The Office Of
State Treasurer
Denise L. Nappier

Press Release

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OTHER POST-EMPLOYMENT BENEFITS (OPEB) TRUST FUND NEARS ENTRY TO HIGHER-RETURNING INVESTMENTS

Hartford, CT - State Treasurer Denise Nappier today announced that $87 million set aside to fund the Other Post-Employment Benefits ("OPEB") Trust Fund has been included among the Connecticut Retirement Plans and Trust Funds ("CRPTF"). The use of the CRPTF's investment pool for the OPEB Trust Fund was made possible following last month's approval by the independent Investment Advisory Council of Treasurer Nappier's plan to formally designate the OPEB Trust Fund as a component of the CRPTF. This approval is one of a series of actions needed to ensure the growth of the trust fund's assets, which represents a portion of pre-funded future costs of retiree health benefits.

Treasurer Nappier said, "State officials and union leaders were wise to consent to the establishment of an irrevocable trust fund to better manage the state's future OPEB costs and lessen the costs to the state budget. This, in turn, can help to reduce the staggering burden on Connecticut taxpayers in meeting the state's single largest long-term unfunded liability. The good news is that the OPEB Trust Fund is at the starting gate, poised to achieve the highest possible risk-adjusted performance."

Historically, Connecticut's health benefits plan has been funded on a pay-as-you-go basis, with benefits paid from current year general fund appropriations. Beginning In 2008, the state committed to partially pre-fund its future liability, but then deferred payments because of budget constraints until March of 2012. Under a revised 2011 agreement reached with the State Employees' Bargaining Agent Coalition (SEBAC), the state will begin contributing to the OPEB Trust Fund in 2017 an amount equal to employee contributions. The state has been setting aside employee contributions for future health benefit costs since 2008, and covering current retiree benefits from the general fund.

Under the Revised 2011 SEBAC agreement, the OPEB Trust Fund can be used to pay health benefits for employees retired on or after July 22, 2011. To date, the state has made no withdrawals for such benefits, and contributed $24.5 million to the trust fund. However, the size of the OPEB Trust Fund at $87 million pales when compared to the state's annual health benefits costs for current retirees of between $577 million and $569 million from 2013 through 2021. For future retirees beginning 2013, the cost is estimated at $84 million and will rise to $581 million by 2021.

According to the Treasury's preliminary asset/liability study, one of the preferred long-term investment strategies under consideration for the OPEB Trust Fund would target a real return of 5.4%. With an initial investment of just under $87 million, expected employer and employee contributions, and interest income generated on these funds, the corpus of the trust fund is projected to grow to $2 billion over the next ten years, assuming no assets are withdrawn.

The bulk of the trust fund assets, currently employee contributions, were initially invested in the Treasury's Short-Term Investment Fund (STIF). These assets have now been transferred to CRPTF's short duration bond fund consisting of securities with global diversification and maturities longer than money market securities like those held by STIF. Pending final arrangements for a longer investment horizon, the Treasurer's Office plans to employ a long-term diversified investment strategy, including domestic and international stocks and bonds and alternative investments. For the 2012 calendar year, this bond fund returned 1.92% versus .16% for STIF for the same period.

A key factor in determining the OPEB Trust Fund investment strategy is the state's funding and spending policy. As the trust fund's investment horizon increases in length, so will its risk tolerance for higher return-seeking investments. "As much as I would like to move swiftly to position the OPEB Trust Fund to maximize return, we must take a measured approach to establishing a sound asset allocation plan," said Nappier. "For that, we need a clearer sense of this trust fund's expected cash flows and the timing of disbursements. In the meantime, the CRPTF's short duration bond fund is our best and only avenue for managing this money. To do otherwise could result in the reckless loss of the trust fund's principal. For example, the annual cost of the current health benefits alone that could be paid by the OPEB Trust Funds is nearly equal to the size of the trust fund's current assets."

According to Nappier, the ability to execute the preferred investment strategy is contingent upon a solid commitment from the state to adopt a stronger funding policy and prohibit benefit payment withdrawals until such time that the trust fund has accumulated substantial assets to ensure preservation of its principal. "The state cannot afford to return to its habits of old in the management of its long-term obligations -- as evidenced by the state employees' pension plan that switched to an actuarially funded plan in the 1970's, and today is ranked as one of the worst funded plans in the country. In other words, no withdrawals, funding holidays or any other gimmicks that will corrupt the fragile financial footing of the OPEB can be tolerated. It is therefore highly advisable that the state strengthen the foundation of the OPEB Trust Fund through any number of means up to and including legislation."

The state's funding and spending policy for the OPEB Trust is one of several features of the OPEB Trust Fund that need to be fully addressed before the assets can be deployed to appropriate long-term investment vehicles. In August of 2012, Treasurer Nappier advised state officials that a number of governance and other structural issues need to be clarified, such as the development of governance documents to comply with state and federal law, IRS guidelines and Government Accounting Standards Board rules.

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