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STATEMENT BY STATE TREASURER DENISE L. NAPPIER CONCERNING THE VIABILITY OF CONNECTICUT'S STATE EMPLOYEE RETIREMENT SYSTEM

On June 30th, *The CT Mirror* blasted a sensational headline "Study Says State Employee Pension Fund Will Be Broke by 2019," and went on to describe -- without any critical analysis of the assertions in the study it cites – how Connecticut's pension plans will run out of money in less than a decade. Missing in both the story and the underlying study are the facts.

Professor Rauh's paper, referred to in the article, seems to assume that states will not continue to contribute to past service liability of their pension funds and will solely rely on the assets in those funds to make retiree pension payments. Fact No. 1: In Connecticut, this is simply not true. The State Employees Retirement Fund has, indeed, been chronically underfunded; but based upon a collectively bargained agreement between the State and its unions, we are on a plan to pay up over a period of time for the past practice of not adequately funding the retirement system. Fact No. 2: As State Treasurer, I introduced and successfully fought for a plan to adequately fund our Teachers' Retirement Fund, which had been short-changed by past governors and legislatures in an effort to 'save' the State money. As a result, public school teachers – who are, by the way, not part of the Social Security system – can be assured that their earned benefits for a lifetime of teaching will be there at retirement. Fact No. 3: The Connecticut Municipal Employees' Retirement System is nearly fully funded.

An analysis of the Rauh paper by four well-regarded actuaries concluded, "Although we share Professor Rauh's concern over the difficult financial situation that state and local governments face in the current economy, we do not believe his analysis or recommendations [with regard to pension funding] are helpful in addressing the situation."[1]

And for me this is the main point: Yes, the cost of funding pensions will increase over the foreseeable future, in part, as a result of the Great Recession and uncertain recovery that have resulted in investment returns below assumptions. This, in turn, will put additional pressure on already stretched state and local governments. But the answer does not lie in reactionary policies that merely 'shift' the financial burden from the government to individuals who have earned a benefit for a lifetime of public service. Fact No. 4: The average retired state employee pension is approximately $28,000 per year -- hardly a king's ransom upon which to live in retirement.

This is not to say or imply that we should merely throw up our hands and say this is a problem too big to solve. But in attempting to address the issues of pension benefits and funding – not to mention health care benefits – we must take a measured and deliberative approach. There are ideas out there that should be considered, analyzed and discussed. For example, all state and local pension plans use an actuarially sound approach to accounting for investment gains and losses over a period of time rather than exposing state and local governments to the uncertainties of the market

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[1] Paul Zorn, Mita Drazilov, Paul Angelo & Keith Brainard, *Analysis of Joshua Rauh's Paper "Are State Public Pensions Sustainable?"*, June 1, 2010, http://nasra.org/resources/RauhResponse.pdf

from one year to the next. This technique, called smoothing, is currently used in all of the State pension plans. One possibility is to look at extending the time horizon over which smoothing is done.

Some have proposed, as does Professor Rauh, that we should cap our defined benefit pension plans and move newly hired employees to a defined contribution plan. In theory, this could save money over a very long time horizon, but would do little or nothing to address the unfunded liabilities that have accrued over the years because of the State's failure to adequately fund its pension obligations. Others have proposed something called a 'DROP' or deferred retirement option plan that would allow for defined benefit payments up to a certain salary level – say $100,000 – and thereafter allow the employee to supplement the defined benefit with a defined contribution plan. And still others would look to the benefit side of the equation and suggest that perhaps employees need to contribute a greater percentage of their salary to support their future pension benefits. I would support looking at these options, and perhaps others, as we look toward a future in which it is clear that a new Governor and General Assembly will have to make many difficult and often painful choices.

When it comes to pension benefits and funding, I propose that a three-prong test be used in the decision-making process: Any proposal offered must meet a 'fiscal responsibility' test. Too often in the past our response has been to kick the can down the road and think that somehow the problem will go away. Second, we must be able to 'quantify' any proposal and understand the fiscal implications over the long term. It is very popular right now to argue that all defined benefit plans should be capped and converted to defined contribution plans. But have we really done the kind of homework and analysis necessary to come to this policy conclusion? Finally, I would impose a 'fairness' test for any proposal that is considered. Not only understanding what the fiscal impact might be on the State, we also need to understand how that relates to the long-term financial security of individuals and families participating in the State's retirement system, and the discernable impact of retirement income on our state's economic activity. Surely within this three-prong test I have laid out there is much room for debate. But any debate must take place in a reasonable and reasoned way. We have too long suffered from bad policy coming out of doing what is politically expedient or taking a fiscal short cut. The times demand better, not less, of all of us.

As I have throughout my tenure as State Treasurer, I will work with the next Governor and General Assembly to chart a prudent and proper course for Connecticut's future – for the sake of both its taxpayers and its retirees.