A Guide to Pension Plan Management

A guide to evaluating your pension plan’s health and suitable solutions for maintaining or improving your plan’s future.

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Introduction

It can happen to you!

Elected officials must balance – and ultimately decide – between short-term benefits and long-term budget savings. These decisions will completely alter the trajectory of localities and impact all residents, employees, and future employees along the way.

The instability of fiscal health among governments at all levels has renewed a focus on the sustainability of public employee compensation packages, especially in relation to pension plans. Many state and local retirement systems are on a downward slope, failing to set aside sufficient funding and falling short of their investment targets. Although contributions to state funds nearly doubled since 2000, the situation is far from showing improvement.¹

The pension crisis is not limited to one state or geographic region, or to a singular level of government. In 2016, state pension funds reported a $1.4 trillion deficit – a $295 billion jump from 2015. Overall, state plans hold assets of just $2.6 trillion to cover total pension liabilities of $4 trillion.²
Debt Drivers

Pension Liability

Poor pension finances can threaten government’s ability to borrow at affordable rates. Since the financial crisis of 2007, bond-rating agencies have begun to account for pension liability in their rate calculations. This can be seen in cases such as Illinois where their credit ratings were downgraded due to unsustainable pension liabilities.

Overall, the 2016 measure of pension plan assets as a percentage of liabilities or funded ratios among our 50 states, ranged from 31% in New Jersey to 99% in Wisconsin. The states facing the most issues are Colorado, Connecticut, Illinois, Kentucky, and New Jersey, all of which are funded below 50%. Another 17 states have less than two-thirds of the assets required to cover the benefits, and only New York, South Dakota, Tennessee, and Wisconsin are above 90% funded. The map below (Figure 1) demonstrates the nationwide scale of the problem.

Implications of unfunded and underfunded pensions are multifaceted and complicated. Tax hikes, drops in credit rating, an inability to recruit and retain quality employees, the creation of poor socio-economic conditions for retirees, and a potential increased burden on the social services system are all possible. In some worst-case scenarios, even the threat of bankruptcy looms large. Increasingly, these scenarios are becoming a reality, as many states have seen their pension funding ratios drop to dangerously low levels. This underfunding of public pensions is not restricted solely to states either. A Pew Research Center study of 61 large cities in the United States uncovered a funding shortage of $99 billion out of the $385 billion needed for pension benefits, or a funded ratio of 74%.

Further Strains on Pensions

As state and local governments see an increased demand for resources coinciding with continuing retirements of Baby Boomers, the ability to “cut a little off the side” of many government programs will become increasingly difficult. This, coupled with underfunded pension programs, will put many state and local governments at risk. As was described earlier, tax hikes, drops in credit rating, and even bankruptcy all come into play. The implications of any action taken can be massive.

Figure 1.
Pension Costs

The cost of pension plans is driven by the design of the plan. Features such as a mandated Cost of Living Adjustment (COLA) or generous early retirement eligibility increase the cost of a plan. Other plan features that increase pension costs include high multipliers, short final average earnings calculations, and special features such as a Deferred Retirement Option Plan (DROP).

Failure of public pension plans can be attributed to a multitude of factors. Some sources of increasing pension debt are:

- Investment returns falling short of plan assumptions. Due to market volatility, public pension plans missed their aggregate return targets in 5 out of the 10 most recent years.

- Changes to assumptions about investment performance either due to previously missed investment return targets or recent regulations introduced by the Governmental Accounting Standards Board (GASB).

- Employer and employee contribution policies do not accurately predict the sufficient level of resources required to meet a plan’s growing costs.

- Benefit changes and shifts in demographics, such as changing rate of growth of employee salaries and increases in retirees’ life spans.³

![Sources of Change in Pension Debt, 2015-16](image)

Figure 2.
Government Pensioners

According to the United States Census Bureau, there are over 10 million people who collect state or local government pension benefits.\(^\text{10}\) The median state or local government annual pension benefit was $17,576 in 2016.\(^\text{11}\) If you include the average Social Security Insurance payment for retirees during the same period, which was $16,320, the average ex-state or local government employee received $33,896 a year, exclusive of any other income. This estimated annual income places government pensioners at slightly above 200% of the Federal Poverty Guidelines for a family of two.

The Aging of America

While pension costs continue to rise, the problems associated with this increase appear to be on a collision course with the effects of an aging America.

Baby Boomers, those born between 1946 and 1964, continue to reach retirement age. As the United States Census Bureau indicates, all Baby Boomers will be 65 or older by the year 2030. At which time, approximately 1 out of every 5 Americans will be at the retirement age.\(^\text{12}\) This shift will also mark the first time in our country’s history that older adults are projected to outnumber children, as shown in Figures 3 and 4.

The United States Census Bureau estimates the 65+ age group will increase from over 49 million in 2018 to over 80 million people by 2038, or 16% of the total population to nearly 22% by 2038, a number that nearly doubles the total 65+ age group.\(^\text{13}\)

This aging of America will bring with it unprecedented critical needs for health care, housing, and government services, and it is expected that there will be significant budget implications at the local, state, and federal government levels.
Public v. Private Retirement Benefits

Retirement benefits account for a greater share of public sector’s compensation – 8.1% compared with 2.8 to 4.8% in the private sector. However, in the private sector employees typically do not contribute to funding defined benefit retirement plans, while in the public sector the funding responsibility is shared between the employer and the employees.

Historically, the defined benefit plan was the primary retirement plan structure in both the private and public sectors. At their peak in 1975, 73% of private and 98% of public sector workers were covered by defined benefit plans. Over time, however, private sector participation in the defined benefit retirement plans sharply declined to 36% coverage in 2005, as compared with the public sector coverage of 92%. At the same time, private sector participation in defined contribution plans began to increase.

Retirement plans in the public sector operate under a separate regulatory framework from the private sector plans. Private sector plan requirements are set forth in the Employee Retirement Income Security Act of 1974 (ERISA), while in the public sector the requirements are largely left to the determination of the plan sponsors and administrators. The stricter private sector regulatory standards can be attributed to the differences in life span, revenue predictability, and stability of the funding bases of the public and private sector employers, and the increased risk of solvency issues in the private sector funds.

Typology of Retirement Benefits

The main types of retirement benefits are defined benefit plans (DB) and defined contribution plans (DC). Recently, hybrid plans, a blend of both DB and DC plans, are considered as an alternative to DB plans. Under DB plans, retirees typically receive a monthly lifetime benefit. The monthly benefit is determined based on the employee’s salary, service time, and a predetermined formula. The plan will have a series of retirement ages, which will determine when employees can retire from the plan. In the public sector, typically, both the employee and the employer contribute to the plan to fund the benefit. The investment and longevity risk reside with the employer who bears the responsibility to ensure the plan has enough money to pay the promised benefits for the lifetime of their retirees.

Under DC retirement plans, the retiree has a pool of money they are responsible for managing at retirement. The most familiar DC plans are the 401(k) and 457 plans. During employment, the employee and/or the employer will contribute to the DC plan. The employee is responsible for determining how the monies are invested. The amount of savings at retirement is dependent upon the amount of contributions, as well as how well the chosen investments have performed. The investment and longevity risk reside with the employee who must continue to manage their investments in retirement as well as their account balance.

Hybrid plans are a combination of DB and DC plans. Typically, the DB portion of a hybrid plan is smaller than a standalone DB plan. A DC plan offsets this smaller DB benefit. Employers are considering hybrid plans as means to reduce the liability and risk associated with DB plans while still being able to offer employees some form of guaranteed income in retirement.
Where Does the Money Come from?

There are three sources of annual income for pension plans: employee contributions, employer contributions, and investment earnings. The amounts contributed from each source can change, primarily because of volatility of investment returns as reflected in Figure 5. For example, there was a $14.4 billion increase to state and local pension benefit claims from 2015 to 2016. During the same period, earnings on pension investments declined 67.9% from $155.5 billion to $49.9 billion.

Figure 5.
Solutions to Consider

Many state and local government retirement systems are not on a sustainable path, but the degree to which reform is needed varies greatly. **Best practices** include tools and suggestions that can be used by all jurisdictions to monitor where they are and to better evaluate their current retirement system. The **preventive course** of action is geared towards retirement systems that can take action now to prevent a future crisis. The **extreme circumstances option** is tailored toward retirement systems on the brink of crisis or currently in crisis. Each plan can be adjusted to fit the needs of the state or local government. Figure 6 below offers a visual guide to the utilization of these suggested solutions.

**Best Practices**

State and local government elected officials should be knowledgeable of pension fund **tools for analysis, reporting, and stress testing** to better identify weaknesses and areas of opportunity within the current pension structure. These tools are described in detail in the following pages.

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Figure 6.
Using multiple tools to analyze pension health annually is key to maintaining a sustainable retirement system. **Funding ratios** are the most basic tool used to show how much of the future benefits can actually be paid with current assets. The ideal funding ratio should be 100% or higher. By looking at the **operating cash flow**, government managers can also see if current expenses are greater than the contributions coming from both the employer and employee. As the operating cash flow decreases, governments become more dependent on investments to keep plan assets up. Less operating cash flow also means there is less money to invest, potentially reducing future investment income, or at least making it harder for the plan to meet its assumed rate of return.

The **operating cash flow ratio** takes it a step further by showing what rate of return is needed on investments to insure assets do not decline. Over time, the assumed rate of return on investments has decreased. However, many pension plans are still calculated with a higher assumption rate than what they are able to realistically generate.

Return shortfalls contribute to increased unfunded liabilities. To have a better idea of how returns could impact pension plans, managers should apply **sensitivity tests**. The simplest approach is to evaluate pension liabilities at different assumed rates of return. This test can show how lower than expected returns can influence liabilities and assist in planning for those possible outcomes.²³

<table>
<thead>
<tr>
<th>Tools for Analysis</th>
<th>Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Funding Ratio</td>
<td>Shows how much of promised benefits can be paid with current assets.</td>
</tr>
<tr>
<td>Operating Cash Flow</td>
<td>Illustrates the pre-investment difference between expenses and employer and employee contributions.</td>
</tr>
<tr>
<td>Operating Cash Flow Ratio</td>
<td>By dividing the operating cash flow by the assets, the operating cash flow ratio shows the rate of return needed to guarantee that asset balances do not decrease.</td>
</tr>
<tr>
<td>Sensitivity Test</td>
<td>Measures the impact of differing assumptions, specifically around investments, on significant pension funding measures.</td>
</tr>
</tbody>
</table>

Figure 7.
**Reporting**

As a preventive best practice, elected officials should use ongoing reporting to increase transparency and awareness of the pension funding issue for all stakeholders, including both government employees and citizens. Reliable, ongoing reporting on the size and scope of pension funding enhances general knowledge of this issue. Reporting also documents the results of corrective actions taken to resolve pension-funding challenges and reduces the political nature of pension-related decisions. To increase the accuracy of reporting, information should be based on an annual actuarial valuation study and a more in-depth actuary experience study performed every three to five years. The annual actuarial valuation provides a snapshot of a plan’s assets and liabilities based on the plan’s provision and a set of assumptions. It also presents a roadmap for the funding of a pension plan. An experience study is a comprehensive study that reviews three to five years of data and identifies trends in the differences between the plan’s assumed experience and actual experience. The utilization of an experience study improves the effectiveness of reporting, because it relies on actual plan experience to make informed decisions regarding plan funding.\(^{21}\)

**Stress Testing**

Stress testing is another commonly recommended pension-risk management practice. This practice applies a simulation test on a plan’s reported assets and liabilities to analyze the effects of external hazards such as fiscal downturns or a stagnant economy. Since stress tests apply a multitude of scenarios, they have proven to be an invaluable tool for evaluating potential policy change options. For this reason, many believe annual stress testing should be a mandatory reporting requirement for all government pension plans. When properly applied, the stress test easily identifies long-term costs that can be expected due to a specific pension plan’s benefits and projected cash flow information. Stress tests can also provide an early warning to a poorly funded plan.\(^{22}\)

**Stress Test Model**

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Figure 8.
Preventive Course

Reforms

Depending on circumstance of the localities and the states, various measures can be considered to reform pension systems. Principal measures include reforming pension plan design, reforming how the pension plan is funded, adjusting the benefit offered to the employees, and applying reform measures associated with changes to the organization and management. In relation to *pension-plan-design reform*, measures include conversion from a DB pension plan to a DC plan, conversion to a hybrid plan, or the introduction of cash balance plans. If considering a *funding reform*, some of the measures that can be implemented are increasing either employee and/or employer contribution or investigating other measures to include the revenue from various sources. Figure 9 below describes the details related to the representative measures that can be implemented.24

<table>
<thead>
<tr>
<th>Pension Plan Design Reform</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Defined contribution plans</td>
<td>Employees contribute to a 401(k)-style investment fund. Employers may or may not match some or all of the employee’s contributions. Unlike benefit pension plans, lifetime income is not guaranteed.</td>
</tr>
<tr>
<td>Hybrid plans</td>
<td>Employees are enrolled in both a defined benefit and a defined contribution plan with benefits from traditional pension usually reduced.</td>
</tr>
<tr>
<td>Cash balance plans</td>
<td>A variation of defined benefit plans that guarantees an annual rate of return on an employee’s pension account, rather than promising a set pension income.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Funding Reform</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increasing employee contributions</td>
<td>Employees pay more for their retirement benefits. Changes in contributions can be implemented for current or newly hired employees.</td>
</tr>
<tr>
<td>Increasing employer contributions</td>
<td>Employer increases the amount of monies paid into the plan.</td>
</tr>
<tr>
<td>Adjusting funding sources</td>
<td>Explore other funding sources through various measures such as increasing taxes/fees, decreasing expenditures, creating special tax districts, issuing pension bonds, transferring resources from the general funds, generating additional investment revenue by diversifying the investment, or evaluating pension liabilities at alternative assumed rates of return.</td>
</tr>
</tbody>
</table>

Figure 9.
If planning to adjust the benefit offered to the employees, changing the rules for cost-of-living increases, changing the retirement age or vesting period, and applying measures to prevent pension spiking can be considered.

<table>
<thead>
<tr>
<th>Changes to Employee Benefits</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Modify COLA increases</td>
<td>Create measures to freeze, decrease, or cease annual COLA increases.</td>
</tr>
<tr>
<td>Amend retirement age or vesting period</td>
<td>Timing is adjusted as to when employees become eligible for retirement benefits by extending the retirement eligibility age and/or required years of service.</td>
</tr>
<tr>
<td>Reduce benefit accruals</td>
<td>Reduce the amount of pension benefits paid out by adjusting the final average earnings calculation or decreasing accrual percentages. These changes could be applied to all employees or just new hires.</td>
</tr>
</tbody>
</table>

Figure 10a.

Making changes to the organization and management, shifting funding to the state, joining a multi-employer system, or changing pension board makeup can also be considered.25

<table>
<thead>
<tr>
<th>Changes to Organization and Management</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shift funding to the state</td>
<td>State to take over full or increased funding for jurisdiction’s pension system.</td>
</tr>
<tr>
<td>Join a multi-employer system</td>
<td>Shift locality’s pension plans to one with multiple local employers that is run by the state or another state-level administrator.</td>
</tr>
<tr>
<td>Change pension board makeup</td>
<td>Ensure that pension board members, who have a great deal of authority over local retirement plans, have sufficient financial expertise or impartiality.</td>
</tr>
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</table>

Figure 10b.

What Happens if You Wait Too Long?

In an effort to reduce its $125 million unfunded pension liability, East Lansing, Michigan, has proposed a slew of potential budget cuts. The list of budget cuts includes the city’s pool, dog park, soccer complex, annual jazz/folk/film/arts festivals, a fire station, and even the suspension of leaf pickup and plowing of public sidewalks.26 Similarly, Kentucky reached a $48.9 billion pension shortfall in 2017, quadruple the state’s annual revenue of $11.7 billion.27 In an effort to increase pension funding, the state has had to divert funds from other priorities, such as public education, and take on additional debt through increased deficit funding, thereby worsening the state’s financial position further.28
Pay Now or Pay Later

Localities may find themselves in a place to “pay now or pay later.” Retirees, especially those who were low-wage earners, may need to fall back on federal, state, and local safety net welfare programs, including housing and shelter, cash assistance, medical and prescription services, and food assistance.

While these services vary by jurisdiction, common types of assistance often used by retirees who are experiencing financial difficulties include:

- healthcare, inclusive of state contributions to Medicaid
- property tax assistance or reductions, which reduce the tax burden
- energy assistance to help pay for utilities
- food assistance programs to provide or help fund the purchase of food
- pharmaceutical insurance coverage and prescription discounts
- housing assistance
- disability and nursing home assistance
- transportation options, including reduced transit fares

Although states and localities are likely to see an increased demand for these programs and services, they will have to make difficult decisions to balance the need for additional services with the need to further fund sinking pension obligations. This is already taking place in some localities today.

Oh, SNAP!

In FY 2017, the Supplemental Nutrition Assistance Program (SNAP) reached 776,000 Virginia residents, or 9% of the state population; nearly 35% of Virginia SNAP households include elderly or disabled individuals. In 2018, the number of Virginia’s extremely low-income renters who receive housing assistance reached 257,338; approximately 22% of these households include elderly individuals. These programs and services, among others, will see increased demand and likely require additional funding should public employees take cuts or lose their pensions.
Extreme Circumstances Option

Structure

The extreme circumstances option is tailored toward retirement systems on the brink of crisis or currently in crisis. In this case, elected officials must gather the required expertise to brainstorm, make unpopular decisions, formulate a solution, and execute their strategy. Paramount in establishing an effective Extreme Circumstances Commission (ECC) is removing partisan politics and focusing on the end goal of salvaging the employees’ pension program while maintaining a funded and effective government. To do so, the ECC should be led by an appointed person who lives in the locality in question, has no political ties, and possesses a relevant leadership background. Once this vital role is fulfilled, the Commission lead can work on establishing the remaining Commission positions as detailed in Figure 11.

A City in Crisis

The City of Harvey, Illinois, is facing an unemployment rate of 22%, while 33% of the population lives below poverty level. The combination of these factors negatively impacted the city’s revenues and its ability to fund pensions for the city’s retired workers. Illinois prohibits municipal bankruptcy; therefore, in February 2018, the state began to garnish Harvey’s revenue to fund its pension liabilities, resulting in layoffs of 25% of the city’s police force and 40% of its firefighters.29
Powers and Scope

In order to be effective in their mission to correct years of severe financial mismanagement and lack of pension plan funding, the ECC must have a predetermined scope and set of powers to enact change. To understand the situation a locality is in, they must have complete access to their financial information, including budgets, sources of revenue, and relevant financial reports. Once the Commission fully understands the predicament the locality is faced with, only then can they move forward with a correctional plan for long-term financial success. When developing this plan, the Commission must have the power to:

✔ set future pension funding policies; modify, diversify, or simplify the plan
✔ alter employee benefits and compensation
✔ offer 401(K) option in lieu of pension
✔ offer opt-out program with continued, but largely reduced contribution to pension program
✔ reduce growth of pensionable salaries
✔ raise taxes and government fees
✔ identify/redirect/create cash-generating public assets or dedicated funding streams
✔ create special tax districts
✔ request state to review the current and proposed plan
✔ implement mediation and/or arbitration
✔ develop and institute early-education programs for financial investment/retirement strategy

The powers of the Commission are equally as important to define as the Commission’s limitations. Specifically, they cannot cut an existing employee or retiree’s benefits to place them below the poverty level. Localities should define lowest acceptable salary cuts and/or tax increases before the Commission is convened.

The Cost of COLA

Retirement systems in the State of Illinois are an example of pension plans in crisis. After years of inadequate pension plan contributions, by June 2017, the funding shortfall for the state’s five retirement systems increased in just two years by $17.8 billion to $137 billion. Since 2015, Illinois’ credit rating was downgraded to the verge of junk, its bonds have tumbled, and Moody’s Investors Service stripped Chicago of its investment-grade status.

The primary causes of the Illinois pension crisis are the automatic 3% COLA, early retirements, and longer life spans of the retirees. The automatic COLA causes the retirement benefits received by retirees to double in just 25 years.

In 2013, Illinois lawmakers approved cuts to COLAs and a higher retirement age for some workers. These measures were estimated to save more than $100 billion over 30 years; however, it was subsequently ruled unconstitutional by the Illinois Supreme Court as it violated the state constitution’s ban on reducing retirement benefits.
Funding and Resources

To support the ECC’s mission, elected officials should allocate additional funding and resources. This dedicated funding should be made available for the following resources:

✔ associated staff time dedicated to the Commission as outlined in Commission structure
✔ office space, supplies, and other non-personnel expenses
✔ consultant funding for subject matter experts and third-party facilitators

To facilitate the Commission’s effectiveness, a third-party facilitator and a subject matter expert should be considered as a resource for the Commission. A public policy facilitator is typically a private, non-profit research center that focuses solely on assisting government officials in finding data-driven solutions through productive non-partisan deliberations. The use of a third-party non-partisan subject matter expert provides the necessary technical expertise to make better-informed policy decisions while insulating the Commission from the appearance of a politically influenced or driven decision-making process. For example, Milwaukee County, Wisconsin has had success with integrating third parties into its own Retirement Sustainability Task Force. To enhance the policy decision-making process, the Public Policy Forum, a Wisconsin based non-profit, was brought in to facilitate and provide expert consultation to the City’s task force meetings. Milwaukee County also invited The Pew Charitable Trusts to provide subject expertise and best practices from its Public-Sector Retirement Systems project. This two-prong approach allows the task force to bypass many of the administrative logistics in order to focus on the decisions at hand immediately.30

Considerations for the cost of establishing and supporting the functions of the Commission should include items such as the salaries and benefits of any existing staff; reimbursements of reasonable and necessary expenses, such as travel and per-diem; and general expenses related to normal business of the Commission, such as administrative support, printing, and information technology support.

Additional costs that may need to be considered and planned for include hiring consultants and experts in various fields, supporting the research costs of staff and experts, and visits to other localities or state governments for information. Additional sources of data that may incur some costs could be consulting services of non-profit expert associations such as the Pew Charitable Trust, the Public Policy Forum, and the National Association of State and Local Governments.

Timeframe

The timeframe in which the Commission must gather data, hear input from employee and community groups, and develop and present a plan for implementation, is very compressed. A single fiscal year should be considered a minimum timeframe for planning. Once the City Council or Board of Supervisors has appointed the Commission, the first meeting should be scheduled immediately. The following considerations should be included in the development of the Commission schedule:

- define a specific term - one fiscal year - with a sunset provision
- no authority to extend or postpone the term, nor to adjourn without completing the plan
- meetings and sessions of the Commission do not require public announcement or advertisement, but minutes of the meetings must be recorded
• meetings must be announced to all of the Commission members and a quorum of members must be present for actions of the whole to be binding

• timeline of Commission must start aggressively on Day 1 of the session

• first meetings must establish the organization including appointing a chair, vice chair, and secretary

• basic rules may follow local procedure for other committees, including the rules of order and the method of minute and note taking

• legalities of the Commission must be established quickly so that data gathering can begin

• presentations may be solicited from employee groups, experts, and public groups, but they must be presented with budget implications and hard numbers taken from the adopted budget in order to be included in the final plan

• draft outline of the plan must be complete, with a rough budget impact included, by the end of the first fiscal quarter

• final outline must be developed, completed, edited, with the final budget numbers calculated and tabulated by the end of the second fiscal quarter

• final review of the plan and budget implications takes place at the end of the third fiscal quarter and is immediately presented to the Council or Board of Supervisors; presentation will coincide with the normal schedule for the annual budget; plan must be adopted before the new fiscal year begins

• implementation begins with the new fiscal year

Figure 12. Timeline for Extreme Circumstances Commission
Today’s elected officials are being asked to do more with less money. These competing priorities are coinciding with uncertain economic times where projected investment returns are at all-time low levels. The result is that governmental officials have to make tough choices between contributions to their pension plans and other competing priorities. The underfunding of governmental pension plans has become a nationwide crisis.

The implications of underfunded pension plans are vast. Some consequences include issues with retention and recruitment of staff, future increased tax rates, reduced credit ratings, and lower standard of living for retirees, who are becoming a growing and increasingly vocal part of the voter base.

Now is the time to take action to ensure pension plans are properly funded or to establish a correction course to secure the plans’ future sustainability. All plans are recommended to follow a handful of industry best practices including reporting, regular monitoring using benchmarking tools, and stress testing. If a jurisdiction’s plan appears to be headed for danger, preventive measures should be taken without delay. Preventive measures include reforming pension plan design, reforming how the pension plan is funded, adjusting the benefit offered to the employees, and applying reform measures associated with changes to the organization and management. In extreme cases where the plan needs immediate intervention, a jurisdiction may want to consider enacting a commission to step in and transform the plan’s design and operation. Regardless of the circumstances of a particular plan, there is an increasing need for elected officials to take an active role in the pension plan’s funding.

Recruitment and Retention

The reality of today’s job market is that workers are expecting more from their employers and are not afraid to move on if their needs are not met by an organization. Many state and local governments are considering cutting their pension benefits for new hires. Doing so could hurt governments’ ability to compete with the private sector for skilled workers.

Governments at all levels have traditionally been passive in their recruiting approach; however, they are beginning to face pressure to modernize and adapt their recruitment strategies to attract young, highly qualified applicants to fulfill their staffing needs. Employee benefits, including the retirement package, are factors which employers are considering when trying to increase their ability to successfully recruit and retain qualified applicants.
Endnotes

In-text citations


Figures


Pictures

Cover photo: https://www.shutterstock.com/image-photo/money-growing-plant-step-deposit-coin-18023393

Page 2: https://www.youvisit.com/tour/photos/gmu/80651?id=69758


Page 5: https://pixabay.com/en/credit-squeeze-taxation-purse-
Pension History

The origin of pension plans in the United States dates back to pensions granted to state militias during the colonial era. Pensions were expanded to all military personnel during the American Revolution and subsequently approved for the Army and Navy after the ratification of the U.S. Constitution. The next expansion wave of pension coverage in the late 1800s included police, firefighters, and teachers. The first pension plan for general state employees was established in Massachusetts in 1911. By 1970, every state and most local governments offered retirement plans to their full-time employees. These plans often included perks such as lower retirement ages, reduced years of service requirements, lowered vesting time requirements, and increased retirement multipliers. By the beginning of the 21st century, public employees were eligible to retire younger, after fewer years of service, and with higher income replacement calculators applied than their private-sector counterparts.

Prior to the 1980s, most public sector pension plans adhered to low-risk, fixed-income investments such as bonds. However, in the 1980s and 1990s, relaxed regulations allowed public retirement funds to invest in equities and other high-risk financial instruments. These new avenues created high rates of return and reduced government payments into retirement plans, particularly during the bull market of the 1990s. Over time, plans increased their reliance on high-risk investments.

In the 2000s, the economic downturn of the Great Recession led to a significant decline in public pension funding and investment returns. State and local governments have struggled to balance their budgets, and reductions in state and federal contributions caused greater financial obligations for local governments already operating with budget gaps.

In 2012, the Governmental Accounting Standards Board (GASB) enacted new transparency rules for government pension plan calculations and documentation. Under the new guidelines, governments must disclose their pension liability, i.e., the difference between expected benefit payments and the assets already set aside to cover them. Specifically, new GASB rules require pension assets be calculated using actual market values and lower assumed rates of return on pension plan investments. This results in higher unfunded liability and volatility than previously reported.