# Iowa's Defined Benefit Public Pension Plans "101"

| Plan | Member Groups | Number of Members | Max. % Avg. High Salary | Min. Age Eligible for Max. Benefit |
|---|---|---|---|---|
| IPERS | Cities, counties, schools | 342,000 | 65% (Regular Members) | Age 62 (Regular Members) |
| Municipal Police and Fire* | 49 largest cities | 3,862 | 82% | Age 55 |
| State Troopers* | State troopers | 1,200 | 88% | Age 55 |
| Judicial | Judges | 386 | | |

* Members in these plans do not contribute to nor receive social security from their public employment.



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# Benefits Must Be Paid No Matter What Happens With Investments or Contributions

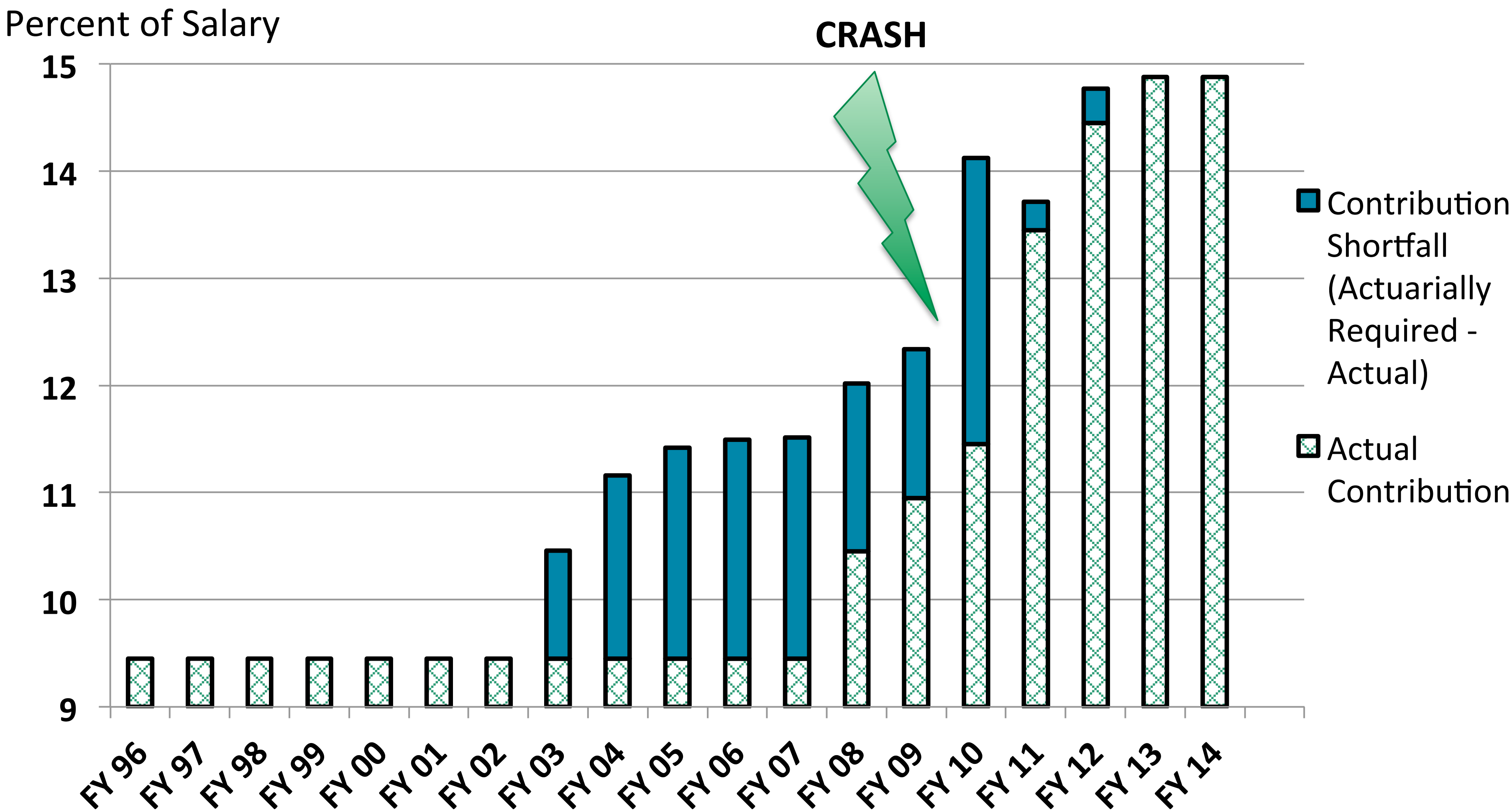

*If investment returns fall, contributions must go up.*

*If contributions don't keep up, debt accumulates.*

Much hinges on the choice of assumptions and methods. Iowa plans assume a long-term annual rate of return of 7.5%*

* Peace Officers Retirement Plan assumes 8%.

# IPERS Contributions Were Not Keeping Up With Actuarial Requirements Even Before the 2008 Market Crash



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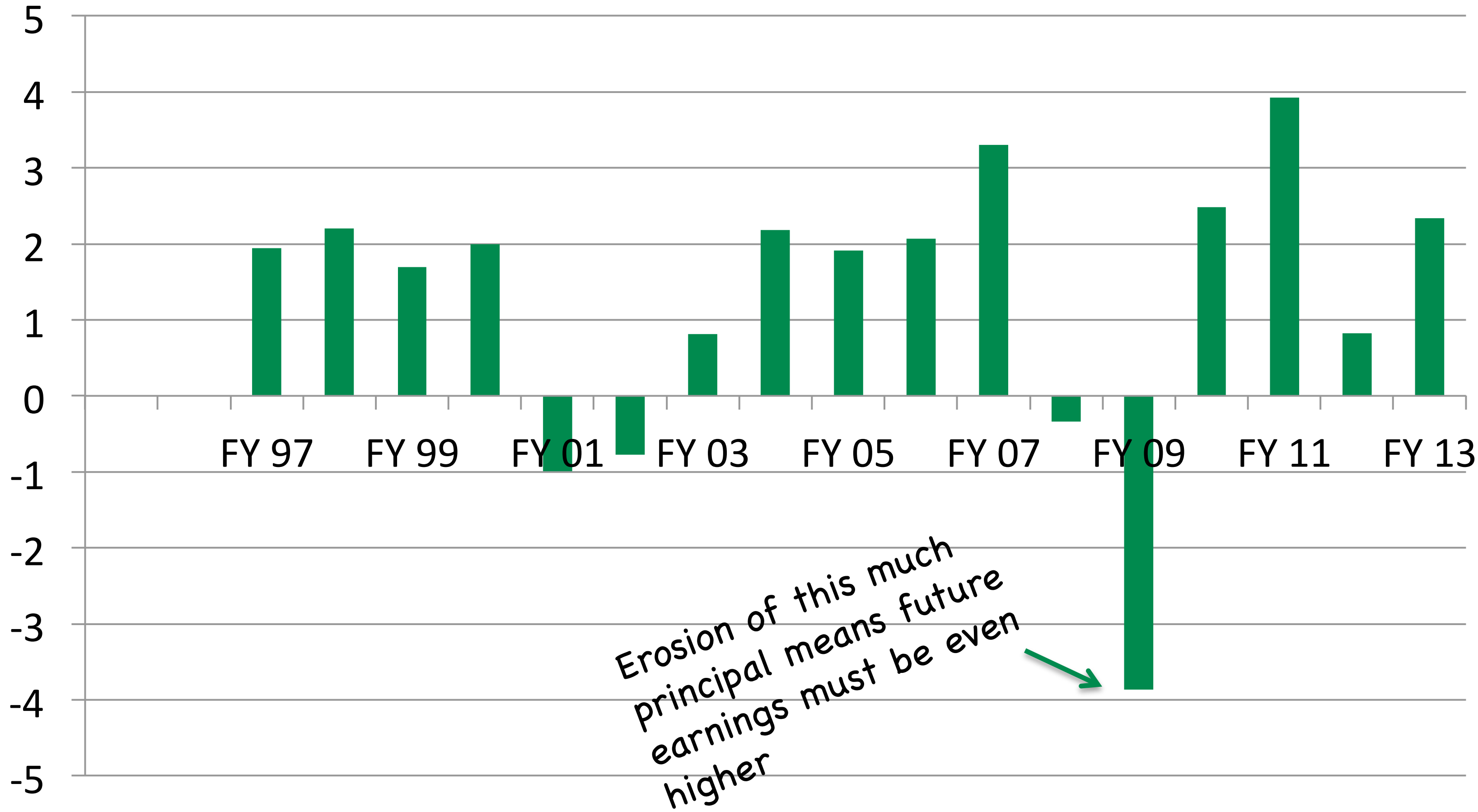
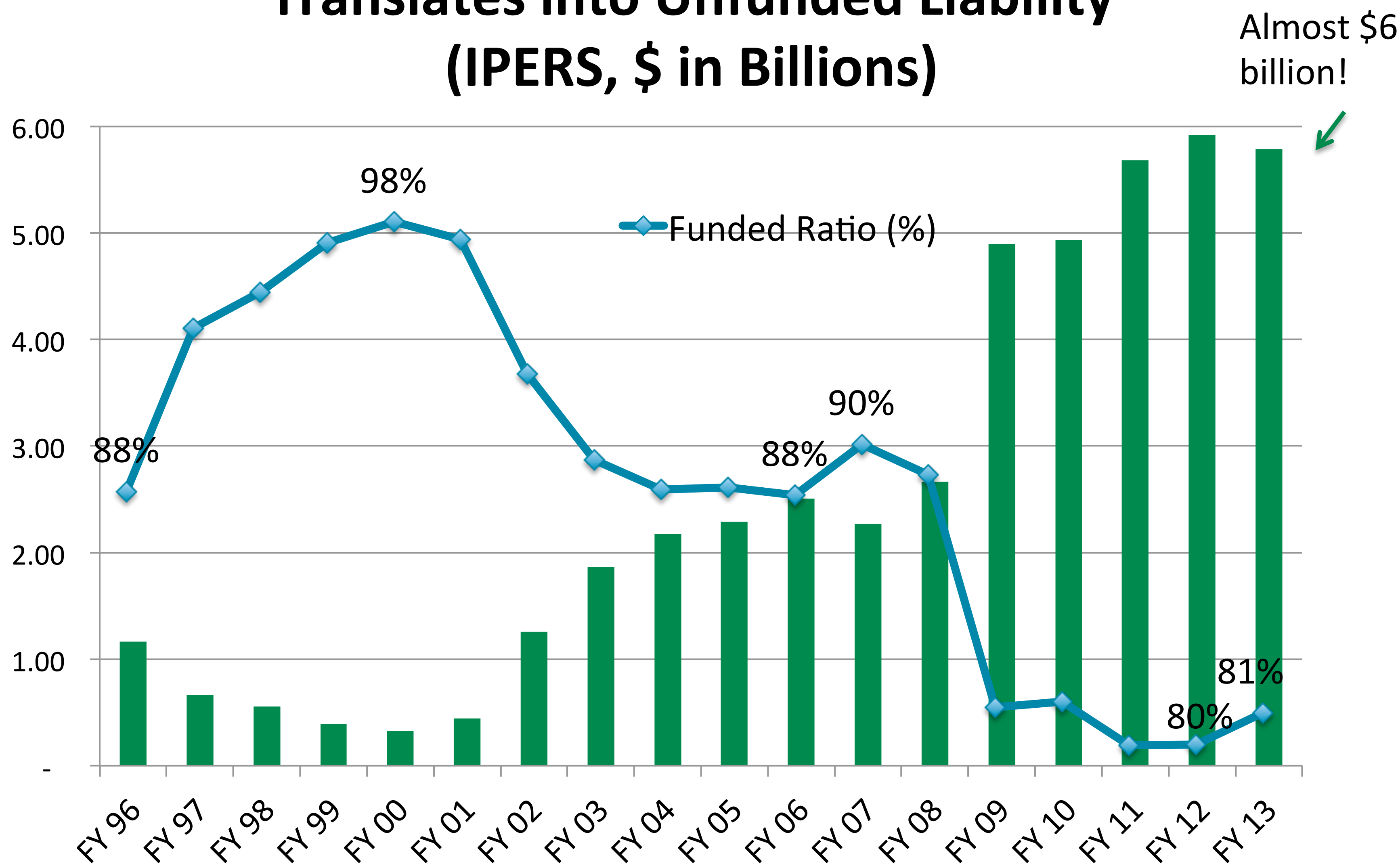
# IPERS Net Investment Income/Loss ($ in Billions)



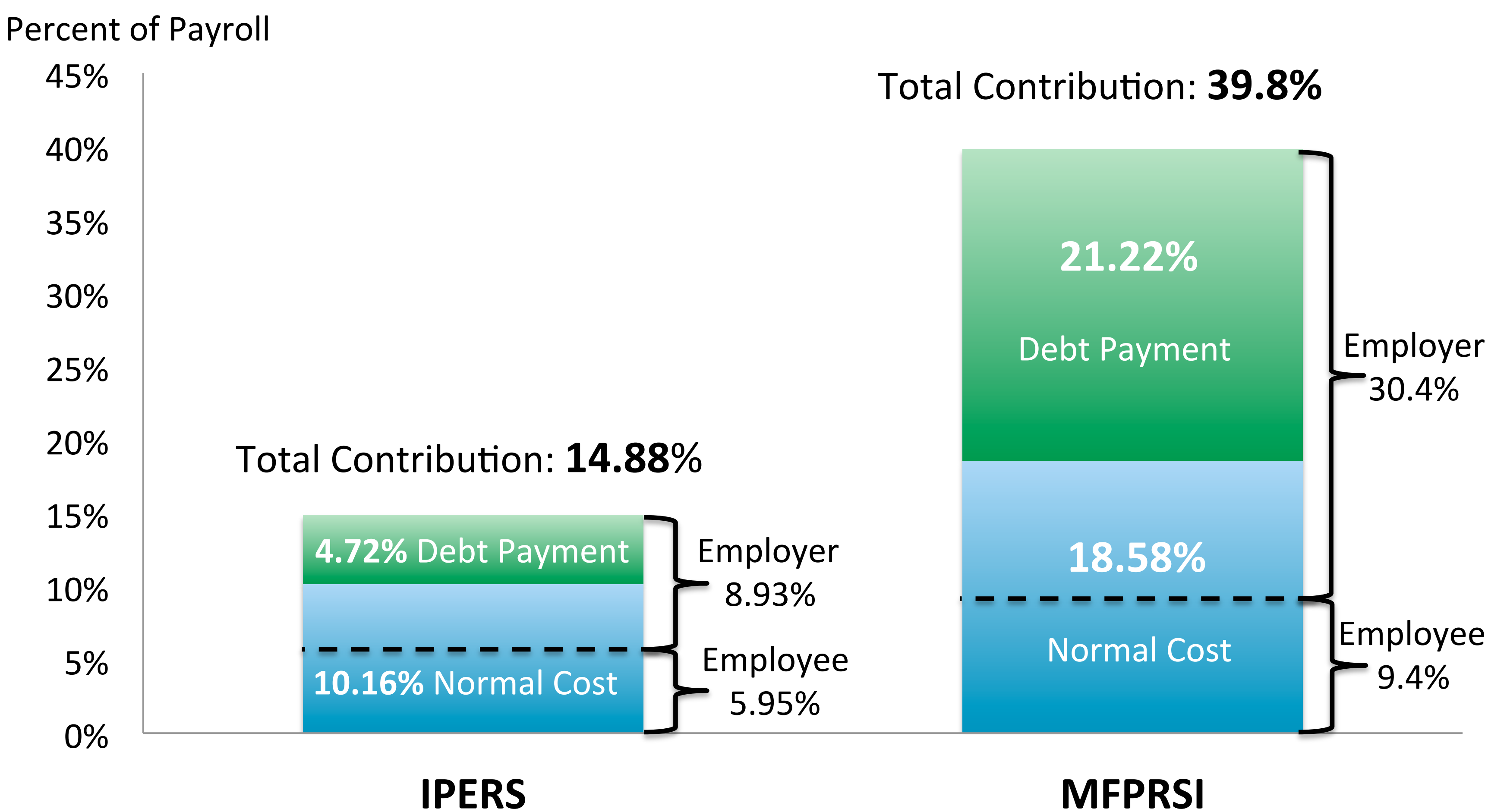

IPERS' funds lost almost 20 percent of their value by 2009.

# Translates into Unfunded Liability (IPERS, $ in Billions)




**Unfunded liability is debt** that must be paid off over a future amortization period. It is above and beyond the annual cost that accrues with each year of an employee's service. With market losses compounding prior years' underfunding, the result has been an almost five-fold increase in the unfunded liability over the past ten years.

# Fiscal Year 2014 Payroll Contribution Percentages

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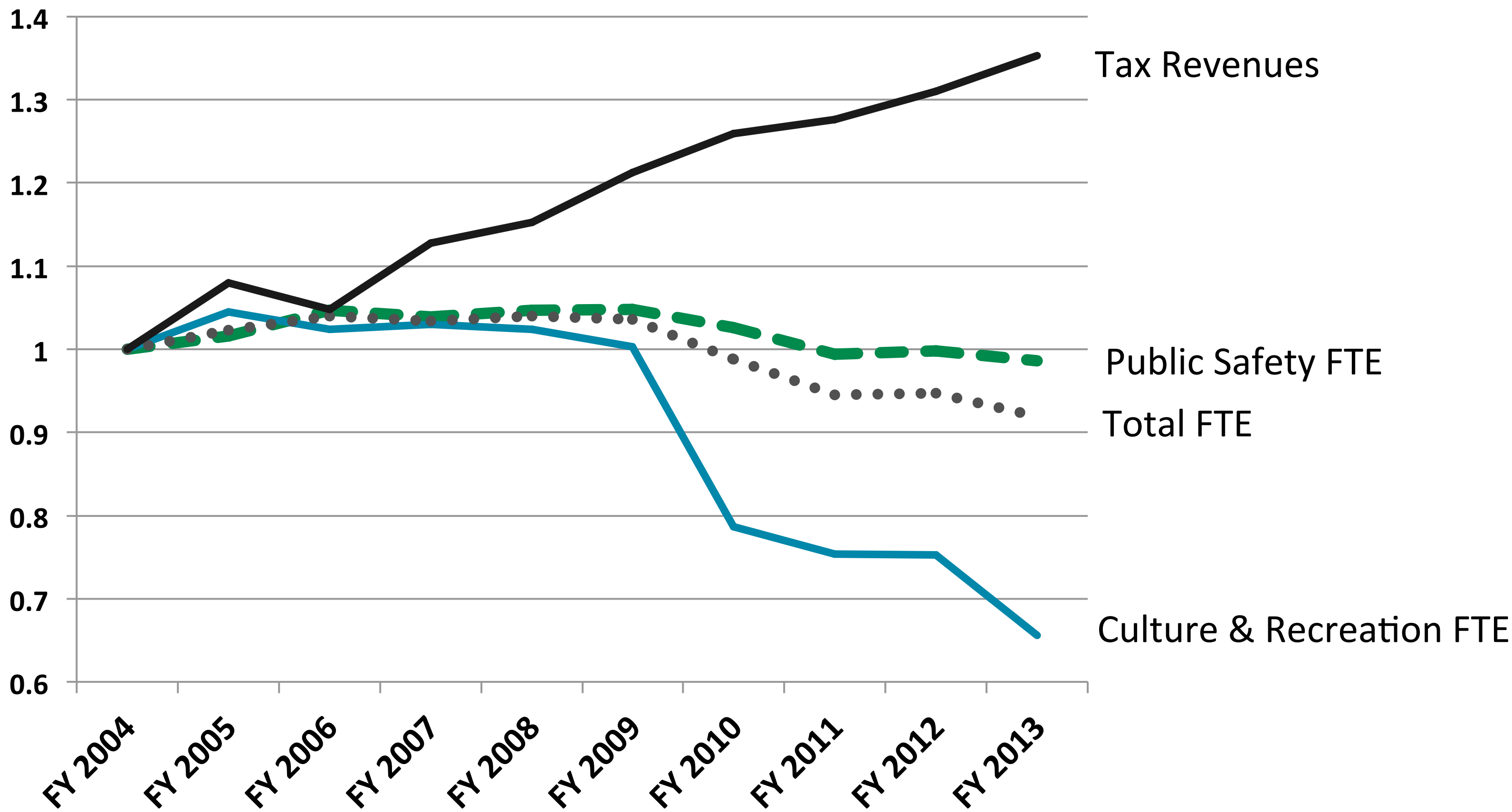
# As Tax Revenues Have Increased, Services Have Declined

## City of Des Moines

## Indexed, 2004 = 1




**Public pension employer contributions now represent the equivalent of 19 percent of all property taxes collected in the City of Des Moines.**



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## Statewide Impacts of Increased Public Retirement Contributions (IPERS and 411)

- $375 million per year of additional public spending **JUST FOR DEBT PAYMENTS OVER NEXT 25-30 YEARS** (total = $700M+)
- What does this represent?
  - 5,000 more public school teachers (a 15 percent increase in any given district)
  - 3,750 more uniformed police or fire officers (a 25 percent increase in any given city)
- Exceeds the total property tax savings from 2013 property tax reform

# All Estimates are Based on Certain Methods and Assumptions That Tend to Understate the Debt

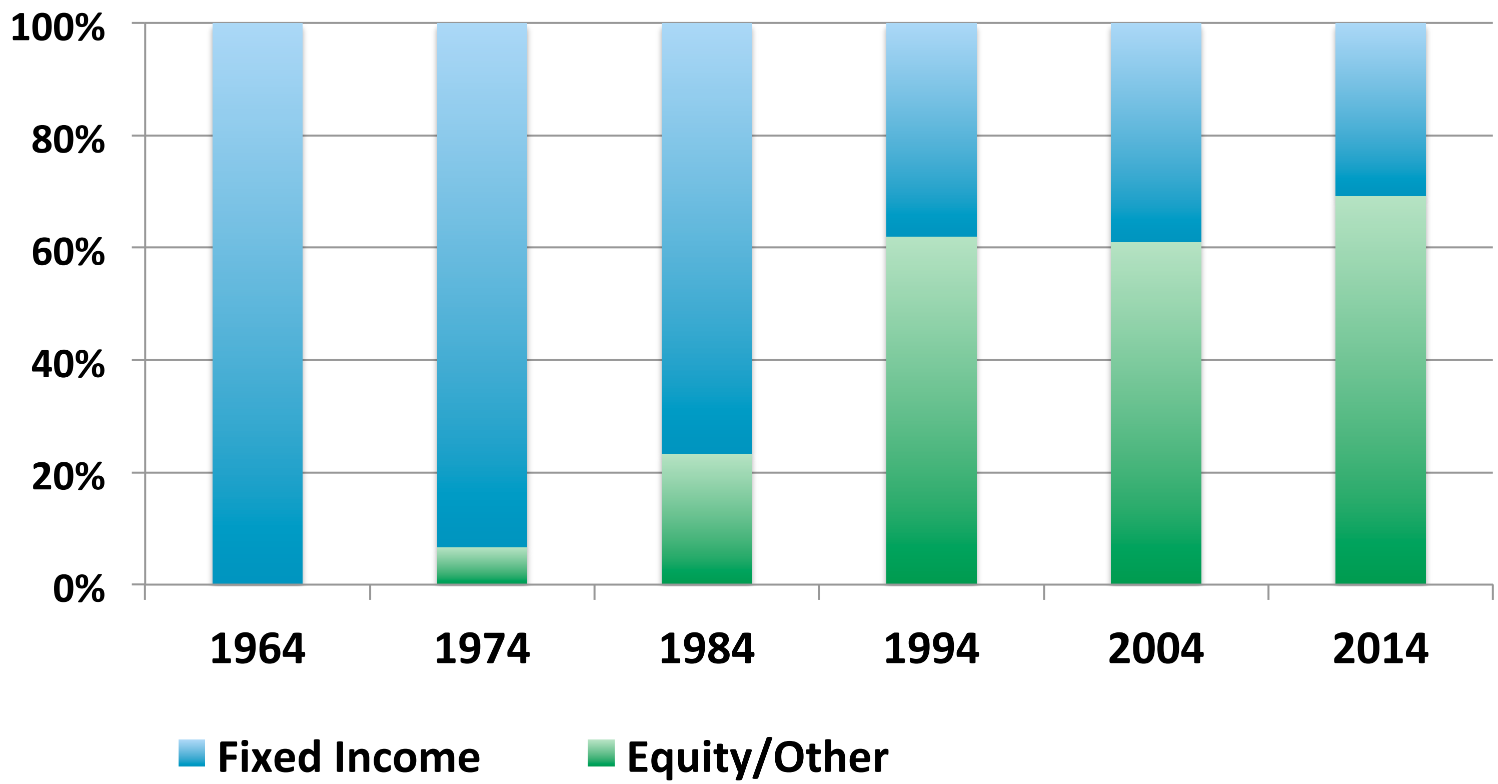
| | IPERS | MFPRSI | Moody's | Society of Actuaries |
|---|---|---|---|---|
| Amortization Period | 30 years, open (to close in 2015) | 25 years, now closed | 20 years, closed | 15-20 years, closed |
| Discount Rate | **7.5%** | **7.5%** | 5.6% | 6.4% (+ or - 3%) |
| Mortality Tables | RP 2000 | 1/3 1971; 2/3 1994 | RP 2000 | New tables |

Moody's analysis suggests that IPERS' unfunded liability is **more than twice what is currently reported.** Assumptions and methods result in understatement of liabilities.

Moody's has downgraded 8 of the 12 Iowa cities it has reviewed using the new methodology which calculates pension liability using its own methods & assumptions.

The Society of Actuaries has issued new RP 2014 mortality tables that will increase costs.

# IPERS Investments by Decade 1964 – 2014
# More Volatility Should be Expected




Source: IPERS Annual Reports, compiled by Taxpayers Association of Central Iowa

# When Times Are Good, Benefits are Enhanced

**Municipal Police and Fire Retirement System of Iowa**

| Year | Prior Year Funded Status | Max. Benefit Percentage |
|---|---|---|
| | | |
| 1995 | 94% | 65% |
| 1998* | 106% | 72% |
| 2000 | 107% | 82% |
| | | |
| 2006 | 92% | DROP Program added |
| 2009 | 99% | Cancer Presumption |

**IPERS**

**Ceiling on covered wages was removed in 1996.**

# Summary of Issues With Defined Benefit Plans in the Public Sector

- Benefits are enhanced when plans appear to be fully funded – but using a "surplus" in one year means it cannot cover the inevitable shortfall in another year, rendering the concept of a long-term rate of return meaningless.

- Plans tend to be underfunded when there are budgetary pressures – it's too easy for politicians to defer action.

- Significant debt can roll up quickly and automatically -- without explicit decision making.

- Debt is being used to cover operating costs, not to pay for long-lived assets.

- Intergenerational fairness issue – future generations will be paying for debt they didn't incur.

# Summary of Issues With Defined Benefit Plans in the Public Sector (cont'd)

- Paying for pension debt is already compromising public services.
- The debt is likely to be much more – probably twice as much -- than what is presented. **It is likely to be as much as all other public debt in Iowa**.
- **There is no upper limit on how much more debt we might incur in the future**, with attendant employee, taxpayer and public service impacts.

**Is this what we really want?**

# Implications

- Immediate relief is needed for cities in the 411 plan. Increasing employee contributions by 1 percentage each year for 3-4 years would achieve a 60%/40% employer/employee split similar to IPERS; use of longer period (5 years vs. 3) to determine average high salary would also be comparable to IPERS.

- Other states and cities are adopting alternative plan designs – "<u>best practice defined contribution plans</u>" (**NOT 401k's**) -- for new employees that capture the best features of defined benefit plans while containing the financial risk. Examples are Michigan, Utah, Rhode Island, Georgia, Tennessee and Kansas. Several have moved proactively and at least one was led by employees themselves.

- Iowa should take a fresh look at what type of public retirement plan is most appropriate for the next 50 years. Much has changed since 1953.