

Future of Retirement Plan Design for Public Employees

2009 NASRA Conference Presentation

Public pension systems across the country are caught in a firestorm of publicity from taxpayers and plan sponsors alike. Criticism centers on declining investment returns, benefit plans that are perceived as too rich compared to the private sector, and a market recession that has resulted in public pension plans losing over \$1.2 trillion since 2008. **Kim Nicholl**, Managing Director of Price Waterhouse Coopers Public Sector Retirement Consulting practice, gave a very informative and revealing presentation on the future of plan design in the face of the current pension system woes.

It is widely acknowledged that there are a number of factors that have contributed to the problems facing pension systems today. Poor market returns are exacerbated by an aging population, increased life expectancies, and, for some plans, the rising cost of health care. According to Ms. Nicholl, the ratio of persons under the age of 65 to those 65 and over is currently 4 to 1, and that will change to 2 to 1 by the year 2050. Not only are the baby boomers reaching retirement age, they are living longer and drawing benefits from their retirement plans far past the actuarial predictions of only a few years ago.

Ms. Nicholl cited the actuarial formula of Contributions + Investments = Benefits + Expenses ($C + I = B + E$) to illustrate that there are few options available to address the decline in funding ratios. In many cases, employee contributions are set in statute and their benefits are protected by an inviolable contract. Employer contributions can also be established in statute and equally difficult to change. Even in plans where the board establishes employer contribution rates through actuarial calculations, the economic recession has brought reduced tax revenues for city, county and state governments, and there is little room in tight government budgets to increase contribution rates.

According to Ms. Nicholl, plans can no longer depend on investment income alone to restore healthy funding. She gave an example of a plan that started the current recession in 2008 with a relatively healthy funding ratio of 80%. Assuming that plan lost 25% of its market value in 2008 and recovered to a positive 8% rate of return for the next 15 years, the funding ratio could continue to decline to below 50% by the year 2023. Under these conditions, the plan sponsor must consider benefit reductions to maintain viability.

While many benefits are protected under an inviolable contract, plans can consider several alternatives. Among those mentioned are reducing or suspending COLAs, increasing the minimum retirement age and years of service, decreasing benefit formulas or increasing the number of years included in the average final salary calculations. It is safe to say that any one correction may be insufficient to move the

needle on unfunded liabilities, and plans may have to consider implementing multiple changes to achieve the desired result. Benefit reductions, though not easy to sell to employees, may be necessary for defined benefit plans to remain viable over the long term.

Mike Burnside, Kentucky ERS

State and local pensions plans are on a path to failure.

Saturday, January 2, 2010; The Washington Post A12

THE RECENT history of pension plans for state and local government employees can be summarized as "promise now, pay later." Eager to attract good workers -- or to placate unionized ones -- elected officials often contracted for generous retirement benefits, including health benefits, without increasing taxes to pay for them. The next governor, mayor or city council could worry about that. Meanwhile, governments used rosy investment earnings projections, typically 8 percent a year, to make their promises appear more affordable than they really were.

Never truly a sustainable strategy, given the aging of the population, this approach took on artificial plausibility during the stock market boom of the 1990s. But the current financial crisis has thoroughly exposed the folly of it. The stock market's plunge since the Dow Jones industrial average hit an all-time high of 14,164 on Oct. 9, 2007, has cost state pension funds hundreds of billions of dollars. The hardest-hit states are those, such as California, Illinois and New Jersey, that made the most lavish underfunded promises. Still even relatively responsible states such as Virginia and Maryland have been hit hard. The market's comeback this year has ameliorated the situation to some extent. Many pension funds are tempted to gamble for higher returns to make up for their losses. Even if pension funds do manage to achieve that magical 8 percent average rate of return over the next 15 years, they will only have an average of 45 percent of the money they need to pay benefits, according to an analysis by state pension expert Kim Nicholl of PricewaterhouseCoopers. The picture for health benefits, which states are generally paying out of current revenue, is even worse.

States must not count on the markets to rescue them from this predicament. There are some savings to be achieved through efficiency measures, such as irrevocable trusts that protect pension funds from periodic raids by the rest of government. But the path to solvency, if there is one, runs through the hard business of restructuring -- i.e., trimming -- benefits. This will take political courage, especially in states where public-sector unions are most powerful. Yet the truth is that state and local public employees often enjoy far more generous pensions and medical benefits than the taxpayers who fund them. Nine out of 10 public-sector employees have a defined-benefit plan, with a median pension in 2005 of \$17,640 per year. By contrast, only 20 percent of private-sector employees enjoyed defined benefits, and the median level was \$7,692. This is a ticking financial time bomb, and the time to disarm it is now.

Public-pension tab in Ohio: \$4.1 billion -- and growing

By Plain Dealer staff and wire reports

January 03, 2010, 5:00AM

About this project

This project is the work of Ohio's eight largest newspapers: The Plain Dealer, The Cincinnati Enquirer, The Columbus Dispatch, The Dayton Daily News, The Akron Beacon Journal, The Toledo Blade, The Canton Repository and The (Youngstown) Vindicator.

The newspapers have been working together for several years to report on issues important to Ohioans.

After reporting locally about extensive cuts in services in their communities, the editors decided to examine the state's pension policies. The objective: To explore the impact of state-mandated pensions and retiree health insurance on local communities and whether potential increases can be absorbed.

Methods used to determine potential costs

Two methods were used to determine the potential cost of the state pension systems to Ohio taxpayers by 2013.

One technique calculated the percentage increase of local and state governments' pension costs for the past five years and projected that same percentage for the next five years. Using numbers from the past five years tends to smooth out any aberrations in a single year. That method showed that an additional \$604.5 million would be needed by 2013.

The other technique calculated the one-year dollar increase in governments' pension costs from 2007 to 2008 and projected that same increase for each of the next five years.

Examining the data that way uses the freshest possible figures on government pay and staffing levels, which are directly proportional to pension costs. That method showed that an additional \$768 million would be needed by 2013.

The numbers for the individual pension systems that lead to this overall projection are very close to the pension systems' own five-year forecasts. The State Teachers Retirement System's figure is 3.2 percent higher; the Ohio Public Employee Retirement System's forecast is 1.2 percent higher. The Ohio Police & Fire Pension Fund did not calculate an amount, but a spokesman said, "We are fine with the numbers you projected." The School Employees Retirement System did not calculate a five-year total.

The system for the State Highway Patrol retirees was not examined because it is totally state funded.

-- Darren Rowland, Columbus Dispatch

James Nash, The Columbus Dispatch

At a time when budget problems are forcing Ohio schools to lay off teachers and cities to raise taxes, eliminate jobs or both, one expense that government leaders have not cut is pensions for their workers.

The pension cost to local governments in Ohio now stands at \$4.1 billion a year. If current trends continue, the pension costs will grow by \$604 million to \$768 million during the next five years, according to a computer analysis by the Columbus Dispatch for The Plain Dealer and the state's other large newspapers.

The increased costs greatly depend on how much government payrolls grow.

But two of the five public pension systems are asking taxpayers to dig deeper to cover funding shortfalls, potentially adding \$400 million more to the tally by 2020. All told, the taxpayer tab easily could top \$5 billion a year by the middle of the next decade.

Those tax dollars will help ensure that retired teachers, police officers, state workers and other government employees receive retirement benefits that many of their private-sector counterparts can only envy, although direct comparisons are difficult.

Retirement incomes for the most experienced government employees top out at 88 percent of their active-duty pay. Unlike most private-sector workers, whose retirement is driven by the strength of the stock market and their 401(k) plans, the pensions for government employees are guaranteed.

In addition to receiving higher average retirement incomes, government retirees in Ohio enjoy government-sponsored health care, can retire as young as 48 for police and firefighters and have the opportunity to "retire" and collect a full pension while going back to work, often at full pay for doing the same job.

Such "double dippers" were paid more than \$741 million by the State Teachers Retirement System last year and \$240 million by the Public Employees Retirement System, records show.

In Toledo, even the mayor is a double dipper.

Since starting his current term in January 2006, **Mayor Carty Finkbeiner** has drawn his annual salary of \$136,000 in addition to a state pension for more than two decades in elected and unelected positions. He is leaving office on Monday.

The Plain Dealer has regularly reported on the practice in Northeast Ohio, including the recent decision by Cuyahoga County Treasurer Jim Rokakis, 54, to collect his retirement and return to the same job at a salary around \$76,000.

Other officials using the practice include Cuyahoga County Commissioners Jimmy Dimora and Tim Hagan, Recorder Lillian Greene, Sheriff Bob Reid and several local judges, mayors, superintendents and clerks of court.

Question have been raised about whether the budgets of local governments can handle higher premiums given that libraries, school districts and cities are receiving less tax revenue.

Increases in pension costs will mean cuts elsewhere, warned John Mahoney, executive director of the **Ohio Municipal League**, which represents cities.

"I can't pay that and still employ 1,700 police officers," he said. "I can't do it. The money's just not there."

Historic shift

For decades, nearly all government workers have been in traditional pension plans that pay fixed amounts at retirement, usually calculated as a percentage of their highest annual salaries multiplied by years of service.

At the same time, private employers have moved dramatically away from such defined-benefit plans. In 1974, 71 percent of private retirement-plan assets were in defined-benefit plans. By 2008, that number had decreased to 24 percent, according to the nonpartisan **Employee Benefit Research Institute**, although some private employers still offer a combination of defined-benefit and 401(k)-type plans.

Ohio's pension systems
 A breakdown of the state pension system participants and expenditures for 2008 (the most recent year available) as well as the current projected state contribution to government employees, compared to their employer's other government costs per year.

PENSION SYSTEM	ACTUAL 2008		2009 ESTIMATE	EXPENDITURES		2009 ESTIMATE		2009 ESTIMATE	
	Participants	Assets		State Contribution	Other Govt. Costs	State Contribution	Other Govt. Costs	State Contribution	Other Govt. Costs
Public Employees Retirement System	274,942	\$4,400,000,000	\$2,100,000,000	\$1.1 billion	\$1.5 billion	\$1.1 billion	\$1.5 billion	10%	10%
Public Teachers Retirement System	175,776	\$4,000,000,000	\$2,100,000,000	\$1.1 billion	\$1.5 billion	\$1.1 billion	\$1.5 billion	10%	10%
School Employees Retirement System	124,278	\$1,000,000,000	\$500,000,000	\$250 million	\$300 million	\$250 million	\$300 million	10%	10%
Ohio State Employees Retirement Fund	20,000	\$1,000,000,000	\$500,000,000	\$250 million	\$300 million	\$250 million	\$300 million	10%	10%
TOTAL	594,996	\$10,400,000,000	\$5,200,000,000	\$2.5 billion	\$3.3 billion	\$2.5 billion	\$3.3 billion	10%	10%

Despite that historic shift in the private sector, many government leaders say the public pensions are all but untouchable.

"The goal should be to continue the defined-benefit plan," said State Rep. Todd Book, a Portsmouth Democrat who chairs the **Ohio Retirement Study Council**. "It's good for the employees of the state. It's also good for the economy of the state. You have retirees pouring billions of dollars into the economy."

Others look at the disparity between public and private retirement plans as an indictment of the private plans, not the public ones. Several national organizations have been pushing to increase retirement benefits for everyone.

"Everyone deserves a universal, secure and adequate retirement, and we need to start a dialogue to get there," said Rebecca Davis, legislative counsel for the **Pension Rights Center**.

Public pension projections

Even by the most optimistic projection, Ohio's state and local governments will need to come up with more than \$600 million in additional money by 2013 to pick up the tab for public employees' pensions. That assumes the payments increase by the same percentage over the next five years as they did over the past five. The total would reach nearly \$770 million if spending continues to increase by the same amount as last year alone. The figures do not include the employee share that some local governments pay for, nor proposed rate increases in the systems covering teachers and police officers/firefighters.

LOCAL GOVERNMENT SHARE		2011, WITH MOST OPTIMISTIC PROJECTIONS	2013, IF SPENDING INCREASES BY THE SAME AMOUNT AS 2008	RANGE OF POTENTIAL INCREASES
FUND	2008			
Ohio Police & Fire Pension Fund	\$402 million	\$467 million	\$480 million	16.2% - 19.5%
Public Employees Retirement System	\$1.84 billion	\$2.285 billion	\$2.232 billion	18.0% - 21.3%
School Employees Retirement System	\$437 million	\$489 million	\$514 million	12.0% - 17.0%
State Teachers Retirement System	\$1.467 billion	\$1.614 billion	\$1.688 billion	10.0% - 15.0%
TOTAL	\$4.146 billion	\$4.756 billion	\$4.914 billion	14.0% - 18.5%

NOTE: The retirement system for the State Highway Patrol is not included since local governments do not fund it.
SOURCE: Dispatch's computer analysis of data provided by state pension systems

THE COLUMBIAN DISPATCH FOR THE PLAIN DEALER

But with Ohio's public pension plan investments faltering in a rough economy and costs increasing because the funds also pay for retirees' health care — a benefit not mandated by state law — taxpayers may have to pour millions more into the retirement systems just to keep them afloat.

The **State Teachers Retirement System** and the **Ohio Police & Fire Pension Fund** are currently in violation of state law requiring them to have enough money to cover their pension obligations for 30 years. They are asking school districts, cities, counties and other local units of government to contribute more toward employee retirements. (They are asking more of the employees, too.)

Under the proposed changes, a full 29 percent of teacher salaries — 16.5 percent from school districts and 12.5 percent from teachers themselves — would go toward pensions. And 37 percent of police and fire employees' salaries — 25 percent from municipalities and 12 percent from employees — would be earmarked for retirement income.

Public vs. private: Plans hard to compare

It's often assumed that public-sector employees have it better than their private-sector counterparts where retirement is concerned.

But making direct comparisons is difficult because of the variability in retirement plans.

Virtually all government workers have defined-benefit pension plans, in which they and their employers contribute toward a multibillion-dollar pool of assets that are invested. When they retire, the employees get a fixed amount of money from that pool, based on their years of service and highest annual salaries.

In Ohio, the average state and local government retiree is paid \$25,736 a year. That's 7 percent more than the \$24,052 average

*pension for government retirees nationwide, according to the **Congressional Research Service**.*

Private-sector pensions and annuities average \$13,326, the research arm of Congress said. Slightly more than half of private-sector retirees supplement their pensions with income from Social Security, which averages \$12,699 a year.

Those are national figures. The research service did not break down its data by state.

Government employers in Ohio do not pay into Social Security, as pensions supplant the role of Social Security income for over-65 government retirees in the state.

That saves the school districts and other units of government the 6.2 percent of payroll that private employers pay into Social Security. Ohio is among eight states in which government retirees are fully exempt from Social Security taxes or benefits.

While nearly all government workers get defined-benefit pensions, private-sector employees are increasingly in 401(k) and other defined-contribution plans.

-- James Nash, The Columbus Dispatch

The increase doesn't sit well with some private-sector retirees, who have watched their own plans all but vanish.

"I think it's ridiculous," said Larry Rausch, 71, of Lancaster, who retired from a sales job at Sears in 1998, before the owner of Kmart purchased the retailer and slashed retirement benefits. "I don't know how they can expect guys like me to pay their retirement."

Many government retirees say pensions are part of their compact with their employers and, by extension, the public.

"We're trying to get away from calling it taxpayer money to calling it deferred compensation," said David Parshall, a retired Southwest Licking science and math educator who heads a statewide group of retired teachers.

Donna Seaman, who retired in 2002 from a 30-year career as a teacher and elementary school principal in Shelby city schools in northern Richland County, sees both sides of the issue.

School districts are hard-pressed to absorb increases in retirement costs without harming educational quality, yet teachers have come to rely on their pensions, said Seaman, whose daughter is a teacher.

"I don't expect that they will be able to have the same comfortable retirement that we have now — not that it's that comfortable," she said. "I'm very concerned about the stability of the system."

In some parts of Ohio, cities and schools pick up part or all of their employees' share of retirement costs, increasing the cost to taxpayers.

Columbus, for example, absorbs the full 10 percent city-employee share of retirements — at a cost of \$43 million a year to the city. Faced with a budget crunch, Columbus officials are attempting to scale back that benefit.

Status quo a no-go

The requests for more money from local governments by the State Teachers Retirement System and the Ohio Police & Fire Pension Fund are expected to go before state lawmakers early this year. But there's already resistance to sacrificing textbooks, police cars and staffing levels today for the long-term security of retirees tomorrow.

For some, it's politically unpalatable to benefit government pensions by heaping additional taxes onto people who have seen their own private-sector retirement plans slashed.

"Does the public-sector pension plan meet the expectations of the taxpayers who pay the bills?" asked Sen. Keith Faber, Republican of Celina and a member of the Ohio Retirement Study Council. "I think it's very difficult to ask the taxpayers to pay more money to support the systems."

Rep. Lynn Wachtmann, a Napoleon Republican who also sits on the panel, dismissed as outdated the argument that government employees deserve better retirement packages than their private-sector peers because they earn less pay.

"The taxpayers of Ohio who are footing the bill for all of this, in the end, need to realize how generous the public-pension systems — all of them — are compared to private-sector retirement plans," Wachtmann said. "Most of our private-sector employers would go bankrupt if they had to pay the kind of money into employee retirements that our public-sector employers do."

James D. DeCamp, Columbus Dispatch
Firefighters are among a group of government workers who enjoy extra perks, such as retiring at age 48 and going back to work, often at full pay for doing the same job. Wachtmann is one of nine voting members of the Retirement Study Council, which is made up of three state senators, three representatives and three appointees of the governor. It considers changes to the state's five public pension systems and makes recommendations to the legislature.

So far, the panel is not discussing the idea of following the private sector into 401(k)-type plans. But Tom Ash, lobbyist for the **Buckeye Association of School Administrators**, said the idea is being floated informally in some circles. He labels it a nonstarter.

"Our goal is going to be to preserve the defined-benefit plan because, as a matter of public policy, we think it makes sense," Ash said. "How do we do that is the question."

House Speaker Armond Budish, Democrat of Beachwood, acknowledged that the pension systems have "significant issues" with funding but said the state should strive to protect benefits for retirees.

Few local-government officials are chafing at how much they already contribute to employee pensions, but they're not thrilled with the prospect of an increase.

For example, Parma Superintendent Sarah Zatik said her school district could ill afford raising payments for retirees. The largest suburban system in the Cleveland area has cut \$6.5 million from its \$150 million budget and slashed 50 high school teachers after voters rejected four tax-increase requests in a row, most recently in November.

But underscoring the political sensitivity of the issue, Zatik wouldn't say whether existing retirement costs are too high. If she backs the pension plans, a district spokesman explained, the district would take

heat from residents angry over the costs. If she suggests trimming the plans, she would alienate teachers already facing cuts.

The Municipal League's Mahoney said his group will fight the proposed increases in pension costs.

"They want to take both police and fire up to 25 percent of payroll," he said. "In these times, well, good luck with that. There will be a prolonged and interesting discussion about all the changes everyone is talking about."

Indeed, politically powerful labor unions representing government workers figure to be influential in the debate.

They reject the idea of a fundamental crisis in the pension funds, saying the funding shortfalls can be remedied with a few tweaks — raising retirement ages here, boosting contributions from employers and employees there — and by counting on investment markets to rebound.

Ohio pension systems are relying on year-over-year investment growth of 7.5 percent to 8.5 percent.

"All classes of investors suffered during the market decline of 2008 — the largest downturn in 70 years," five unions representing the majority of government workers in Ohio said in a joint statement. "The long-term strategy and design of our retirement systems smooths gains and losses over a longer period of time, so [defined-benefit] plans are better able to reduce volatility. The same cannot be said of [defined-contribution] plans."

But the assumption of average 8 percent investment growth — without which the pensions may have to come back and ask for more tax money or slash benefits — seems overly rosy, said Leo Kolivakis, a pension consultant and writer.

"They're trying to inflate their way out of this problem," Kolivakis said.

AFSCME Ohio Council 8, OCSEA AFSCME Local 11, the Ohio Education Association, the Ohio Federation of Teachers and Service Employees International Union District 1199 say it would be folly for government employers to follow the lead of private companies into less-secure 401(k)-type retirement plans.

The unions cited statistics from the **National Institute on Retirement Security** that 357,234 retired government workers in Ohio received a total of \$8.41 billion in pension benefits from state and local pension plans in 2006, with most of that sum going back into the state's economy via purchases of medications, cars and other products and services.

"These dollars are vital to fuel Ohio's economic engine," the unions said.

That argument is less persuasive among private employers. In 1996, investments in 401(k)-type defined-contribution plans overtook traditional pensions, and the trend has accelerated since then, according to the Employee Benefit Research Institute.

The consulting firm **Watson Wyatt reported in October that the value of retirement benefits as a proportion of income had declined** from 7.8 percent in 2002 to 6.9 percent in 2008 among the 183 corporations it surveyed. Much of that decline was attributed to companies switching from guaranteed pensions to defined-contribution plans.

In contrast, retirement benefits account for at least 14 percent of payroll for all of Ohio's locally funded public pensions — topping out at 24 percent for firefighters in the Ohio Police & Fire Pension Fund.

Book and other defenders of public pensions say that government employees trade lower wages for more generous retirement plans.

But that's not necessarily the case. According to U.S. Department of Labor statistics, there is virtually no difference between private-sector and public-sector pay in Ohio.

But there is a difference in the willingness of private employers to take on the risk of having to bail out pension plans if investments go sour or costs increase sharply, said Alan Glickstein, a senior retirement consultant for Watson Wyatt.

Still, traditional pension plans actually generate more bang per investment buck because of the economies of scale of handling billions of dollars in retirement assets for tens of thousands of retirees, Glickstein said. Traditional pensions can offer the same level of benefits at 30 percent less cost than 401(k)-type plans, he said.

"It's almost impossible for a pension plan to be less efficient," Glickstein said.

Leaders of all five state pension systems say they're committed to maintaining retiree health care and full pension benefits over the long haul, even if some of the terms become less generous.

Michael Nehf, head of the State Teachers Retirement System, said keeping pensions for teachers is "extremely important." The alternative is welfare for some of his retirees.

The other major school pension system is taking a different approach.

The **School Employees Retirement System**, which represents nonteaching employees such as bus drivers and cooks, is not asking school districts to contribute more toward its employees' retirements, which average \$879 a month — far lower than their counterparts in the other state pension systems and below the federal poverty level. Some of the nonteaching employees are part time.

Forcing school districts to boost their contributions would invariably mean cutbacks elsewhere, such as eliminating busing, said James Winfree, executive director of the School Employees Retirement System.

"We understand the financial stress that school districts are under," he said.

Dispatch reporter Doug Caruso and Plain Dealer reporter Patrick O'Donnell contributed to this story. Dispatch Public Affairs Editor Darrel Rowland analyzed the data.

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Pension numbers

This is a breakdown of proposed changes offered by the pension systems: Proposals by the four pension systems to increase rates and make other moves to fix their budgets. The following are highlights of

the plans presented to the Ohio Retirement Study Council by the state's five public pension funds:

Ohio Public Employees Retirement System

Employee contributions: *No change to current 10 percent.*

Employer contributions: *No change to current 14 percent.*

Retirement eligibility: *Members with 32 years of service receive an unreduced pension at any age, up from 30 years of service, while members 67 and older with five or more years of service receive an unreduced pension, up from 65. The minimum age to retire and receive health care would be 55.*

Cost-of-living benefit: *Maintain current 3 percent rate, except in years when the Consumer Price Index increase is less than 3 percent.*

Final average salary: *Will be based on the five highest years of earning, up from three highest years.*

Pension calculator: *Maintain current 2.2 percent of final average salary per year of employment, but delay the increase to 2.5 percent from 30 years to 35 years of service.*

State Teachers Retirement System

Employee contributions: *Increase 0.5 percentage points each year starting in 2011 from the current 10 percent, rising to 12.5 percent by 2015.*

Employer contributions: *Increase 0.5 percentage points each year starting in 2016 from the current 14 percent, to 16.5 percent by 2020.*

Retirement eligibility: *Starting in 2015, members at any age with 35 years of service would receive an unreduced benefit. The same would be true for those at 60 with 30 years of service, and for those*

age 65 with five years of service. Members retiring at age 55 with 30 years or age 60 with five years would receive a reduced benefit.

Cost-of-living benefit: Starting in 2011, cost-of-living increases would be 2 percent per year for current retirees. Members retiring July 1, 2011, or later would receive a 1.5 percent yearly increase.

Final average salary: Would be based on the five highest years of earnings, starting in 2015.

Pension calculator: Starting in 2015, members' pensions would accrue 2.2 percent of their salaries for each of the first 30 years and 2.5 percent per year after 30 years.

Ohio Police & Fire Pension Fund

Employee contributions: Will increase from 10 percent to 12 percent over five years.

Employer contributions: Police employer contribution will increase from 19.5 percent to 24 percent over three years, to match fire employer rate. Then phase in an additional 1 percent contribution from both.

Retirement eligibility: Increase to age 52 for new hires, from 48 for those with 25 years of service.

Cost-of-living benefit: Delay until age 55, with the exception of survivors and beneficiaries.

Final average salary: Will be based on highest average salary from five years, up from three.

Pension calculator: No change.

School Employees Retirement System

Employee contributions: No change to current 10 percent

Employer contributions: No change to current 14 percent.

Retirement eligibility (for those who joined before May 14, 2008): A member must be 67 with 10 years of service credit or 57 with 30 years of service credit to retire with unreduced benefits, up from 65 with five years of service credit or any age with 30 years of service credit, respectively. A member may retire early at age 62 with 10 years service or age 60 with 25 years service and would receive reduced benefits, up from 60 with five years of service credit or 55 with 25 years of service credit.

Cost-of-living benefit: No change.

Final average salary: No change.

Pension calculator: No change.

Highway Patrol Retirement System

Employee contributions: Will increase from 10 percent to 11 percent.

Employer contributions: No change to current 26.5 percent rate.

Retirement eligibility: No change.

Cost-of-living benefit: Will decrease to 2 percent from 3 percent, with the exception of those 65 and older whose pension payment is 185 percent or less of the Federal Poverty Level. Eligibility for a cost-of-living adjustment will increase to age 60, from 53.

Final average salary: Will be based on a five-year period, up from three years.

Pension calculator: No change.

SOURCE: Pension fund reports

Pension costs swell amid deficit

By: [Joshua Sabatini](#)

San Francisco Examiner Staff Writer

January 4, 2010

As service cuts and layoffs are being utilized to slash the budget deficit San Francisco is facing, the hidden expense of health benefits and pensions for workers is skyrocketing, putting a strain on city coffers.

Ten years ago, about 23 percent of city workers' salaries were benefit costs. By fiscal year 2013-14, that percentage could grow to about 52 percent, according to a report from the Department of Human Resources. The City is looking at a cost of \$3 billion during the next 30 years for retiree health.

Health benefits for active workers, retiree health benefits and pension costs are also substantially outpacing the revenue growth of The City.

Ten years ago, San Francisco spent \$383.7 million on health insurance for active and retired workers, retirement contributions and Social Security. In the current fiscal year, that bill has risen to \$890 million, a 132 percent increase. Three years from now that bill could skyrocket to \$1.4 billion.

As San Francisco faces a \$522.2 million budget shortfall next fiscal year, Supervisor Sean Elsbernd and Mayor Gavin Newsom introduced a charter amendment in December that would overhaul the pension system — if approved by voters.

“Our constituents say to us, ‘Why do we have to keep raising fees, why do we have to consider taxes, why are we always cutting?’” Elsbernd said Dec. 15 when introducing the proposed ballot measure.

“This isn’t the only reason, but quite frankly, colleagues, this is a very significant reason. These costs are far exceeding our growth in revenue across the board,” he said.

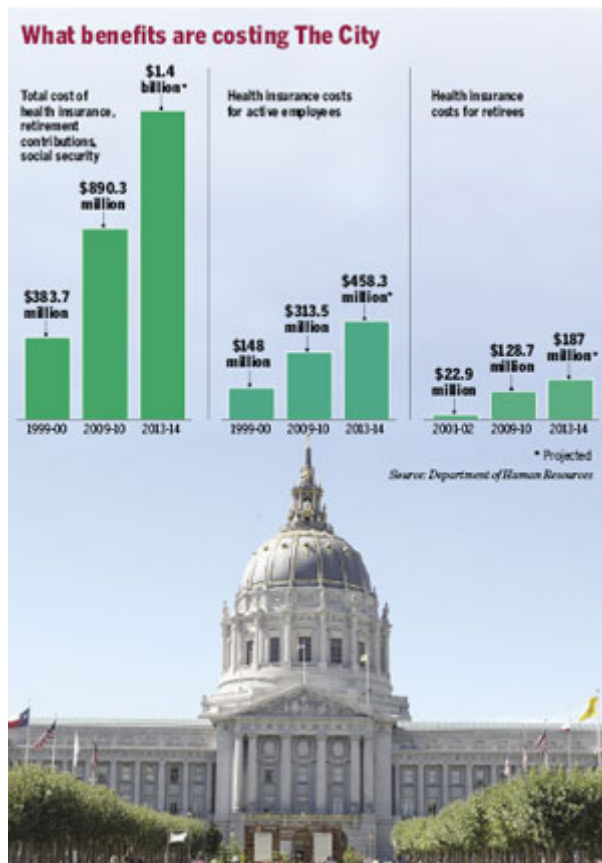
One factor contributing to The City’s pension cost increase is the pension investment fund took a 20 percent hit in 2008 when the economy plummeted. That led to The City having to contribute \$200 million to pension costs this current fiscal year. With the investment hit, The City was also looking at paying double that in three years, according to the most recent projections released in January 2009.

In the 1990s, the pension fund was performing so strong that The City did not have to contribute to the pension cost; the expense was covered by the fund’s investment earnings.

That grim outlook for pension costs, however, could brighten a little as the investment

portfolio is rebounding, said Steve Ponder, a manager with the Department of Human Resources. The next projection is expected in January. But there are no signs the projected ballooning health costs will decrease.

“Pension and other employee and retiree benefit costs continue to grow rapidly, and are one of the biggest challenges for The City’s long-term financial health,” said Newsom spokesman Brian Purchia.



Proposal would update payment system

A proposed charter amendment that would make several changes to the pension system for San Francisco would also establish a large set-aside — money that is required to be spent on a specific budget item.

If the proposal by Supervisor Sean Elsbernd and Mayor Gavin Newsom makes it onto the June ballot and is approved by voters, it would ensure all city workers contribute to pension cost. As well, it would increase newly hired public safety workers’ pension retirement contribution from 7.5 percent to 9 percent, and calculate pension using the average salary of the past 36 months of service, not just the last 12.

“This is a bill we must pay,” Elsbernd said. “There is no avoiding this bill.”

Perhaps the most significant component of the measure is that it would ensure The City starts socking away millions of dollars to address the retiree health cost liability.

Each year The City is told how much it has to fund in pension costs. Investment earnings from the pension fund are used to meet the obligation, and if they are short the money comes out of The City's operating budget. The obligation is about 9 percent, or \$200 million.

Under the ballot proposal, The City would always contribute the 9 percent from the city budget, and the money in excess would go into a fund to pay for retiree health care costs.

"The proposal by Mayor Newsom and Supervisor Elsbernd will set The City on a path to stabilize its pension costs and begin to address the large unfunded liability The City faces from employee and retiree benefit costs," Newsom spokesman Brian Purchia said.