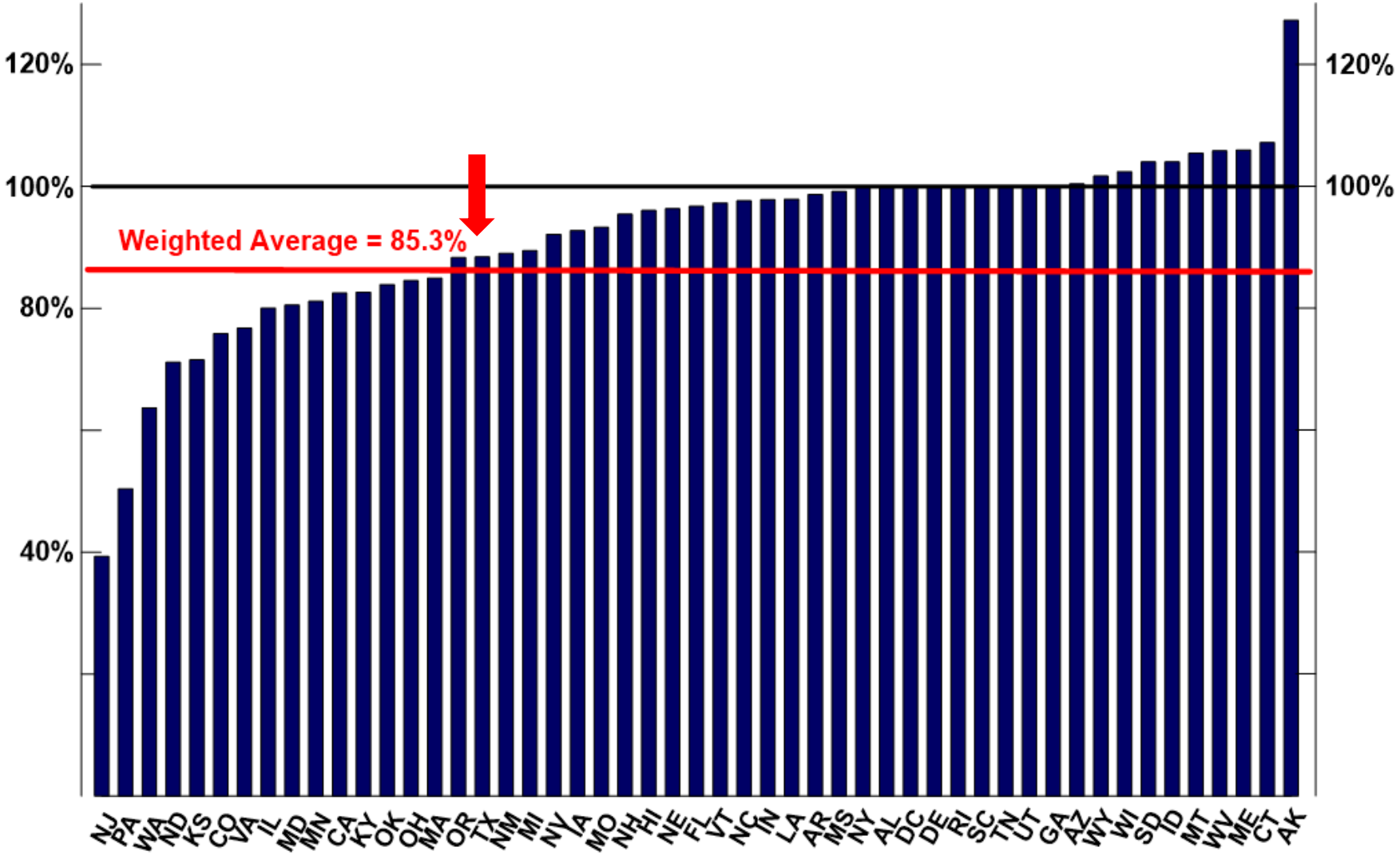
Weighted Average ARC/ADC Paid by State FY 01 to FY 15



"State and Local Government Contributions to Statewide Pension Plans: FY 15," NASRA 2017

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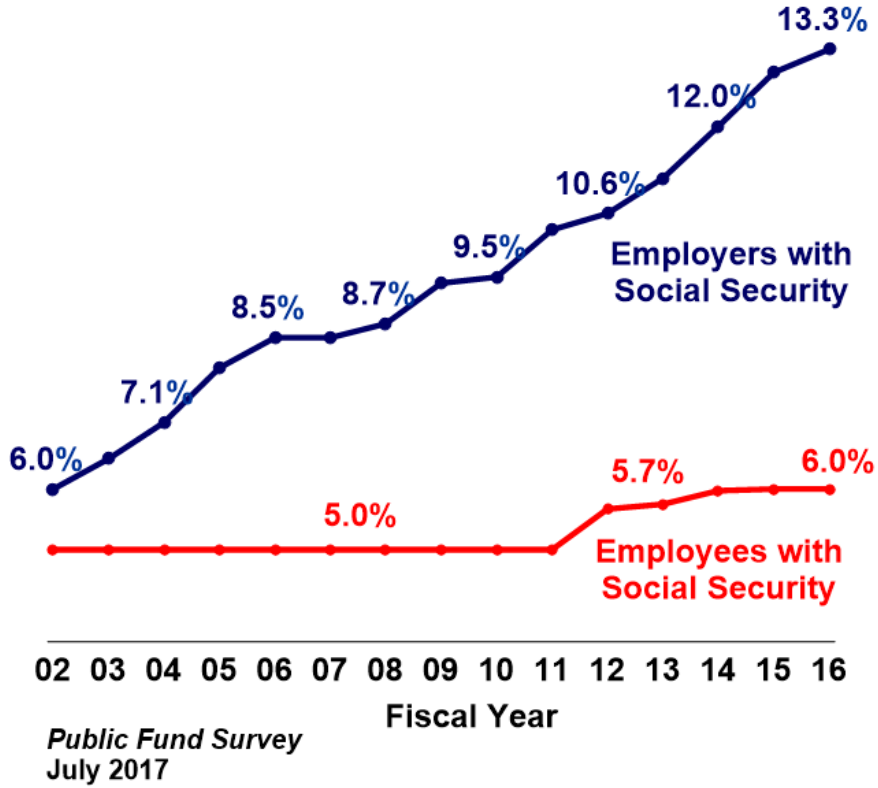
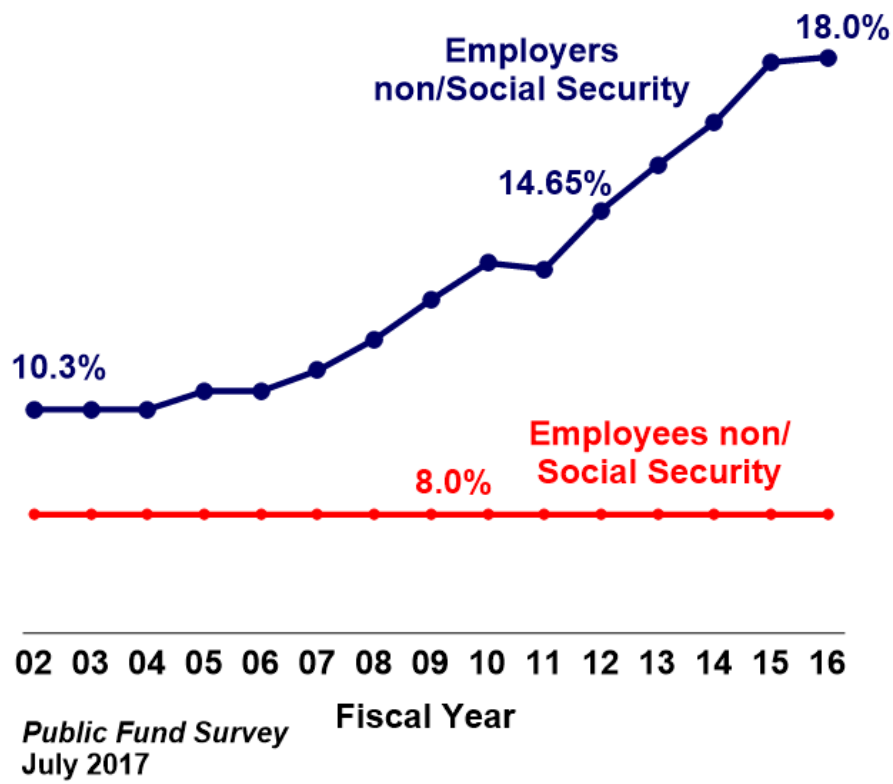
Median contribution rates, Social Security eligible and ineligible





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Methods states are using to amortize unfunded pension liabilities

- Pay the actuarially determined contribution
- Commit a portion of the budget surplus to the unfunded liability, either ad hoc or in statute (AK, HI, RI)
- Issue pension obligation bonds
- Establish a dedicated funding stream, such as revenue from tobacco, liquor, gambling, or severance taxes (KS, MT, OK)
- Dedicate a portion of sales, use, and/or corporate income tax revenues (OK)
- Reduce the funding amortization period/change the method
- Transfer ownership of the state lottery to the pension fund (NJ)
- Funding Policies@NASRA.org http://www.nasra.org/funding

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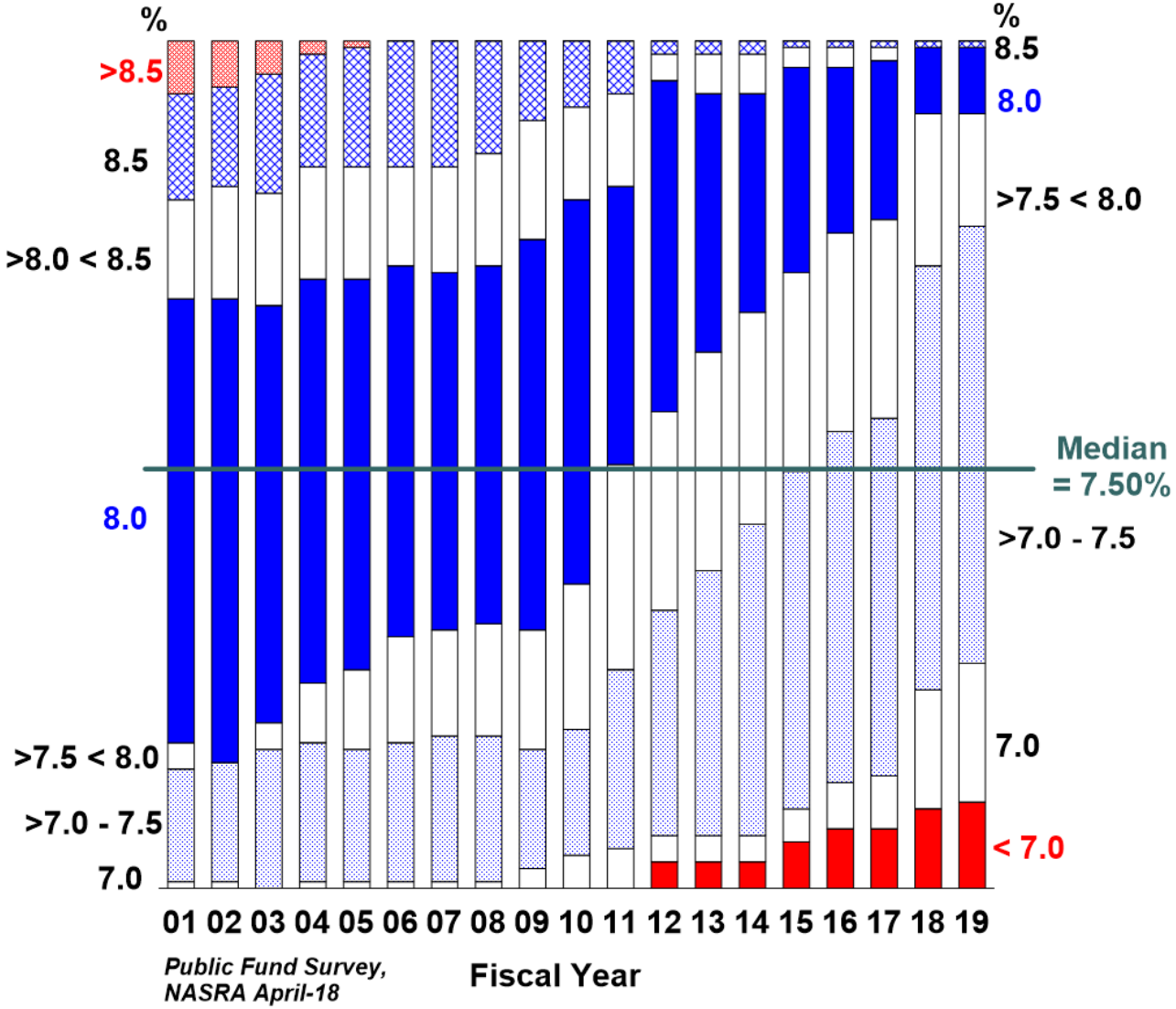

Change in distribution of nominal investment return assumptions, FY 01 to FY 18

TMRS: 6.75%

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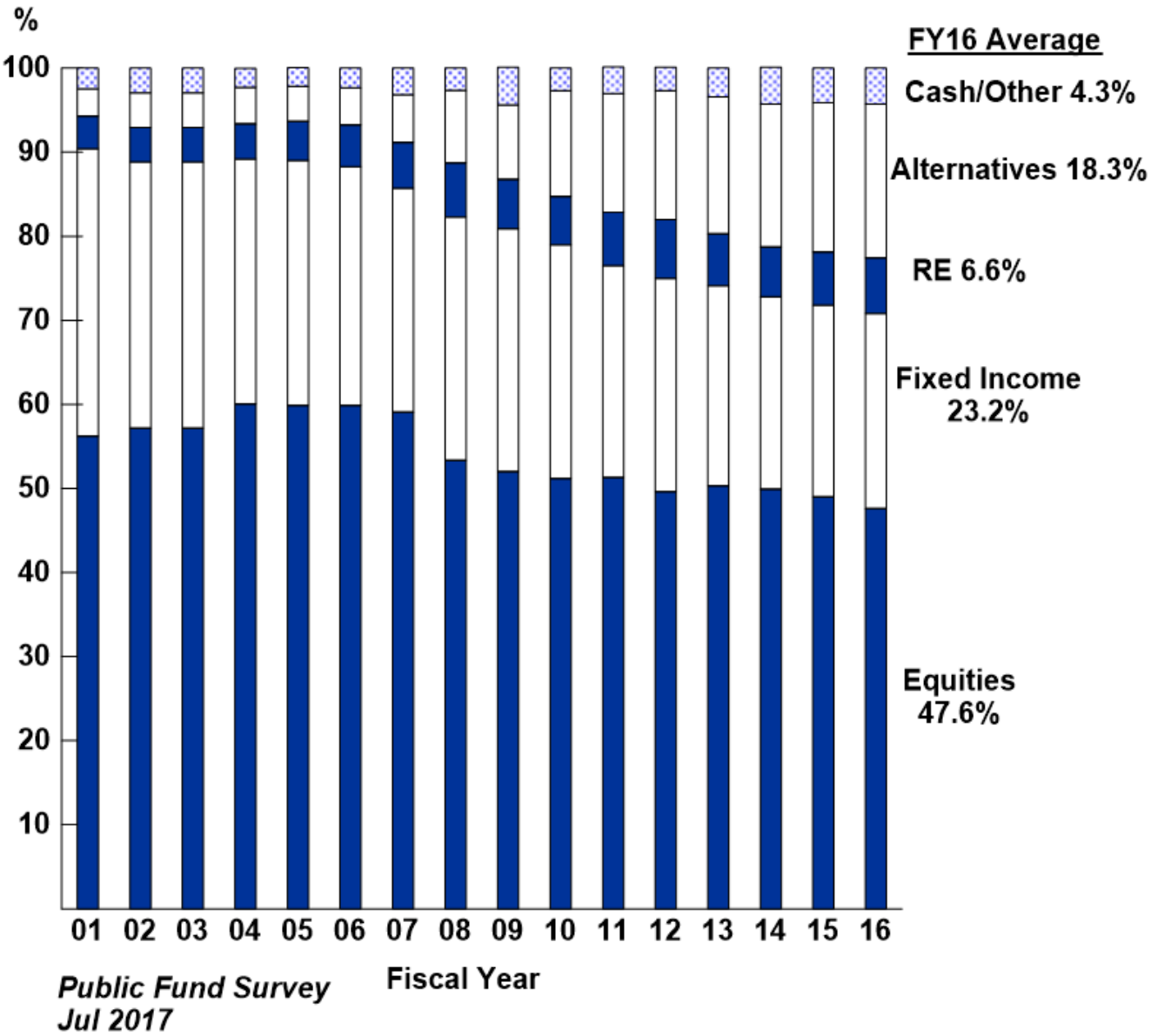
Change in average public pension fund asset allocation, FY 01 to FY 16



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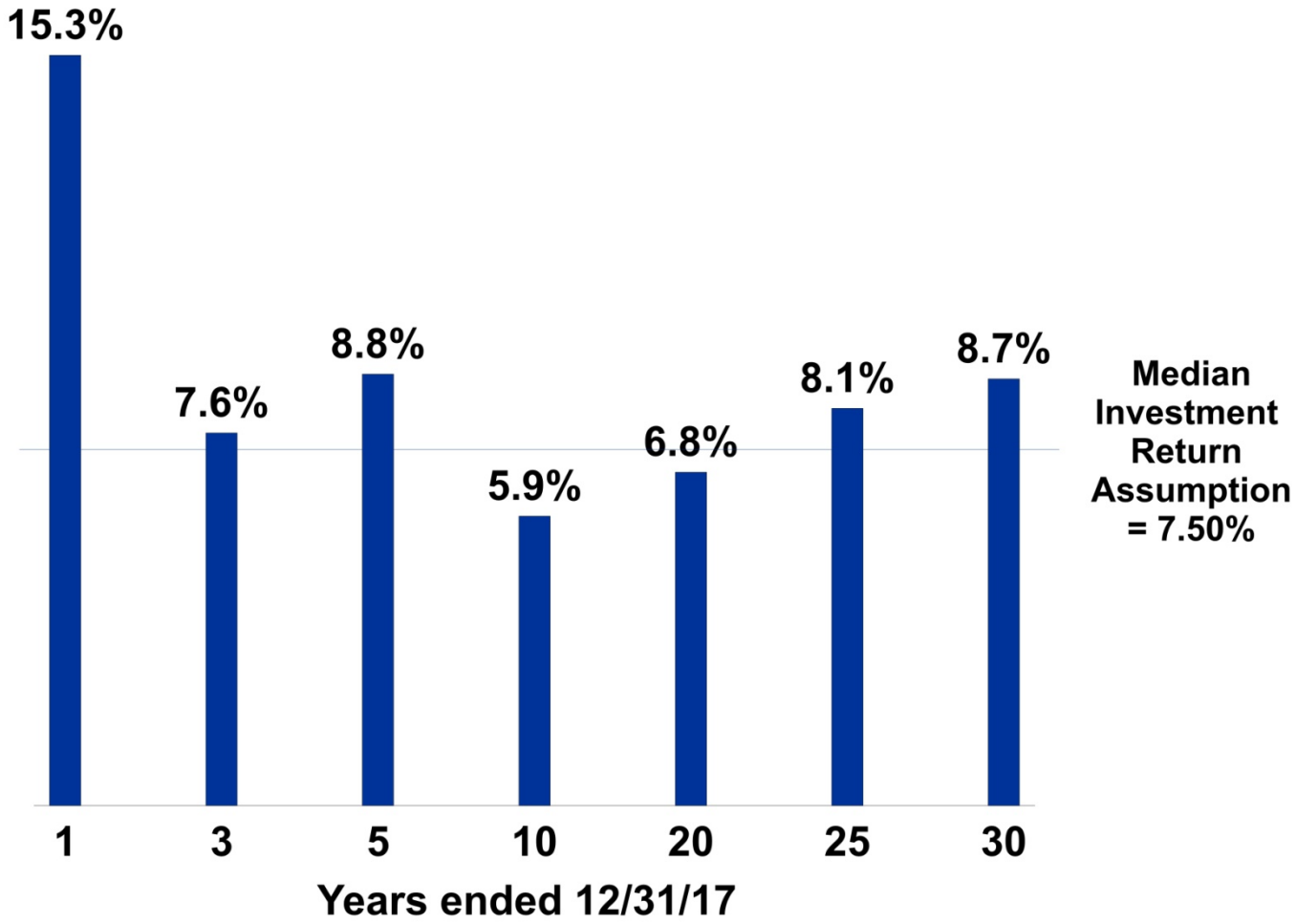
Median annualized public pension fund returns for periods ended 12/31/17



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Pension challenges facing state and local government

- For some states and cities, adequately funding their pension will be a challenge, especially for those with large unfunded liabilities
- Funding challenges are exacerbated by
  - low interest rates
  - declining projected returns
  - improving mortality
  - maturing population
- Providing a retirement benefit that aligns with key stakeholder objectives

Pension challenges facing state and local governments, continued

- Understanding and responding appropriately to multiple pension measures (books, budgets, and bonds):
  - Books: GASB statements provide standardized financial reporting
  - Budgets: Actuarial funding calculations identify the amount needed to fund the benefit
  - Bonds: Bond rating agencies assess the degree to which pension obligations affect a government's ability to repay bonded debt

Update on Texas Pensions

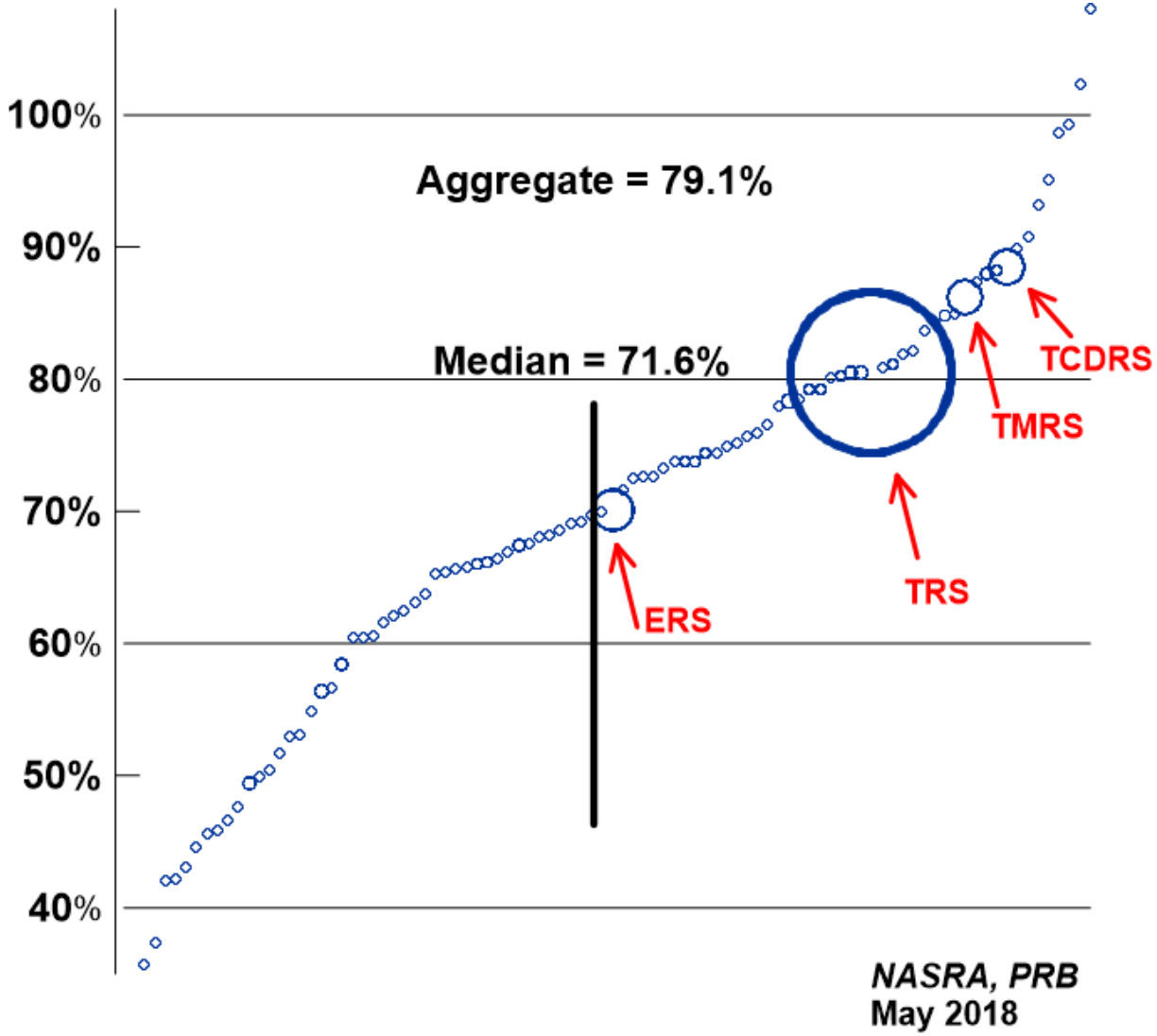
- Virtually all public employees in Texas participate in a pension plan, including the cash balance plans administered by TMRS and TCDRS
- Texas pensions are a microcosm of the US: a small number of large retirement systems comprise the vast majority of assets and participants
- A large number of small retirement systems
- Funding conditions run a wide range
- Texas is unusual in having an entity like the Pension Review Board statutorily responsible for reviewing public plans
- Dallas and Houston plan funding challenges were addressed last year by the Legislature

Public pensions in Texas

- ~ $240 billion in assets
- ~ 1.35 million active (working) participants
- ~ 680,000 retirees and their survivors receive around $15.9 billion annually in benefits
- Annual contributions = $11.3 billion
  - $6.5 billion from employers; $4.8 billion from employees
- ~93 public retirement systems
- TRS, ERS, TMRS, and TCDRS account for more than 90 percent of all assets and participants
- TRS alone accounts for more than one-half

US Census Bureau, 2016

Public pension funding levels and Texas statewide plans, FY 16



Size of bubbles is roughly proportionate to size of plan liabilities

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Legislation Affecting the Dallas Police & Fire Plan

- The plan was in distress as a result of poor investment returns and an unsustainable DROP plan design
- Reforms increased employee contribution requirements, from 8.5% to 13.5%
- Increased employer contribution rates from 27.5% to 34.5%, plus $13 million annually until 2024
- Suspended COLA until funding level reaches 70%, when board may consider paying a COLA
- Capped max COLA at 4%

Legislation Affecting the Dallas Police & Fire Plan

- Increased normal retirement age to 58 from 50 or 55, depending on hire date
- Beginning 9/1/17, increased early retirement age, for those hired on or after 3/1/11, from 45 to 53
- Prohibits future benefits increases unless funding level is below 25 years
- Reduced DROP interest crediting rate
- Required annuitization of DROP assets rather than allowing lump sum access

Legislation Affecting Houston Plans

- Three municipal plans, for police, firefighters, and general employees, had relatively large unfunded liabilities and associated costs
- Legislature approved a corridor cost management system that increases or reduces employer and employee contributions based on changes in the plans' funding level
- Shared sacrifice: higher contributions for employees and employers
- Lower COLAs
- Lower DROP provisions

Legislation Affecting Houston Plans

- Houston voters approved a $1 billion pension obligation bond late in 2017, as part of the agreement.
- Proceeds were used to reduce plans' unfunded liability
- Established a new cash balance plan for new general employee hires beginning this year
- Established triggers to switch plans to cash balance in case the plan funding level falls below a designated level

Pension Review Board Update

- PRB statutes direct the board to "conduct intensive studies of potential or existing problems that threaten the actuarial soundness of or inhibit an equitable distribution of benefits in one or more public retirement systems."
- The PRB has been focusing on plans whose actuarial measures suggest the plans may face potential or existing problems that threaten actuarial soundness
- The PRB currently is conducting two studies:
  - Funding policies for fixed-rate plans
  - Feasibility of merging assets of smaller public pension funds
- Results will be conveyed to the legislature prior to convening next January