Testimony on Senate Resolution 7 and House Resolution 8

Submitted by Suzanne Bates, Policy Director

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Good morning Senator Formica, Senator Osten, Representative Walker and Representative Ziobron.

My name is Suzanne Bates. I am the policy director for the Yankee Institute for Public Policy, a Connecticut-based free market think tank.

I am here to discuss our views on the agreement between the State of Connecticut and the State Employees Bargaining Agent Coalition.

The agreement includes some positive steps forward, including lowering the discount rate from 8 percent to 6.9 percent. This gives us a truer picture of how expensive our past and current pension benefits are for taxpayers. However, the reduction does not go far enough. Our discount rate is supposed to be tied to the rate of return we receive on our pension investments, and yet for the past fifteen years we've averaged only 5.5 percent returns.

The federal government, under ERISA rules, requires that private pension plans have discount rates between 1.8-5 percent. This is to protect investors as well as beneficiaries. Why isn't the state of Connecticut similarly protecting taxpayers? Beneficiaries of public pensions are automatically protected both because states can't declare bankruptcy and because court opinion has weighed heavily in favor of protecting existing pension benefits. It would be much safer for the state to set a rate that valued future benefits honestly, and protected taxpayers from growing liabilities.

Another positive step is moving to a level dollar instead of a level percent of payroll amortization. This would provide greater stability for taxpayers in the long run.

We are concerned about shifting liabilities onto future taxpayers by extending the amortization period out over 30 years instead of 14.

Above all, I want to share our concern that this agreement is being misconstrued as "pension reform." This is not pension reform. Under this agreement the state would essentially be refinancing its mortgage, but still living in a house that is too expensive.

We have a paper coming out next month that lists 10 solutions for reforming our pension system. We hired an actuary to build a model to determine the cost savings from some of these solutions. The solutions include:

1. Lowering the discount rate to 5 percent.
2. Increase employee contribution rates to the national average of 6 percent. This would reduce taxpayer contributions by $4.3 billion over 30 years.
3. Adopt a cap on the compensation eligible for pension benefit determination. Applying a cap of $100,000 for new hires would reduce employer contributions by $4.1 billion over 30 years.
4. Change the formula for cost of living adjustments so that the maximum is 2 percent. This would save $1.3 billion over 30 years.
5. Change the definition of compensation to remove overtime.
6. Create a new Tier IV Defined Benefit Plan with greater cost sharing and reduced benefits.
7. Move instead to a Cash Balance Plan that would guarantee a fixed investment return for individual employee accounts plus revenue sharing for years with big returns.
8. Move all new employees into a Defined Contribution Plans.
9. Move all new employees into a hybrid defined benefit/defined contribution plan.
10. Give new hires the choice between a hybrid plan or DC plan only.

In addition, it is important that the legislature takes a look at how the state is setting its pension benefits, and how the pension funds are governed. All of our neighboring states, and the vast majority of states across the country, set their benefits by statute instead of through collective bargaining. For too long the legislature has been shut out of state employee compensation discussions. This should change. This is not far fetched. Connecticut already sets teacher pensions by state statute.

In terms of the governance, currently the pension fund is governed by a board that is half labor appointees and half executive branch appointees. The legislative branch – those closest to the taxpayers, who ultimately bear the full risk of these benefits – is left out. We believe that should be remedied.