



Presentation on Connecticut Pension Fund Issues

Benjamin Barnes, Secretary
Office of Policy and Management
October 5, 2016



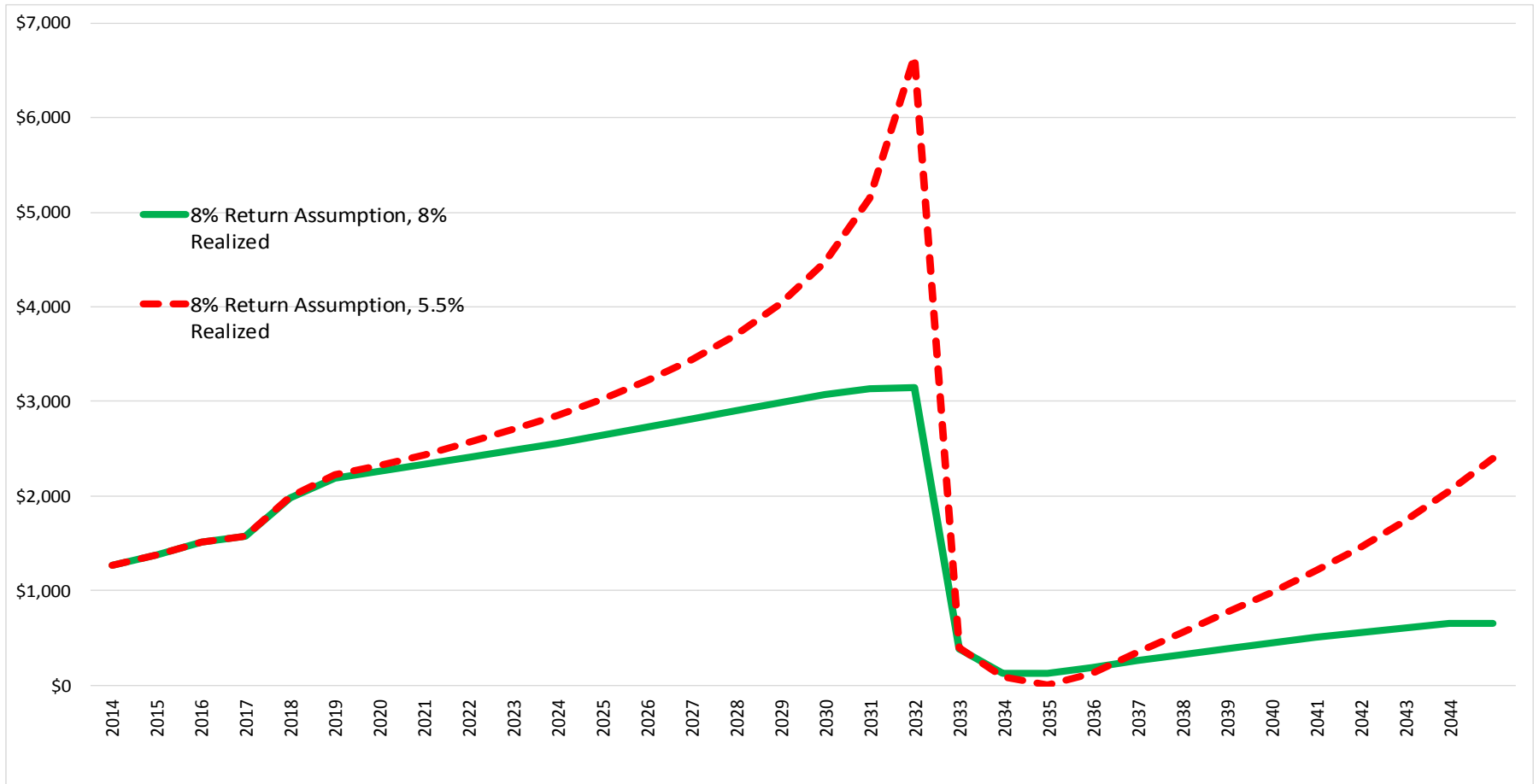
Connecticut's Pension Systems

- Connecticut's state employee and teacher pension plans have promised benefits to members for many years
 - Both systems began in 1939, but actuarial funding did not begin for SERS until 1971 and TRS until 1982
 - Pre-funding was phased in over more than a decade
 - Before then, benefits were paid out of the State's general revenues each year
- While Connecticut faces challenges in funding its currently underfunded pension plans, progress has been made since 2011 to better-fund both SERS and TRS



Projected SERS Contributions

(in millions)





Fixing Our Pensions - SERS

Recent steps to address SERS liability include:

1. The 2011 SEBAC agreement:
 - a) Reduced the minimum pension COLA and doubled the early retirement reduction factor
 - b) Increased the age for normal retirement eligibility by 3 years for all non-hazardous duty employees who retire after July 1, 2022
 - c) Created a new Tier III for employees hired on/after July 1, 2011
2. In 2012, certain provisions (part of SEBAC IV and V agreements) which artificially reduced required contributions were eliminated
2. In 2012 more conservative actuarial assumptions were adopted, including lowering the assumed rate of investment returns from 8.25% to 8%
3. The state has budgeted its full required contribution since FY 2012
4. As a result, budgeted SERS contributions have grown from \$944 million in FY 2011 to \$1,569 million in FY 2017
5. In 2015, OPM engaged the Center for Retirement Research at Boston College to assess both SERS and TRS and devise a set of actions for consideration
6. Additional analyses have been undertaken by the State Comptroller and State Treasurer



Fixing Our Pensions - TRS

The Teachers' Retirement Board has taken the following steps toward a more sustainable pension plan:

- Reduced the assumed rate of return from 8.5% to 8.0%;
- Adopted more conservative mortality and other assumptions;
- Increased the state's contributions to the plan; and
- Directed the plan actuary to develop additional funding strategies that could be implemented in order to limit the volatility of future contributions



Major Reasons for Pension Underfunding

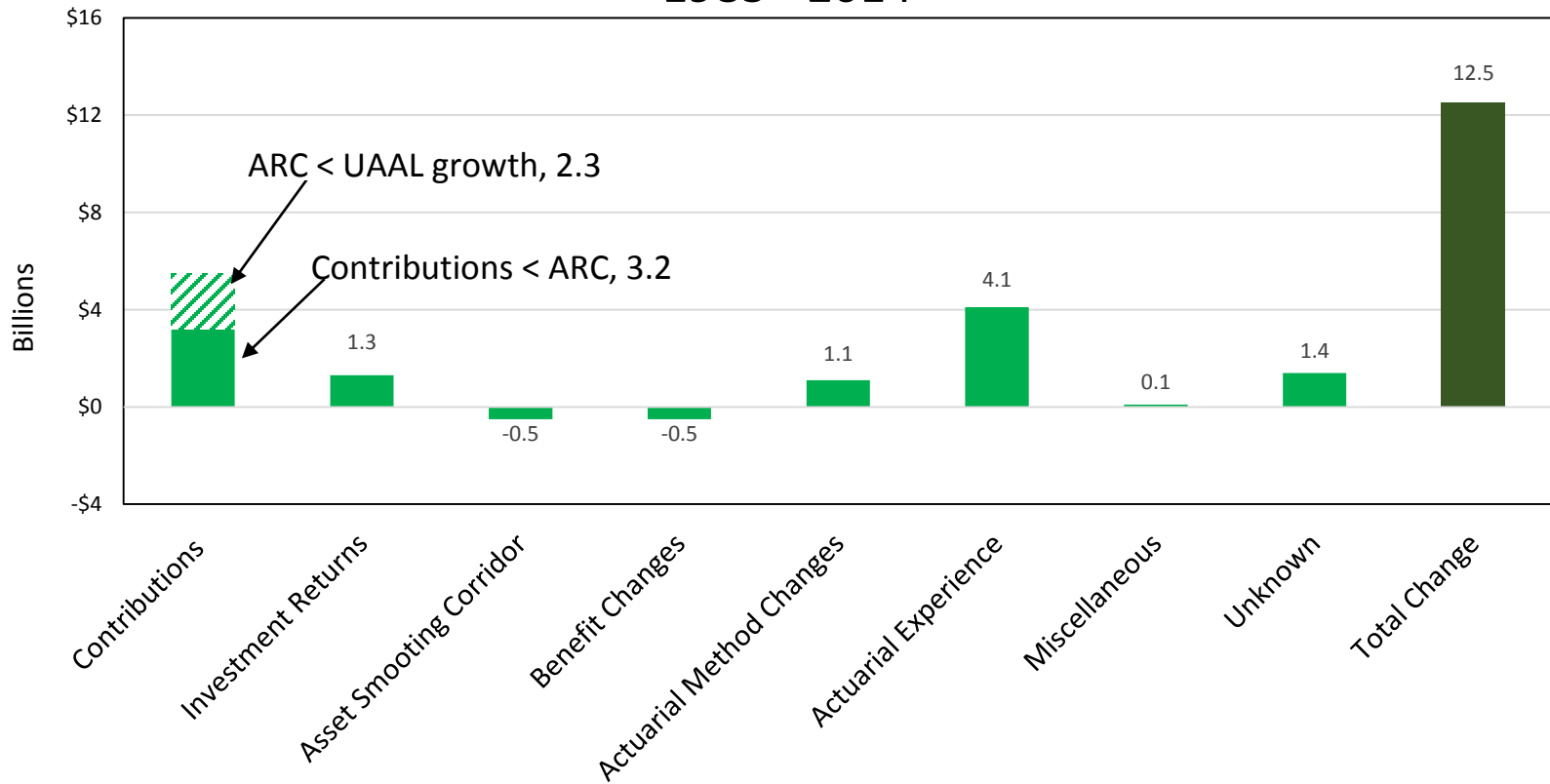
The BC report identified four factors that underlie the current underfunded status of the pension funds for state employees (SERS) and teachers (TRS):

1. Legacy costs from benefits promised before the systems were prefunded
2. Inadequate contributions once the state decided to prefund
 - a. Initially a ramp-up period
 - b. Switch from level dollar to level percent of payroll amortization (resulted in back-weighting of contributions)
3. Assumed rate of return exceeded realized rate of return on investments
4. For SERS, poor actuarial experience relative to expectations
 - a. Retirement incentives may have contributed to this underperformance relative to actuarial assumptions



Fixing Our Pensions

SERS - Sources of Changes to the Unfunded Accrued Actuarial Liabilities (UAAL) 1985 - 2014



Source: Final Report on Connecticut's State Employees Retirement System and Teachers' Retirement System, by CRR



Proposed Reforms

- In early 2016, the Governor convened a workgroup:
 - Office of Policy and Management,
 - Office of the State Comptroller,
 - Office of the State Treasurer, and
 - Organized labor
- The workgroup, working with the plan actuaries, recommended the following strategies for SERS:
 - Continuing to pre-fund all liabilities on an actuarial basis
 - Reducing the assumed rate of return from 8% to 7%
 - Transitioning from level percent of payroll to a level dollar amortization for unfunded liabilities (removes some back-weighting of contributions)
 - Transitioning the actuarial cost method from Projected Unit Credit to Entry Age Normal
 - Maintaining the current 2032 date for amortization of those liabilities that existed when the current 40-year amortization schedule was first enacted
 - Transitioning to multiple fixed amortization schedules for new liabilities consistent with the model funding approach developed by the Conference of Consulting Actuaries
- OPM is in negotiations with SEBAC to implement a package of reforms in the coming biennium



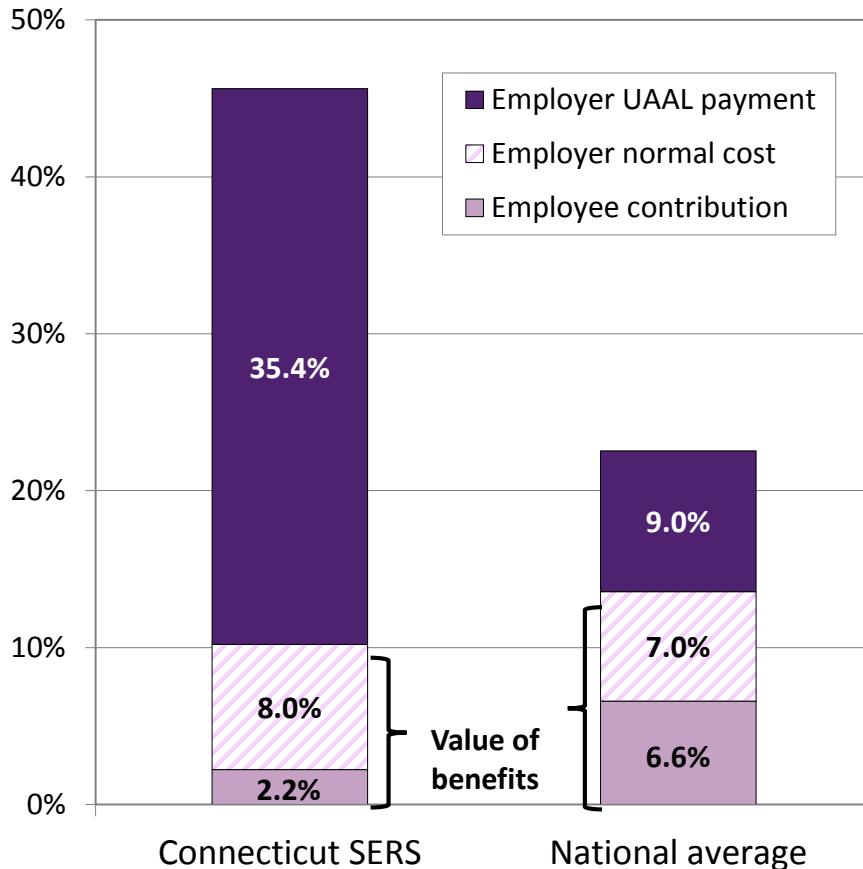
Many Factors Determine the ADEC

- There are many actuarial, economic, and demographic assumptions that are used to calculate the actuarially determined employer contribution (ADEC) to a pension fund
- The choice of assumptions will vary depending on the intended use of the numbers
 - CAFR reporting (follows GASB rules)
 - Funding policy (budget)
 - External evaluations (e.g., credit rating agency approach to establish comparability across governmental units)
- The core objectives for a funding policy should include:
 - Accumulation of assets needed to pay promised benefits
 - Stability and predictability of cost
 - Intergenerational equity

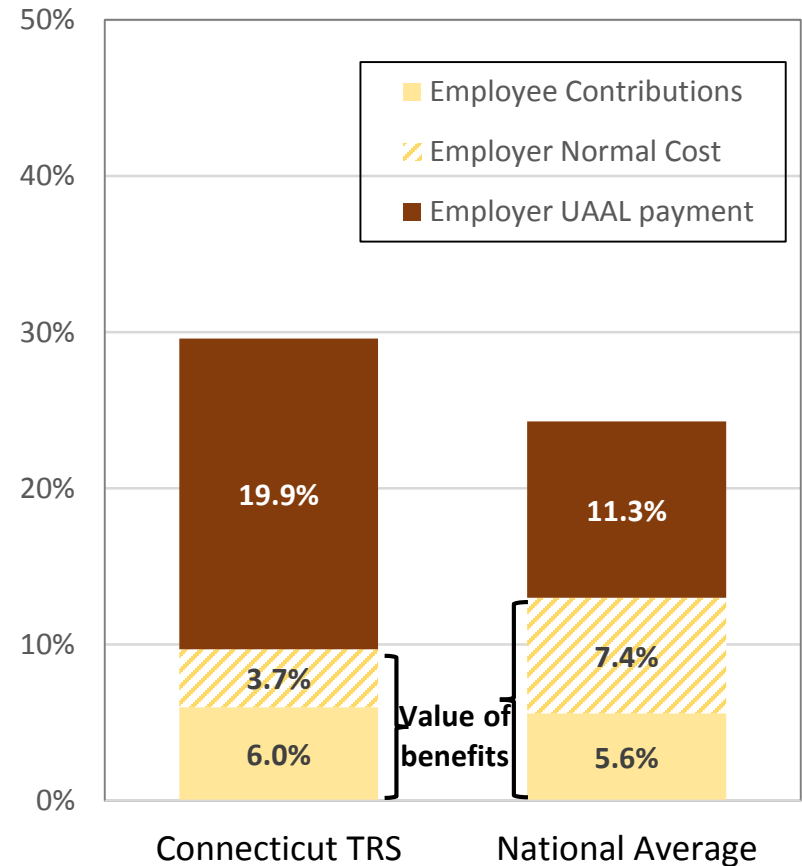


Actuarial Costs as a Percent of Payroll

State Employees Retirement



Teachers Retirement



Source: Final Report on Connecticut's State Employees Retirement System and Teachers' Retirement System, by CRR



Question for the Spending Cap Commission

1. Is any component of the state's pension liability an "evidence of indebtedness"?
2. Ratings agencies generally consider pension liabilities to be debt-like
For example, Moody's states, "In assessing long-term liabilities we treat pension liabilities as a form of debt."
3. Inclusion or exclusion of pension contributions from the cap does not impact the requirement that the state pay its ADEC, *however:*
4. Inclusion under the cap may limit the State's ability to implement a more rapid pay-off of these liabilities, and
5. Treating the state's unfunded accrued liability as a cap-exempt evidence of indebtedness decreases the possibility that future pension holidays will be proposed as a tool to achieve short-term expenditure cap compliance when other budget components are growing faster than the cap



Cap Room and Pension Growth

Fiscal Year	SERS+TRS+JRS		
	Allowable Capped Growth (in millions)	State Contribution Growth (in millions)	State Contributions as a % of Allowable Growth
2006	\$ 464.5	\$ 317.5	68.3%
2007	476.7	57.6	12.1%
2008	431.0	156.1	36.2%
2009	655.4	8.7	1.3%
2010	885.0	26.8	3.0%
2011	680.7	128.0	18.8%
2012	532.4	290.1	54.5%
2013	485.9	163.9	33.7%
2014	261.1	372.3	142.6%
2015	258.8	139.4	53.9%
Avg.	\$ 513.2	\$ 166.0	32.4%

Questions?