Public Pension Landscape and Trends

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Presentation Summary

• Broad overview of the public pension community in the US and Texas
• Public pension funding issues and challenges
• Public pension reform and risk sharing
• Risk assessment
• Texas pension legislation, 2019
Public Pensions in Texas

- $280 billion in assets
- 1.34 million active (working) participants
- 700,000+ retirees and their survivors receive $17 billion in benefits annually
- Annual contributions = $11.8 billion
  - $5.3 billion from employees
  - $6.5 billion from employers
- Approximately 95 systems in the state
- TRS alone accounts for more than half of the assets and participants
- TRS, ERS, TCDRS, TMRS account for 90+
- Aggregate funding level = ~78%

U.S. Census Bureau, Pension Review Board, Public Fund Survey
Change in Aggregate Public Pension and TMRS Funding Levels, FY 01 to FY 17

Public Fund Survey
Nov-18
Distribution of Public Pension Funding Levels, FY 17

Median = 72.9%

Size of bubbles is roughly proportionate to size of plan liabilities
Headwinds Facing Public Pension Plans

• Higher costs resulting from
  – Declining investment return assumptions
  – Slow payroll growth, which is a result of
    • Sluggish hiring and
    • Tepid salary growth
  – Updated mortality assumptions to reflect longer life expectations

• Increasing plan maturity
Change in Distribution of Investment Return Assumptions, FY 01 to present

TMRS = 6.75%

Public Fund Survey, NASRA Feb-19

Fiscal Year
Change in Average Public Pension Plan and TMRS Investment Return Assumptions, FY 01 to present

- Average: 7.27%
- TMRS: 6.75%

Fiscal Year: 01 03 05 07 09 11 13 15 17 19
Relative Change in Private and State and Local Employment, 07-19

Data final as of April 2019

U.S. Bureau of Labor Statistics
Number of Active Members per Annuitant, FY 01 to FY 17

Fiscal Year

Number of Active Members:
- TMRS
- Public Pension Aggregate

Values:
- FY 01: TMRS = 4.09, Public Pension Aggregate = 2.43
- FY 17: TMRS = 1.76, Public Pension Aggregate = 1.38
Annualized Quarterly Change in Wage and Salary Costs for Private and State and Local Workers, 01-19

Data final as of Q1 2019

U.S. Bureau of Labor Statistics
Median Annual Change in Payrolls
FY 02 to FY 17

Public Fund Survey
Nov-18
External Cash Flow, Median Public Pension and TMRS, FY 01 to FY 17
Tailwinds Supporting Public Pension Plans

• Stabilizing investment returns?
• Stronger employer efforts to pay contributions
• More aggressive liability amortization strategies
  – More closed amortization periods
  – Shorter amortization periods
• Lower benefit levels = lower long term costs
• Stronger hiring and salary growth
Where Will Public Pension Funding Conditions Go From Here?

• Many plans continue to struggle with key actuarial challenges
  – Lower investment return assumptions still to be incorporated
  – Sub-par investment returns, particularly in 2015 and 2016, yet to be fully incorporated
  – Rates of public sector hiring and salary growth remain below historic norms
  – Some employers are still not contributing the full ADC

• The size of the challenge varies widely
  – Some plans have relatively small UALs and affordable costs
  – Other plans have UALs that are quite large and burdensome
• Since the 2008-09 market decline and recession, states and other public pension plan sponsors have implemented an unprecedented series of reforms to their pension plans
• Unprecedented both in the number of states where reforms were made and in their magnitude
• A major theme of reforms has been the establishment of risk-sharing plan design features
• Also, lower benefit levels and higher employee contributions
• More dedicated funding sources
In-depth: Risk Sharing in Public Retirement Plans
States Adding Shared-Risk Plan Designs Since 2000
Examples of Risk-Sharing

• Hybrid retirement plans
  – DB-DC
  – Cash balance
• Contingent or limited cost-of-living adjustments
• Flexible employee contribution rates
• Adjustable benefit levels
Statewide Hybrid Plans, and Percentage of Public Employees Participating, 1995

[Map showing state participation in hybrid plans with Texas and Indiana highlighted.

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- 26-40%
- 75-100%]
Flexible Employee Contribution Rates

• Employees and employers split the cost of the retirement benefit at the Arizona State Retirement System and the Nevada PERS

• Most new hires in California since 1/1/13 are required to pay at least one-half of the normal cost of the plan

• Iowa statute requires employees participating in the PERS to pay 40 percent of the cost of the plan

• Public employees in Utah must pay the cost of their pension plan above 10 percent

• There are other examples
Flexible Benefit Levels

• Retirement benefits for public employees in New Brunswick (Canada) and Houston, Texas are tied to their plans’ actuarial and investment experience.

• The New Brunswick plan design features “base” and ancillary benefits. Base benefits are nearly certain to be paid; ancillary benefits may adjust during an employee’s working career depending on investment and actuarial experience.
Flexible Benefit Levels

• The Houston plans feature a contribution rate corridor arrangement. A rise or fall in the employer contribution rate of five percent triggers changes, including a change in:
  – actuarial methods and assumptions
  – employee contributions
  – COLA
  – normal retirement age
Another Public Pension Trend: Risk Assessment

• Following federal requirements that large banks conduct periodic stress tests, calls are growing for public pensions to undergo risk assessments
• Most larger plans already conduct periodic risk assessments in some form, such as through an asset-liability study
• ASOP 51 requires all actuarial valuations and related analyses to include a risk assessment
• A stress test is a form of risk assessment that measures the effect on the plan of various projected—particularly adverse—investment and actuarial events
• Sensitivity testing—another form of risk assessment—examines the effect on the plan of different actuarial assumptions and methods
Texas Pension Legislation, 2019

• Investment Performance Evaluation (SB 322)
  – Requires public retirement systems to report information about the system’s investments to the Pension Review Board, including fees and commissions, asset managers, investment practices and performance, etc.

• Funding Policy (SB 2224)
  – Requires every public retirement system in the state to publish a funding policy
Thank you

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