

**Framing the Issue:
Overview of Public Pensions
in the U.S. and California**
for the
**Public Employee Post-Employment
Benefits Commission**

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Size and Scope of State and Local Government in the U.S.

- **~16 million people are employed full-time by state or local government**
 - More than 10 percent of the nation's workforce
 - Education, police, fire, and corrections comprise 65 percent of total
- **90 percent have a traditional pension, or defined benefit (DB) plan**
- **Public DB assets are ~\$3.0 trillion**

Benefits Distributed in the U.S.

- **Public retirement systems in 2005 distributed:**
 - \$141 billion in monthly benefit payments
 - to ~7 million annuitants
 - average \$20k annually
- **Exceeds the personal income derived from the nation's farming, fishing, logging, and hotel/lodging industries, *combined***

Public Employees and Plan Type

- **Ninety percent of full-time state and local government employees in the U.S. have a defined benefit plan, aka a traditional pension, as their primary retirement benefit**
- **Policymakers in many states have considered changes to plan type; the percentage of public employees with a traditional pension benefit has not materially changed**

Defined Contribution Plan Only

- **On a statewide basis for broad employee groups (teachers, public safety personnel, general employees) with only a defined contribution plan as the primary retirement benefit:**
 - **District of Columbia general employees**
 - **Michigan state employees hired since 1996**
 - **All newly-hired public employees in Alaska since July 2006**

Plan Type Switches This Decade

- **Since 2000:**
 - **Nebraska switched its state and county workers from a defined contribution plan to a hybrid**
 - **West Virginia switched newly-hired school teachers from a defined contribution to a defined benefit plan**
 - **Alaska switched newly-hired public workers from a DB to a DC**

Hybrids and Choice

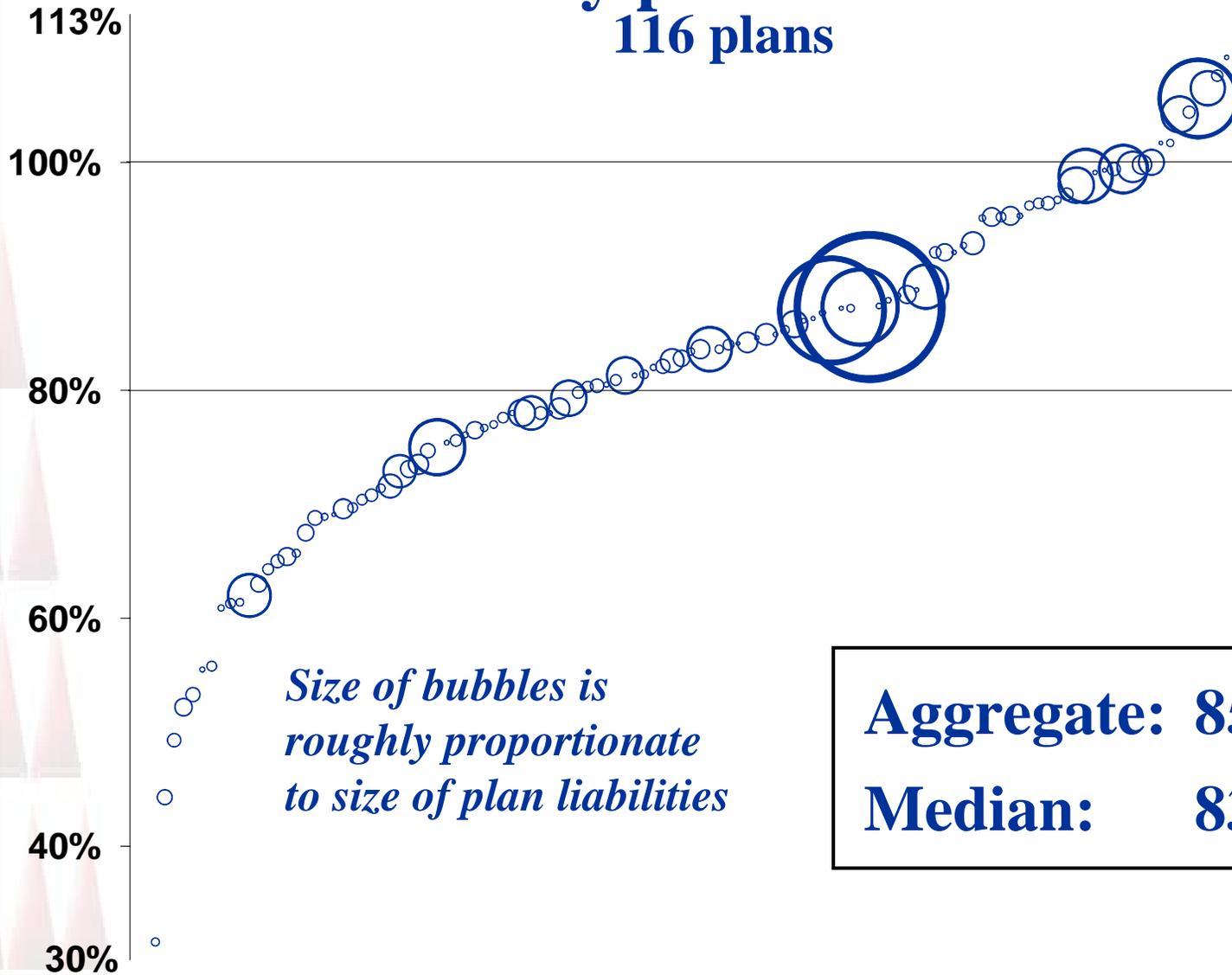
- Hybrid plans have been established since 2000 in Washington state, Oregon, Ohio and Nebraska
- Hybrids have been in place for many years for public employees in Indiana and many Texas municipal and county workers
- Since 2000, broad groups of employees have been given the opportunity to choose their retirement benefit
 - FL, SC, OH, MT, CO

Core Elements of a Traditional Pension Plan

- Prefunded benefits
- Investment risk that is pooled and shared by large numbers of participants and multiple age cohorts
- Low investment and admin costs enabled by economies of scale and non-profit administration
- Professionally-managed assets invested in diversified portfolios using a long time horizon
- Regular contributions from employers and employees
- Annuitized benefits based on salary and length of service
- Mandatory participation and automatic enrollment
- A decentralized state- and local-driven regulatory structure featuring plans overseen by independent boards of fiduciaries

Public pension funding levels by plan size

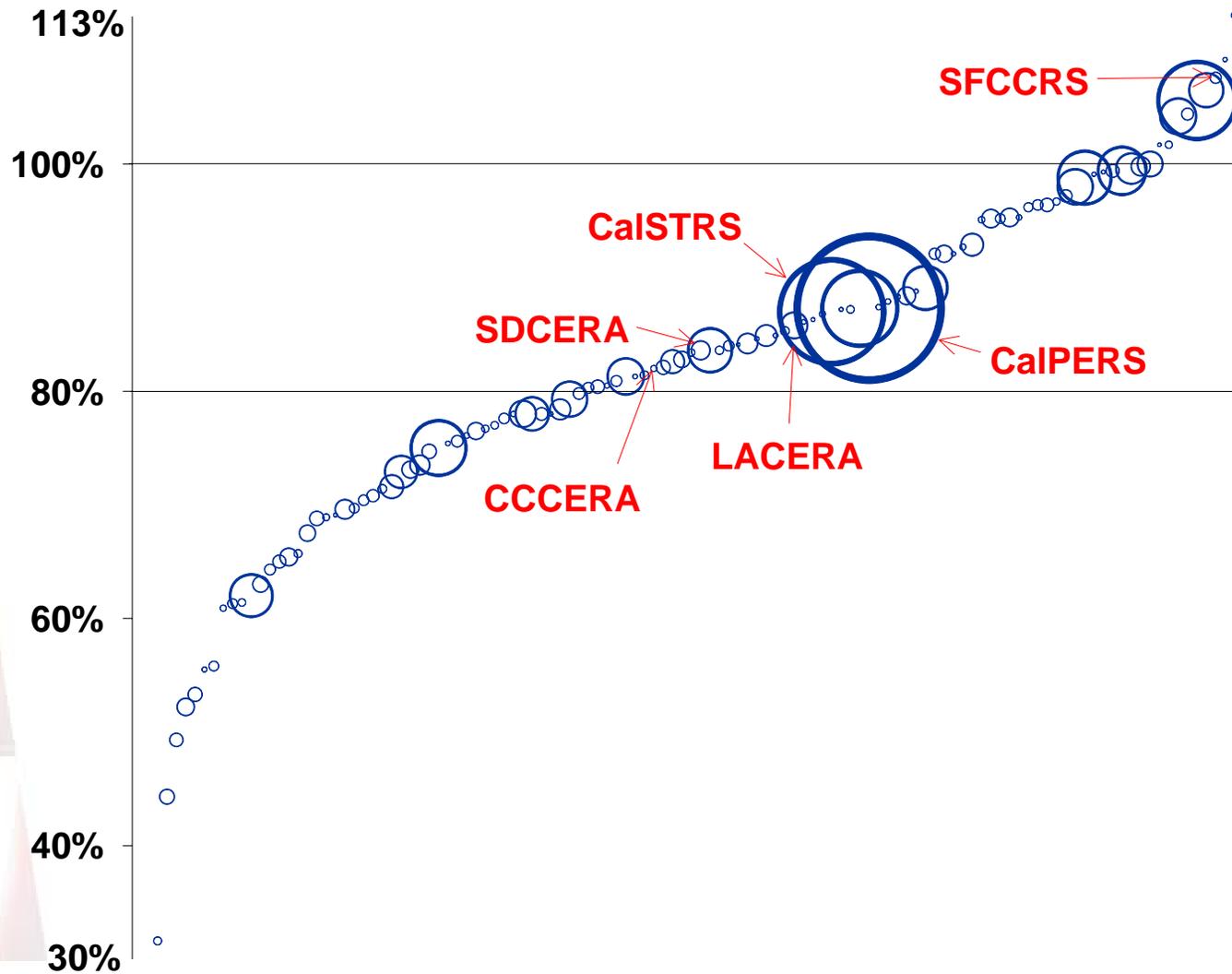
116 plans



Aggregate: 85.7%
Median: 83.7%

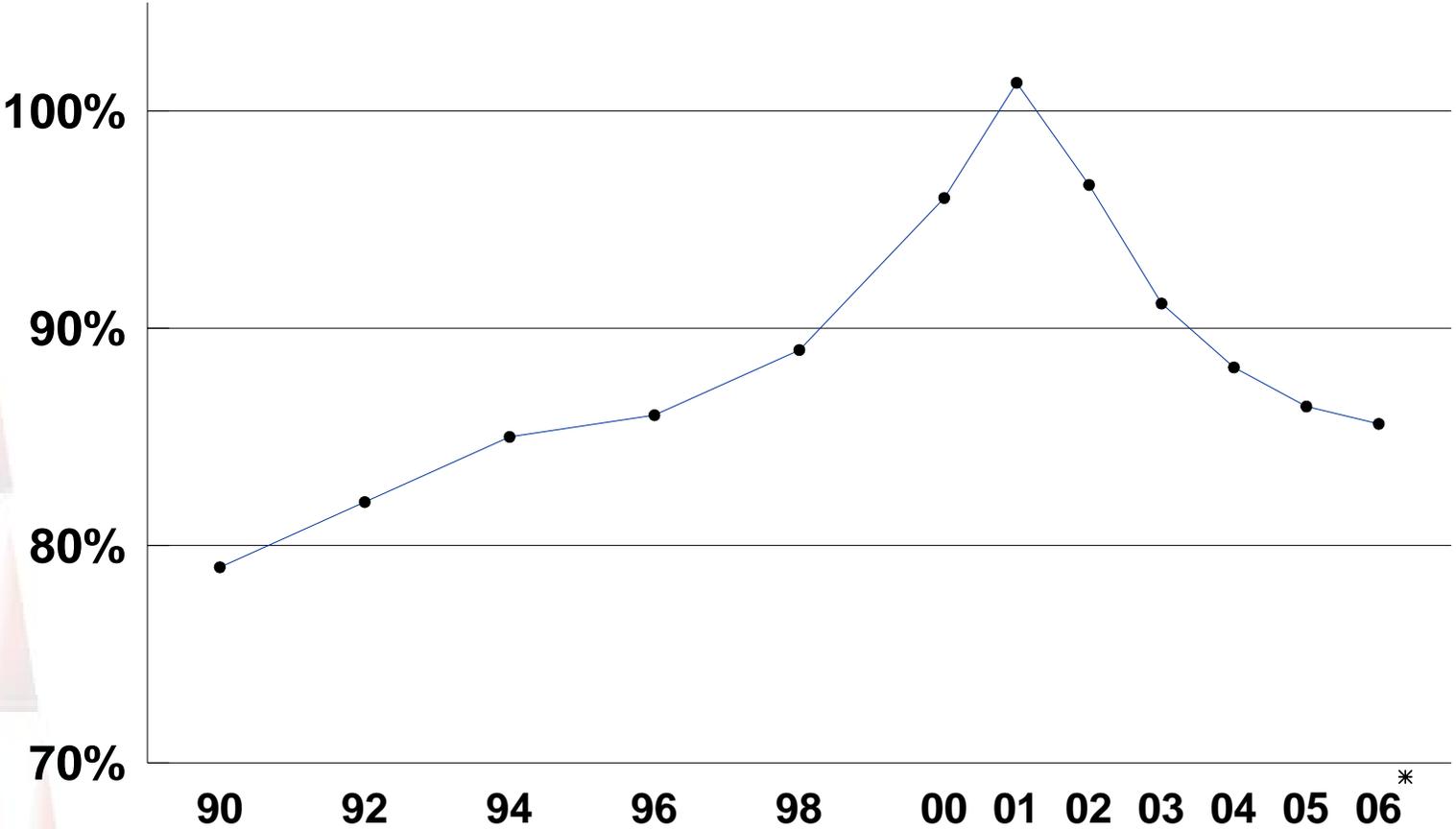
Public pension funding levels by plan size

Delineating selected California plans



Aggregate Public Pension Funding Level

State and Local Pension Plans



Standard & Poor's and
Public Fund Survey

Fiscal Year

*Preliminary

Public Pensions in CA - 2005

- Active (working) participants: ~1.7 million
- Annuitants: ~850,000
- Assets: \$500+ billion
- Sources of revenue:

Employee Contributions **9%** \$6.9 B

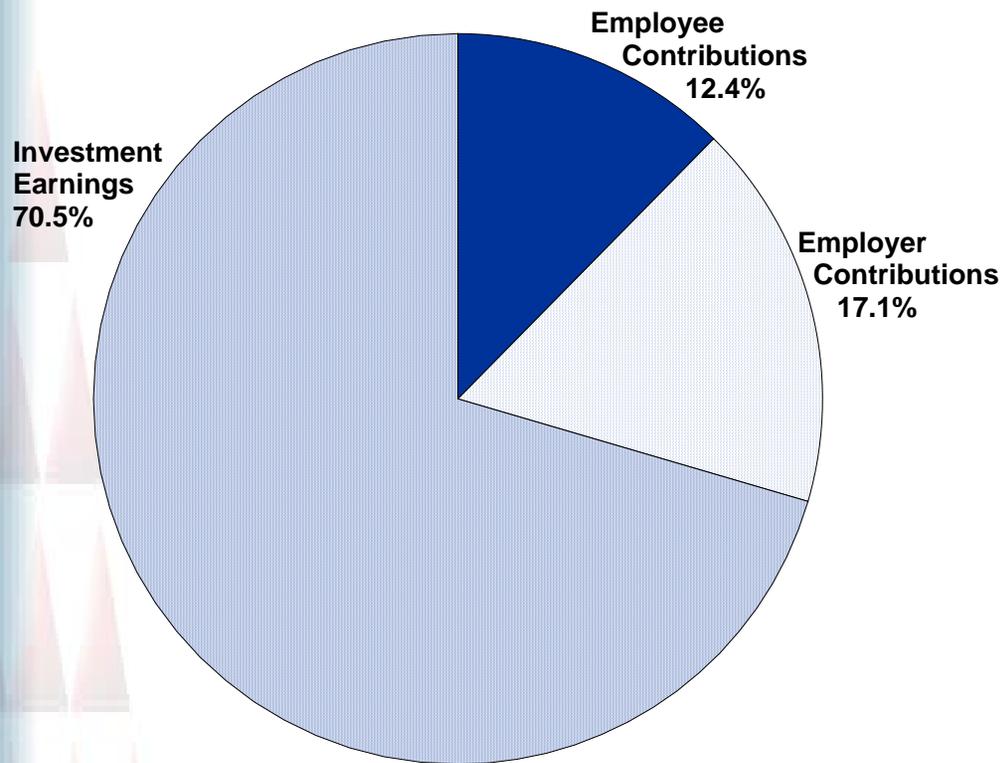
Employer (Taxpayer) Contributions **16%** \$12.4 B

Investment Earnings **75%** \$56.9 B

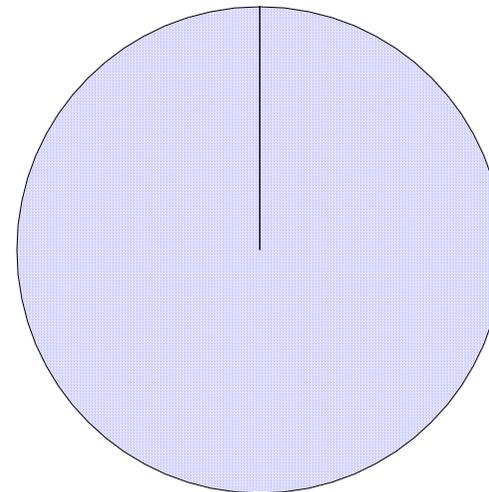
Benefits Distributed by California Public Pension Funds – FY 05

- \$22 billion in monthly benefit payments to 850,000 annuitants
 - average \$26k annually
- **Exceeds the personal income derived from California's farming, fishing, and mining industries, combined**

California Public Pension Revenues and Benefits Distributed FY96 – FY 05



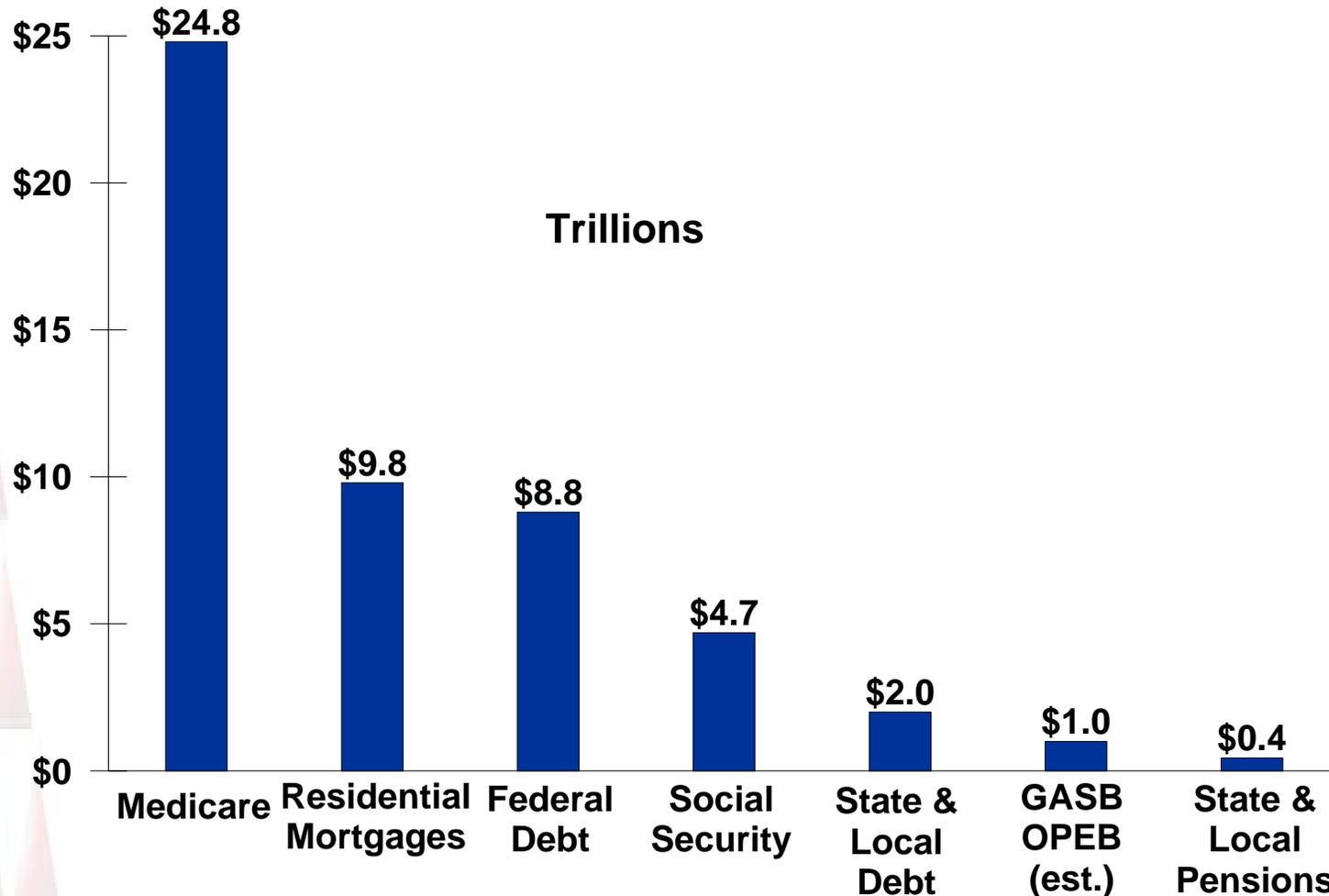
Revenues:
\$281.4 Billion



**Benefits
Distributed:**
\$171.6 Billion

U.S.
Census
Bureau

Comparison of Selected Outstanding Debt and Unfunded Liabilities, U.S., 2007



Federal Reserve, Social Security Board of Trustees, Census Bureau, Public Fund Survey, compiled estimates

Public Employees and Social Security

- **Nationally, about one-fourth of state and local government employees do not participate in Social Security**
- **In California, this figure is higher:**
 - **Public school teachers and most public safety personnel do not participate**

Public Employees and Social Security

- **Non-SS-participants and their employers each save 6.2% of pay relative to SS-eligible participants**
- **For example:**
 - **CalSTRS annual payroll: \$24 B**
 - **Estimated annual savings to school districts and other CalSTRS employers: \$1.5 B**

Key Differences Between Public and Private Sector Pensions

- The public has a compelling interest in ensuring that certain positions remain filled with qualified and experienced personnel
- Unlike private pensions, active participants in public sector plans are required to make contributions
- Public pension plans are not subject to federal regulations that make them onerous and expensive to administer and maintain
- The life cycle and business models of the public and private sectors differ
- Pensions and other benefits traditionally have been used to offset lower salaries in the public sector

Key Differences Between Social Security and Public Pension Plans

- **Social Security**

- Is a *pay-as-you-go* plan
- Is highly sensitive to demographic changes
- Has a trust fund with no tangible assets

- **Public pensions**

- Are mostly *pre-funded*: the aggregate actuarial funding level of public pensions is currently around 86%
- Are less sensitive to demographic changes
- Hold ~\$3 trillion in tangible assets

Key Differences Between Pensions and Retiree Health Care Benefits

- Health care costs are rising faster than pension costs
- Factors driving the cost of these benefits are different, and the solution must be different
- A pension is a promise to make a cash payment at a future date; retiree health care is usually a promise to finance a service whose future cost is less certain
- Eligibility standards for retiree health care benefits usually are more stringent than for pensions
- Pension benefits generally are inviolable; retiree health care benefits usually are not
- Unlike public pensions, methods for financing and administering retiree health care varies widely
- Public pension benefits are fairly consistent around the U.S.; retiree health care benefit levels vary widely

Retirement Benefits and Public Policy

As both policymaker and a major employer, the public sector is uniquely situated to model innovative retirement policies that meet the needs of all stakeholders while promoting retirement financial security.