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STATE TREASURER
DENISE L. NAPPIER

NEWS

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Nappier Says with Proposed Plan to Reduce State Contribution to Pension Fund, State Hits "Trifecta of Bad Fiscal Management"

Testimony Before Legislative Committee Cautions of Potential for Increased Costs to Taxpayers, Lower Credit Rating, Lost Investment Opportunities

State Treasurer Denise L. Nappier said today that Governor Rowland's plan to provide less than 70 percent of the State's annual contribution to the State's teacher retirement pension plan in each of the next two years – the lowest contribution levels in decades – could ultimately cost taxpayers hundreds of millions of dollars and adversely affect the state's credit rating.

Nappier, in testimony before the legislature's Appropriations Committee, said that moving forward with the proposed reduction in the annual retirement contribution would be like hitting "the trifecta of bad fiscal management."

The Treasurer cited the potential impact on taxpayers, both now and in the future, the potential reduction in state services as funds are taken away from core services in coming years to pay for deferred pension contributions, and the likelihood of higher debt costs if the State's credit rating were to be downgraded by the rating agencies due to growing pension liabilities.

The Governor's proposed budget for Fiscal Years 2004 and 2005, call for the State to pay only 68.5 percent and 65.9 percent, respectively, of the actuarially recommended contribution. In recent years, the State had been paying 85% of the annual recommended contribution. Nappier has been a consistent advocate for the State to contribute 100% of the actuarially recommended amount to ensure a sound pension fund.

In her testimony, Nappier also pointed out that the result of chronic underfunding of pension funds has been evident in recent years in the City of Waterbury. To right that City's finances, including its pension fund, the legislature in 2001 appointed a fiscal oversight board, of which Nappier is a member.

"Waterbury is one municipality that has learned a painful lesson when it comes to the pitfalls in financing its retirement system. The State need not go down that same path.

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I urge you to protect the soundness and integrity of the State's retirement system and its financial structure," Nappier said.

The Treasurer said a preliminary assessment by her office of the long-term impact of reducing the State's contribution level in Fiscal Years 2004 and 2005, reveals significant fiscal impact.

- **Lost investment opportunities**: By failing to contribute $85 million in Fiscal Year 2004 -- the difference between the actuarially recommended amount and the Governor's proposal -- the State will lose the chance to earn an additional $822 million over a 29 year period. The 2005 reduction will have similar adverse consequences, resulting in lost investment opportunity of $847 million over this same period. **Taken together, the short-term budget fix proposed by the Governor will deny the Teachers' Retirement System the opportunity to earn $1.7 billion over a 29-year period.**

- **Higher costs to taxpayers**: The State's contribution that is not appropriated today but suspended or deferred into the future will **ultimately end up costing the State and its taxpayers far more**, over and above lost investment opportunity. It is estimated that eventual payment of the State's deferred contribution to the Teacher's Retirement System will total an additional **$573.9 million** over the 29 years scheduled for the amortization of the unfunded liability.

- **Liquidation of pension fund assets**: The proposed reductions over the next two fiscal years will result in having to **liquidate additional assets of the Teachers' Retirement Fund in order to make payments** to retirees and beneficiaries, as our pension liabilities grow at a much faster pace than our pension fund assets. The impact of pension liabilities on cash flow means that a larger portion of fund assets will have to be invested short-term rather than long-term, where the returns are traditionally higher.

"The bottom line is that the fiscal impact of the Governor's proposed budget is further growth in unfunded pension liabilities exacerbating previous years of underfunding the State's contribution. These billions of dollars of unfunded liability will eventually come due in the form of required appropriations. These will be appropriations that might otherwise fund core programs and services, such as the provision of educational services to our young people," Nappier said.

"When one considers all of these consequences, coupled with three consecutive years of market decline and growing market uncertainty, the results produce a double whammy on the pension fund," Nappier told the Committee.

Nappier also criticized those that suggest she ought to adopt a more aggressive investment approach to make up for the growing unfunded pension liability that would be caused by diminished state contributions.

"Not on my watch," Nappier said. "Making larger bets on riskier investments to help minimize the potential for a precipitous drop in the funding ratio would not be prudent," Nappier said.

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Nappier noted that one of the compelling reasons for recent legislative action to reduce the state's pending deficit was to avoid a reduction in the State's credit rating by the rating agencies. Each of the rating agencies has cited the current unfunded liability of the State's pension plans as a very important factor in determining the State's fiscal he alth – and the credit rating they assign.

"This is not just an issue for tomorrow. We are feeling the impact of past shortsightedness in our State's funding practice right now. And the rating agencies continue to watch how we respond," Nappier cautioned.

The Treasurer also urged members of the General Assembly to adopt legislation that would grant the State Treasurer flexibility -- depending on market conditions -- to use any future unappropriated surplus funds to either pay of debt or reduce pension liabilities.

"This flexibility is of paramount importance, especially when one considers that we have on our books relatively low cost debt, and that a better use of any unappropriated surplus in certain economic conditions would be to address the under funding that exists with our pension plans," Nappier said.

Treasurer Nappier also renewed her call for a constitutional amendment that would require the appropriation of the State's contribution to the Teacher's Retirement Fund equal to 100 percent of the actuarial recommendation.

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