Federal Legislative and Regulatory Update

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NASRA Director of Federal Relations

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About NASRA

• NASRA Members are the directors of the nation’s largest state/statewide public retirement systems
  – Administer benefits for approximately 15 million working and 8 million retired employees of U.S. states and local governments
  – Hold more than 2/3 of the $3.7 trillion held in public pension trusts
The 114th Congress
2014 House Election Results

Democratic
Net -12, Gained 3, Lost 15

218 of 435 Seats Needed for Majority
Current House: 189 (D); 233 (R); 3 Vacancies

Republican
Net +12, Gained 15, Lost 3

Source: Politico.com
Governor’s Party Following 2014 Elections
Post-Election Breakdown of State Legislatures & Governors

Source: National Conference of State Legislatures
To Know Your Future You Must Know Your Past
Growing National Interest in Public Pensions

• Congressional Hearings
• Federal Reports
• National Taskforces, Panels and Studies
• Federal Legislation
• Federal Regulatory Interest
Numerous Federal Hearings

- Public pensions implicated in each as "largest driver of state and local fiscal problems"
Deluge of Federal Reports
Barrage of National Taskforces, Panels and Studies

Creating a New Public Pension System

Introduction

State and local budgets across the nation are facing enormous distress. Although part of this handicap can be attributed to the worldwide financial crisis and the recession that followed, a significant portion has been caused by widespread, unsound budgetary practices. By and large, the financial crisis merely uncovered deep, veiled structural flaws. Chief among these flaws is the perpetual underfunding of public employee benefits. Failing to address the public pension crisis promptly would be economically catastrophic, triggering bankruptcies of cities, school systems and potentially even entire state governments.

The states’ own estimates of the unfunded liability due to their retirement benefit promises grew to $1.26 trillion in fiscal year 2009, up from $1 trillion just one year earlier.1 Pension promises make up over half ($660 billion) costs of this crisis are potentially crippling to our nation. Figure 1 highlights the unfunded liability per household in selected jurisdictions. As shown above, the average family living in Chicago today is burdened with $34,559 in liability due to underfunding at the state level and an additional $31,066 in the municipal level for a cumulative burden of $65,625. More than one in four families in Illinois are currently carrying such heavy debt.2 There are already over 50,000 public employees who have had their pension annuities cut, and there are over 1 million public employees who face substantial cuts and other (often hidden) changes to their retirement benefits.3

Violent change requires good information, thoughtful debate, and difficult choices.

The most important task facing states and cities is to pay down their existing pension debt in order to keep the promises already made to retirees and workers. This will require years of fiscal discipline and may involve raising revenue, cutting spending, or asking employees to contribute more. Some stakeholders will want to solve the pension shortfall only with tax increases. Others will want to solve it only with spending cuts. Each state and city will address the issue differently and we know there is no one-size-fits-all solution.

Policymakers also need to ensure that they have a sustainable retirement system for the future. This can involve keeping the existing retirement plan but doing a better job at funding it; or, it can involve looking at questions of plan design. States and cities will need to find their own solutions that will help protect against future funding crises.

Why are you partnering with the Laura and John Arnold Foundation?

We share the goal to help states design and adopt retirement systems that are fair, affordable and fiscally sustainable—while at the same time preserving governments’ ability to recruit and retain a talented public-sector workforce. We realize there is no one-size-fits-all solution so we offer policymakers information that can help them offer retirement security to public workers, protect taxpayers and maintain the state’s ability to deliver important public services.

By Joan B. McCoo, Ph.D.
Vice President for Public Accountability Initiatives

Figure 1: Unfunded Liability per Household


Notes: All figures are for fiscal year 2009. The median unfunded liability for all 50 states is $57.7 billion.


Objectives and Principles for Funding Public Sector Pension Plans

Funding a pension plan involves determining how contributions are to be made to plan assets to ensure that the fund will be able to pay expected future benefits. States and local governments are responsible for paying the costs of their public pension plans. These contributions are often made through a payroll deduction scheme, whereby employers contribute a set percentage of each employee's salary into the pension plan. The contributions are made to ensure that the fund will be able to pay expected future benefits.

Key Points

- Contributions should be sufficient to fund the plan's obligations.
- Contributions should be made on a regular basis to ensure the fund's solvency.
- Contributions should be made in a way that is fair to both employers and employees.
- Contributions should be made in a way that is consistent with the plan's funding policy.

Implementing State and Local Pension Reform

Executive Webinar Series
Fall – 2013

Dr. Adrian Moore (Reason Foundation)
Hon. Carl DeMaio (San Diego)
Hon. Pete Constant (San Jose)
Josh McGee (Arnold Foundation)
The State of Retirement: Grading America's Public Pension Plans

Our pension report card and interactive map grade state-administered retirement plans on their financing; how much retirement security they provide to short- and long-term employees; and the workforce incentives they create for younger, older, and mid-career employees. Results are based on the Urban Institute's State and Local Employee Pension Plan (SLEPP) database, which includes detailed state-by-state information on plan rules for public school teachers, police officers and firefighters, and general state and local government employees.

The database and report card were compiled by Richard Johnson, Barbara Butrica, Owen Haaca, Ben Southwick, and Eugene Stouffer.

Grade Distributions
State-Level Grade Distribution
Plan-Level Grade Distribution

Grade Tables
State Breakdown Table
Nationwide Best
Nationwide Worst

State-Level Distributions: All Employees, All Hires
Overall Grade

Rewarding Younger Workers

Promoting a Dynamic Workforce

Encouraging Work at Older Ages

Providing Retirement Income to Short-Term Employees

Providing Retirement Income to Long-Term Employees

Making Required Contributions

Funding Ratio
Leading Federal Legislative Proposals

- New Reporting Requirements
- Public Sector DB Alternative
- “No Bailout” Legislation
- Bankruptcy Protections
Recent Congressional Activity on Pensions
Leading Tax Expenditures Will Continue to Be Eyed for Revenue

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<th>Expenditure</th>
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<td>Health care exclusion</td>
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<td><strong>Pension deferrals</strong></td>
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<td>Reduced dividends/cap gains</td>
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(Joint Committee on Taxation estimates 2013-2023, in billions)
Potential Future Targets

• Mandatory Social Security
• Contribution/benefit limits
• Distribution rules
• Public employee DB contributions
Heightened Regulatory Interest

- SEC established new Municipal Finance and Public Pensions enforcement unit; renewed efforts to regulate issuers with focus on pension disclosure
- MSRB’s jurisdiction expanded under Dodd-Frank Act to regulate municipal advisors and protect state and local governments and their pensions
- Pensions under review by Financial Stability Oversight Council
- Treasury established new Office on State and Local Finance that includes review of pensions
Pending Federal Regulations

• Application of federal normal retirement age rules
• Definition of “governmental plan”
• Employee elections that change public employee DB contributions
Getting Out the Facts

- Municipal bankruptcy is rare
  - Only 12 states specifically authorize Chapter 9 filings for their general-purpose local governments
- Chapter 9 is uniquely designed to ensure a municipality can continue to provide essential services while debts are reorganized
- Chapter 9 does not provide for a Federal bailout
Pension Costs Are a Small Percentage of State and Local Budgets

3.7% Spending on pensions

96.3% All other spending

Reflects direct general spending, which excludes intergovernmental transfers
Pension Spending Is Not at an Historic High

Figure 2: State & Local Pension Contributions, in Dollars, and as a Percentage of State & Local Direct General Expenditures, 1982-2011
Pensions Are Not the Drivers of Most Municipal Fiscal Distress

Drivers in Cities with fiscal problems:

- Fiscal mismanagement (32%)
- Economic issues (28%)
- Pensions (9%)

Source: Boston College
Many New Disclosures Underway

- **Books**—computing an annual position regarding pensions for financial statements (GASB)
- **Bonds**—calculating how pension obligations affect a government’s creditworthiness (Ratings Agencies)
- **Budgets**—determining the appropriate annual contribution to the retirement system for sound funding (Funding Policies)
Long-term Investment Returns Have Exceeded Assumptions

Source: Callan Associates

Median public pension annualized investment returns for period ended 6/30/2014
Nearly Every State Has Made Notable Pension Changes

• Lower benefits:
  – Higher retirement age
  – More required years of service
  – Longer vesting period
  – Reduced or eliminated COLAs

• Increased financing

• One shift—for new Oklahoma state hires—from DB to DC

• Increased use of hybrid retirement plans
Timeline of Establishment of Optional or Primary Hybrid Retirement Plans

- TMRS
- Indiana PERF
- TX County & District
- CA State Teachers
- WA
- OH STRS
- GA
- TN, KY
- GA
- WA
- OH STRS
- GA
- TN, KY
- VA, KS
- UT, MI
- VA, KS
- UT, MI
- NASRA
Distinguishing Elements of Public Pension Plans Have Been Retained

• Mandatory participation
• Employee-employer cost sharing
• Assets that are pooled and professionally invested
• Targeted income replacement (including/excluding SS)
• Lifetime benefit payout
• Survivor & disability benefits
What Can Your Delegation Do?

• Understand the value of public plans in Texas to their district and their constituents:
  – $200+ billion in assets
  – 1.4 million active (working) participants
  – 500,000 retirees and other beneficiaries
  – $12 billion annually in distributed benefits throughout state

• Oppose efforts to impose conflicting and costly federal regulations and mandates

• Protect the tax treatment of public plans and employee contributions