Rhode Island's Retirement Security Act

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Background

- As of 2011, state and teacher pension plans were less than 50% funded
- Employer contributions were to increase from 22.4% of payroll in FY 2012 to 36.3% in FY 2013
  - Approximately 3/4 of increase due to changes in assumptions in rate of return and mortality rates
- Pension costs consuming larger share of resources
- State struggling to emerge from economic downturn and facing structural deficits in five-year forecast
  - No near term projection to grow out of the problem

Background

- Similar to other pension programs across the country, asset losses largest reason for declining funding ratios
- Investment earnings not meeting actuarial expectations
  - Recent revisions assume 7.5% investment return; a decrease from 8.25% through 2011
- Demographic experiences exceeded actuarial assumptions
  - Retirees were retiring earlier, living longer
  - Employee salary growth larger than anticipated in assumptions used to calculate costs

Pension Reform – Did Not Happen Overnight

- Rhode Island had already implemented a series of reforms, including:
  - Retiree health care reform
  - Retirement age adjustments
  - COLA modifications
- However, these reforms were not sufficient to close the growing gap between public pension obligations and available resources

Pension Reform – Path to Success

The Governor, the President of the Senate, the Speaker of the House and the General Treasurer recognized that action was necessary to protect pension plans in an affordable way.

- Publically committed to comprehensive reform in a Special Session in November 2011
- Outlined a public information plan to educate elected officials, members of the pension plans and taxpayers

Pension Reform – Path to Success

- Clearly articulated that solutions will require shared sacrifice among retirees, existing employees and taxpayers
- Established ongoing communication to work the issue through the summer and into the Special Session
- Assigned fiscal staffs to work together to develop alternatives for Leadership to consider

Pension Reform – Path to Success

- In June 2011, the General Treasurer released a report entitled "Truth in Numbers" that:
  - Estimated the costs for past practices and benefit plans
  - Diagnosed the key drivers of the structural pension deficits
  - Outlined the implications of further inaction
  - Provided a framework for solutions
- General Treasurer led Retirement Board's efforts to revise the rate of return assumption down from 8.25% to 7.5%
- Provided a series of briefings to both chambers of the General Assembly

Pension Reform – Path to Success

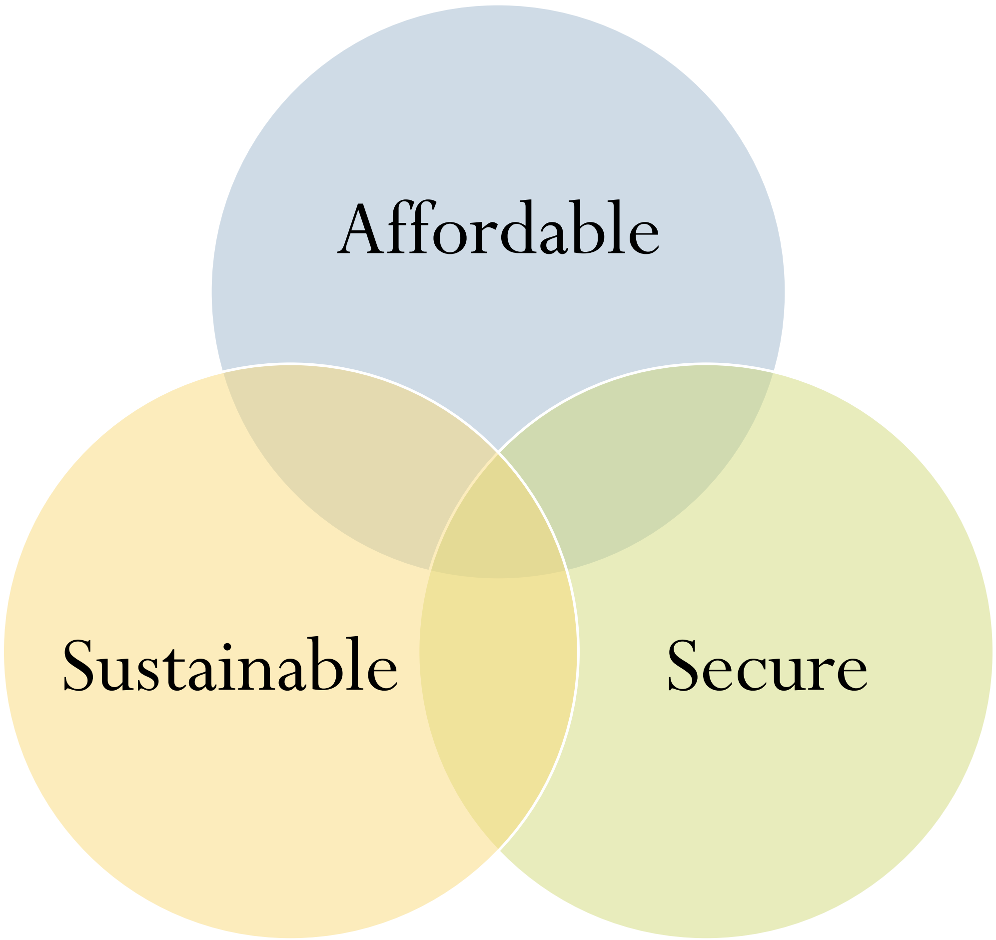
To ensure elected officials were prepared to take action, State leadership embarked on a process to educate elected officials, members of the pension programs and taxpayers about the deterioration of the public pension programs. This included:

- Joint Legislative meetings to learn about pension programs, the funding status of plans across the country and potential actions to consider
- Pension Advisory Group – 12 member advisory body included local and national experts on pension reform

Pension Reform – Path to Success

- Prior to the Special Session, the General Assembly invited and heard from national experts on pension issues, including Kil Huh from Pew Center on the States and Diane Oakley of National Institute on Retirement Security
- Three joint Finance Committee Meetings included fiscal staff briefings on existing pension plans and how they work
- Three joint Finance Committee Meetings to take public testimony, resulting in nearly 30 hours of public testimony over the three day period

Goals of Reform



Summary of Reform

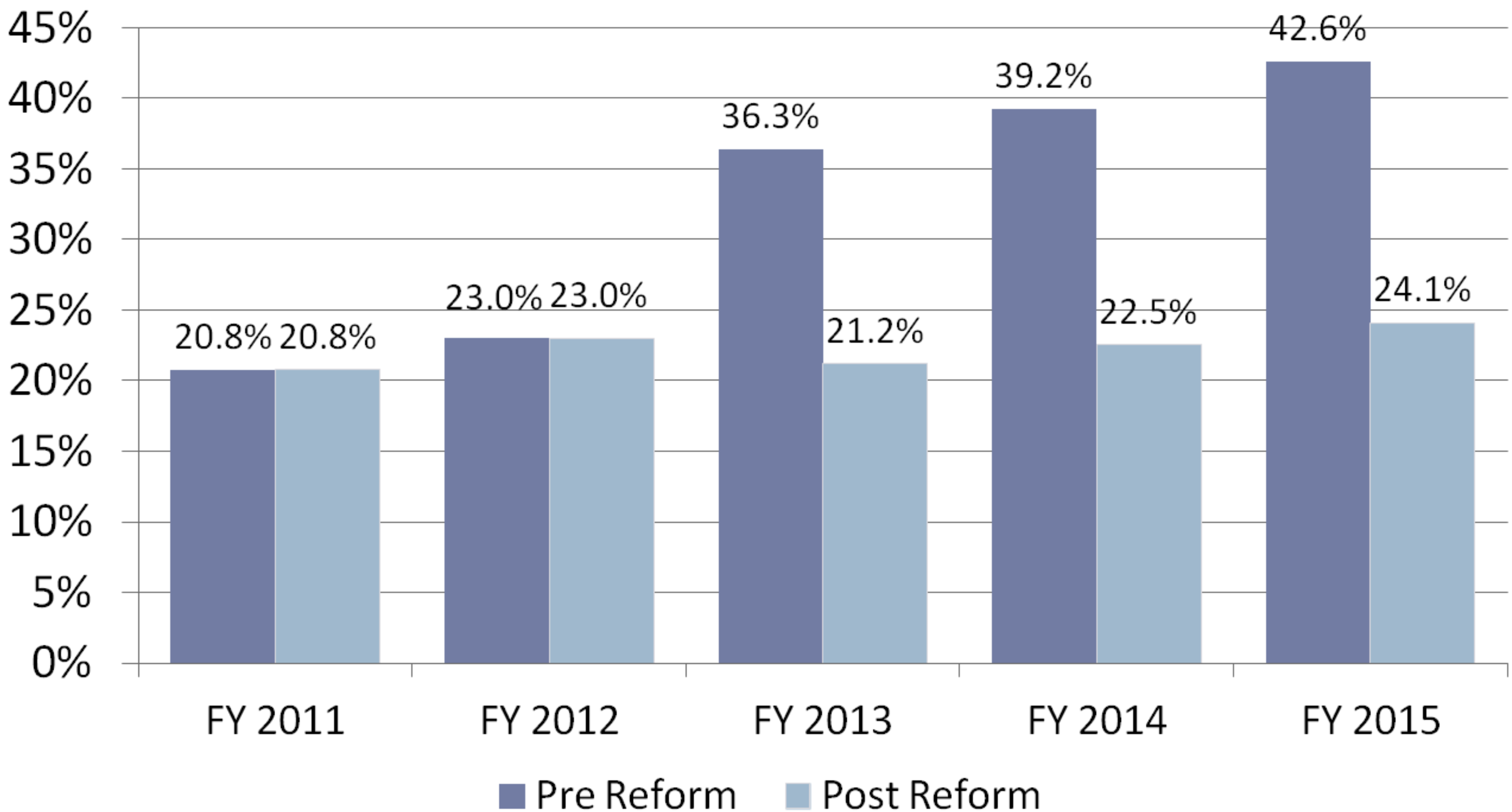
- Reduces state's unfunded liability by over $3.0 billion and funded ratio immediately returns to 60%
- Preserves benefits earned through June 30, 2012
- Increases minimum retirement age for most employees <u>not already</u> eligible to retire
- Moves all but public safety employees and judiciary to hybrid pension plan
- Suspends COLA until system better funded and provides an intermittent COLA every five years until 80% funded
- Begins addressing local pension plan solvency issues

Impact on State

Employer Retirement Contributions (all funds)

	Pre Reform	Post Reform	Change
FY 2013	$406.8	$235.9	($170.8)
FY 2014	$442.9	$234.7	($208.1)
FY 2015	$488.2	$258.8	($229.5)
FY 2016	$521.6	$276.4	($245.1)
$ in millions			

State (Employer) Contribution Impact



% of salary - State employees only

Funded Ratio Impact

	Pre Reform	Post Reform	
Group	FY 2013	FY 2013	Change
State Employees	48.4%	59.8%	11.4%
Teachers	48.4%	61.8%	13.4%
Judges	77.8%	81.6%	3.8%
State Police	69.7%	90.0%	20.3%
MERS – General	74.8%	87.6%	12.8%
MERS - Public Safety	70.7%	86.2%	15.5%

Unfunded Liability Impact

	Pre Reform	Post Reform	Change	
	FY 2013	FY 2013	Amount	Percent
State Employees	$2,700.0	$1,701.9	$(998.1)	-37.0%
Teachers	$4,133.0	$2,392.2	(1,740.8)	-42.1%
Judges	$11.0	$8.6	(2.4)	-21.8%
State Police	$29.0	$7.3	(21.7)	-74.8%
Total	$6,873.0	$4,110.0	$(2,763.0)	-40.2%

$ in millions

Plan Design Changes

- Cost of Living Adjustments
- Specific Employee Groups
  - State Employees and Teachers
  - MERS General Employees
  - State Police
  - Judges
  - MERS Police and Fire

Pre Reform - Cost Of Living Adjustments

Group	Rate	Type	Start	Application
Retirees – State Emp. & Teachers	3%	Compound	3^{rd} Jan. after retire	Full Benefit
Active – State Emp. & Teachers	CPI up to 3%	Compound	Later of 3^{rd} anniv. or age 65	First $35k indexed to CPI
Judges	3%	Simple ex. for Traffic & W. Comp	3^{rd} Jan. after retire	Full benefit ex. for non-eligible limited to $35k
State Police	$1,500	Flat	3^{rd} January	n/a
MERS (Optional)	3%	Simple	1^{st} anniv.	Full Benefit

Post Reform - Cost of Living Adjustments

COLA Provisions – Applies to All Groups	
Risk Based:	7.5% - 5.5% = 2% average
COLA applied to:	Applied to only the first $25,000 of benefit, indexed
COLA limits:	0.0% to 4.0%
COLA - Annually	80.0% funding
COLA - Interim	Every five years, risk based calculation
COLA Funding Test	State plans are blended, MERS stay separate

State Employee/Teacher Hybrid Plan

- No change to state employee contribution rate of 8.75% however, 3.75% of this contribution now goes to the defined benefit program and 5.0% goes to a new defined contribution program
- Reduces teacher contribution rate from 9.5% to 8.75%, with 3.75% of this contribution going to the defined benefit program and 5.0% to a new defined contribution program
- Reduces vesting requirement from 10 years to 5 years for DB component and calculates benefits on 5-year highest average compensation
- Revised benefit accruals to 1.0% per year of service beginning July 1, 2012

Transition Language

- For employees with at least five years of service on July 1, 2012, new retirement age is discounted proportionally based on how close they are to retirement as of June 30, 2012
  - The closer employees are to the pre reform retirement age, the fewer additional years get added to that retirement age
  - The new age can be no lower than 59
- Members with at least 10 years of service on June 30, 2012 may elect to retire with benefits accrued as of June 30, 2012 at their current retirement age

State Employee/Teacher Contribution Rates

Group	Pre Reform	Post Reform			
		DB	*DC*	*Suppl.*	*Total*
State Employee	8.75%	3.75%	5.0%	n/a	8.75%
Teacher w/Soc. Sec.	9.5%	3.75%	5.0%	n/a	8.75%
Teacher w/o Soc. Sec.	9.5%	3.75%	5.0%	2%	10.75%

Municipal Employees' Retirement System (MERS)

- Covers various local employees – general municipal, police and fire
- 110 State Administered Plans (43 are public safety plans)
- Total assets of $1.2 billion as of June 30, 2010
- Unfunded Actuarial Accrued Liability of $430.2 million as of June 30, 2010
- Funded ratio of 73.6% as of June 30, 2010
- <u>Reform increases overall funded ratio to 87.6%</u>

MERS General Employees Hybrid Plan

- Reduces contribution rates from 6.0% to 1.0% (7.0% to 2.0% for those electing the COLA provisions)
- Reduces vesting requirement from 10 years to 5 years for DB component
- For DC component, employees vest immediately, but three-year vesting for employer contributions
- Benefits calculated based on the member's 5-year highest average compensation
- Benefit accruals of 1.0% per year of service beginning July 1, 2012

MERS Public Safety

- Reduces contribution rates from 9.0% to 7.0% (8.0% for those electing the COLA provisions)
- Requires 25 years of service or age 55 with 10 years to retire with full benefits, with 2.0% benefit accrual rate
- Reduced eligibility requires 20 years of service or age 50
- Reduces vesting requirement from 10 years to 5 years for DB component
- Benefits calculated based on the member's 5-year highest average compensation

Employee Contribution Rates: MERS Employees

Group	Basic	Optional	Post Reform			
			DB	*DC*	*Suppl.*	*Total*
General	6%	7%	1-2%	5%	n/a	6-7%
Public Safety w/Soc. Sec.	7-8%	8-9%	7-8%	n/a	n/a	7-8%
Public Safety w/o Soc. Sec.	7-8%	8-9%	7-8%	n/a	3%	10-11%

Impact on Municipalities - FY 2013

Contributions (millions)	Pre Reform		Post Reform (FY 2013)		
	FY 2012	FY 2013	DB	DC	Total
MERS Municipal	$20.4	$40.9	$25.3	$2.2	$27.4
MERS Police & Fire	$12.8	$24.8	$9.6	$1.0	$10.6
MERS Subtotal	**$33.1**	**$65.7**	**$34.9**	**$3.2**	**$38.1**
Teachers	$134.2	$221.0	$120.7	$16.2	$136.9
Total MERS/Teachers	**$167.3**	**$286.7**	**$155.6**	**$19.3**	**$175.0**

$ in millions

Other Issues

- Act proposes to re-amortize remaining unfunded liability over a 25-year period
- Provides for "laddered" re-amortization designed to smooth out the cliff effect and reduce volatility over a long period of time
- Reduces liability without using pension obligation bonds as a funding mechanism given associated risk

Other Issues

Self-Correcting Mechanism

- Creates a trigger to indicate need for course correction
- Trigger = if plan under 50% funded and experiences 5 years of decline in funded ratio
- Action = A default plan which cannot include further benefit reductions, only increased contribution rates
- Risk adjusted COLA

Locally Administered Pension Plans

- 36 plans within 24 municipalities, of which half cover public safety employees with $2.1 billion unfunded liability and an overall funded ratio of 40.3%
- Not governed by state law - municipality is entirely responsible for administration and funding the plans
- May be included in collective bargaining agreements

Locally Administered Pension Plans

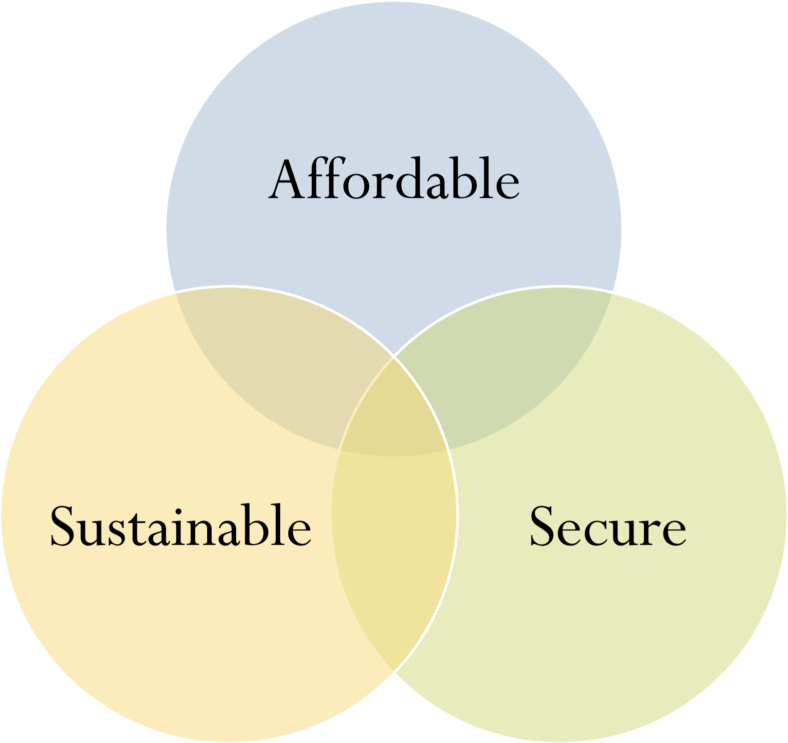
Reform requires Locally Administered Plans to:

- Conduct actuarial and experience studies by April 1, 2012
  - A majority met the deadline
  - To date, all but three plans have submitted updated studies
- Submit funding improvement plans if deemed to be in critical status (<60% funded) to commission with state and local representation
- RIRSA also established the Locally Administered Pension Study Commission, which is currently working to develop recommendations for municipalities

Key Takeaways from RI Pension Reform

- The General Assembly found that RI had one of the lowest funded and most vulnerable pension systems in the country
- Reforming and ensuring the long term sustainability of the pension plans was deemed central to protecting the public interest of the state
- Reforming public pension plans was deemed critical to protect the plans for members
- Pension reform resulted in solvent, sustainable and affordable pension systems
- Although RIRSA begins to address independent local plan solvency issues, there is still work to be done

Goals of Reform



Reform:

- Reduces state's unfunded liability by over $3.0 billion
- Dampens growth in employer contribution as a percent of payroll in out-years
- Prevents future erosion of the state's pension systems and protects expected benefits