Purpose

- Recap some of the content that was presented at the 2014 Public Pension Funding Forum at Columbia University, New York.
- Share with you some of the research we have been engaged in since the Columbia Forum.
- Discuss some of the future research we plan to undertake.
PUBLIC PENSION FUNDING FORUM
Presidential Ballroom, Faculty House, Columbia University
64 Morningside Drive, New York, NY 10027

A Joint Conference by the
National Conference on Public Employee Retirement Systems
and the
Institute on Public Pension Solutions

AGENDA

MONDAY, APRIL 21, 2014
3:00 pm – 5:00 pm  Registration
5:00 pm – 6:00 pm  Welcome Reception

TUESDAY, APRIL 22, 2014
8:00 am – 8:30 am  Registration
8:30 am – 9:45 am  Breakfast Session – Welcome and Opening Remarks: Exploring Policy Options in a New Framework for Pension Reforms
        Mali Aaronson, President, NCPERS

Pensions and the Economy
        Joseph Stiglitz, Nobel Laureate in Economics, Columbia University

9:45 am – 11:00 am  Trends in Pension Legislation
        Luke Martel, National Conference of State Legislatures

The Evolution of Public Sector Pension Underfunding
        Robert Triest, Federal Reserve Bank of Boston

Chair: Dana Bilyeu, National Association of State Retirement Administrators

11:00 am – 11:15 am Break
11:15 am – 12:30 pm  Risk Management in Economic Cycles and Maturing Plans  
Michael Papadoyannou, International Monetary Fund

Pension Funding: It’s Not Just a Math Problem  
Jim Linke, The PFM Group

Chair: Dana Dillon, CalSTRS

12:30 pm – 2:30 pm  Luncheon Session – Closing the Funding Gap  
Obligation Bonds – Questions to Ask Before Issuing  
Elizabeth Wity, Chairon

What Can We Do Differently Going Forward?  
Garth Schnitz, Independent Municipal Finance Expert

Portfolio Approach  
David Winton, Nuveen Investments

Chair: Theresa Lechta, Maryland State Retirement and Pension System

2:30 pm – 3:30 pm  What’s Adequate Funding and How can we Manage Risks?  
Gene Kulberski, Chairon
John Hasley, Assured Guaranty

Chair: Roger Ras, Omaha School Employees Retirement System

3:30 pm – 4:30 pm  Long Term Strategy – Revenues and Economy  
Susan Kennedy, Alabama Education Association
Richard Sims, Sierra Institute for Applied Economics

Chair: John Jensen, Chair IPPS Research Advisory Group

4:30 pm – 5:00 pm  What Other Strategies Should We Consider? Open Discussion  
John Jensen, Chair IPPS Research Advisory Group

5:00 pm  Closing Remarks, and Next Steps  
Michael Kahn, IPPS, and Hank Kim, NCPERS

5:00 pm – 7:30 pm  Reception and Dinner  
Special Guests include Joseph and Anya Siegels, and Rob Johnson, Roosevelt Institute. Rob will share his latest research on public pensions.
• **Joseph Stiglitz** was very critical of Wall Street’s accounting practices and lack of transparency. He also was very critical of GASB rule that require public pensions to use an artificially lower rate of return for the unfunded portion of liabilities.

• He said pension funds are long-term investors, and we know that in the long-term equity returns are higher than the rate of return pension funds usually assume.
• **Luke Martel** reviewed the pension legislation that was enacted by April 2014. He noted that almost all states have modified their pension plans by increasing employee contributions, reducing benefits and COLAs, and in some cases moving to defined contributions or hybrid plans.

• **Robert Triest** shared his analysis of evolution of underfunding of public pensions. He said states have been making contributions to pensions, they just did not make enough.
Michael Papaioannou shared with the audience his analysis of investment behavior of institutional investors from several countries. His analysis showed that investors who stayed focused on the long-term through economic ups and downs came out ahead compared to those who reacted and made changes to their portfolios during economic downturns.
• **Jim Link** (this year **Dan Kozloff** is taking Jim’s place) Spoke about important social and economic role pensions play in our society.

• He then focused on funding status, causes of underfunding, and some possible ways to improve funding levels, especially use of Pension Obligation Bonds.

• After I go through a few more highlights, I’ll let Dan Kozloff speak.
• **Elizabeth Wiley** shared with the group various questions pension plans need to consider when they plan to issue POBs.

• **Garth Schulz** spoke about closing pension funding gap using POBs and shared his analysis of back-testing of this concept.

• **David Wilson** made a case for active risk management as a way to improve returns and close funding gap (David will speak on this subject in a few minutes).
• Gene Kalwarski addressed the question following questions: what does adequate funding mean and what factors should be kept in mind to achieve and maintain adequate funding?

• John Hallacy underscored some of the cautions that must be kept in mind in considering POBs.
• Richard Sims discussed how changes in pensions impact local economies.
• Susan Kennedy shared her research on how tax loops work in different states and how closing these loopholes can generate additional revenues to fund pensions appropriately.
Let me now turn over to Dan and David to recap some of what they had shared with us at the last year’s Forum in New York.

After they speak, I’ll share some of the subsequent research we have been doing.

I’ll also some thoughts on our future research.
There is little or no research on how prevailing public pension reforms impact income inequality.

NCPERS is leading the research on this subject, and I want to share some results with you.
It is just common sense. Income inequality is bound to rise when incomes of some people are reduced through pension cuts and incomes of others are increased through cuts in marginal (top) tax rates.
Overview of Presentation

• What are the prevailing approaches to pension reforms?
• Do these reforms exacerbate income inequality?
• Does rising income inequality slow down the economy?
• What can we do?
At the national level, the main trend has been conversion of defined benefit plans into defined contribution plans.
Empirical data from 1982-2011 show that as the percentage of workforce (public and private) in DB Plans declines, income inequality rises.
At the state and local level pension reforms consist of the following actions

- Between 2009-2013, 48 states made changes to their pension plans – some more than once
- 34 states increased employee contributions
- 38 states instituted higher age and service requirements for retirement
- 30 states reduced COLAs
- 18 states instituted steps to convert DB plans into DC or Hybrid Plans (Mandatory Hybrid – 6 States, Mandatory Cash Balance – 3 State, Mandatory DC – 2 States, and Choice of Plan – 7 States)
We reviewed state and local pension changes during 2000-2010.
Counted number of negative pension changes such as cutting benefits, increasing employee contributions, converting DB plans into DC or hybrid plans in each state.
Examined changes in income inequality in each state during the same period.
Conducted an analysis of the relationship between the negative pension changes and income inequality.
What did we find?

- The analysis shows that the higher the number of negative changes a state makes to its pensions, the higher the increase in income inequality in that state.
- This relationship holds even when we take into account other factors that might impact income inequality – such as lack of investment in public education.
- Furthermore, the analysis shows that a single negative change increases income inequality by about 15%.
There is mounting evidence that rising income inequality drags the economy down

- International Monetary Fund – “Redistribution, Inequality, and Growth,” February 2014
Each Time Income Inequality Reached its Peak, A Major Recession Followed, and Everyone Suffered

Source: Robert Reich Documentary – Inequality for All
Empirical data from 1984-2011 show that as income inequality rises economic growth dampens.
Analysis of state income inequality and economic growth in the states, 2000-2010

- We examined changes in income inequality in each state from 2000 to 2010.
- We also examined economic growth in each state during the same period.
- We conducted an analysis of the relationship between income inequality and economic growth.
What did we find?

- The higher the rise in income inequality in a state, the lower the economic growth in that state.
- This relationship holds true even when we take into account other factors that might impact economic growth such as productivity.
- The analysis shows that during 2000-10, when income inequality in a state rises by one, economic growth in that state declines by about 18%.
Bottom line

- Analysis of empirical data shows that the prevailing pension reforms increase income inequality.
- Rising income inequality in turn slows the economy down.
- In the end, everyone suffers, not just public employees.
PRESS RELEASE

Shifts Away from Defined-Benefit Pensions Widen Income Gap Between Rich and Poor, NCPERS Study Finds

Published: May 5, 2015 9:30 a.m. ET

Prevailing Approaches by States Have Hidden Economic Costs

WASHINGTON, May 05, 2015 (BUSINESS WIRE) -- Reforms that negatively affect pension plan participants and beneficiaries also exacerbate income inequality and hinder economic growth, according to a new study by the National Conference on Public Employee Retirement Systems (NCPERS).

The study showed a strong correlation over three decades between the declining number of workers covered by defined benefit pension plans and the growing income gap between rich and poor Americans. Other variables that were associated with increased income inequality included declines in unionization, marginal tax rates, and investment in education, according to the study, "Income Inequality: Hidden Economic Cost of Prevailing Approaches to Pension Reforms."

The study was released at NCPERS' Annual Conference and Exhibition, held in New Orleans May 3-7.
Blame the 401(k) for the wealth gap

MAY 07, 2015 | BY MARLENE Y. SATTER

Rising income inequality is a byproduct of pension reform actions that have made people rely on defined contribution plans rather than defined benefit plans.

So says research from the National Conference on Public Employee Retirement Systems, which made the point in a paper titled “Income Inequality: Hidden Economic Cost of Prevailing Approaches to Pension Reforms.”

The paper found that benefit cuts, larger employee contributions and conversion of...
Pension program changes hurt economy, NCPERS report warns

BY MEGHAN KILROY | MAY 8, 2015 5:01 PM | UPDATED 10:15 AM

Some pension program changes, such as the shift to defined contribution plans from defined benefit plans, might be widening the income gap and dampening economic growth, said a new report from the National Conference on Public Employee Retirement Systems.

There are conversations about income and equality, but few touch on the treatment of pensioners and how that contributes to income inequality, said Hank Kim, Washington-based, executive director and counsel at NCPERS and co-author of the report.

In the private sector, there has been a shift to DC plans from DB plans. Between 1975 and 2011, the number of private sector DB plans declined by 57% and the number of employees covered by DB plans declined 10%, NCPERS' research found.

While DB to DC conversion is less common in the public sector, there are other changes — benefit
Shift to 401(k) Plans Increasing Income Inequality: Study
What Can We Do?

- For starters, policy makers should pay serious attention to the hidden economic cost to taxpayers before they diminish public pensions.
- Instead of diminishing pensions, state and local governments should close tax loopholes and corporate subsidies first.
- The political justification: Whereas taxpayer money given to global corporations through loopholes and subsidies often ends up in overseas tax havens, pension checks are spent to stimulate local economies.
A clip from Roseanne demonstrates that Tax Subsidies and Loopholes are not a good idea.
## Comparison of Annual Employer Pension Contributions and Annual Cost of Corporate Tax Loopholes and Subsidies in Selected States

<table>
<thead>
<tr>
<th>State</th>
<th>Annual employer normal pension costs</th>
<th>Annual cost of corporate subsidies and tax breaks/loopholes</th>
<th>Annual pension costs as a share of subsidies + tax breaks/loopholes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Arizona</td>
<td>$474,524,688</td>
<td>$552,108,211</td>
<td>86%</td>
</tr>
<tr>
<td>California</td>
<td>$6,822,294,460</td>
<td>$9,701,000,000</td>
<td>70%</td>
</tr>
<tr>
<td>Colorado</td>
<td>$179,560,282</td>
<td>$593,109,000</td>
<td>30%</td>
</tr>
<tr>
<td>Florida</td>
<td>$905,581,094</td>
<td>$3,810,902,291</td>
<td>24%</td>
</tr>
<tr>
<td>Illinois</td>
<td>$1,855,100,000</td>
<td>$2,400,796,000</td>
<td>77%</td>
</tr>
<tr>
<td>Louisiana</td>
<td>$348,471,694</td>
<td>$1,813,729,079</td>
<td>19%</td>
</tr>
<tr>
<td>Michigan</td>
<td>$586,592,328</td>
<td>$1,860,600,000</td>
<td>32%</td>
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<tr>
<td>Missouri</td>
<td>$427,300,226</td>
<td>$840,231,523</td>
<td>51%</td>
</tr>
<tr>
<td>Oklahoma</td>
<td>$221,501,696</td>
<td>$479,033,081</td>
<td>46%</td>
</tr>
<tr>
<td>Pennsylvania</td>
<td>$1,395,509,900</td>
<td>$3,888,000,000</td>
<td>36%</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$13,216,436,368</strong></td>
<td><strong>$25,939,509,185</strong></td>
<td><strong>51%</strong></td>
</tr>
</tbody>
</table>

Source: Good Jobs First, 2014
WHEN A RISING TIDE SINKS MOST BOATS: TRENDS IN US INCOME INEQUALITY

PAVLINA R. TCHERNEVA
Figure 1 90 Percent vs. 10 Percent: Distribution of Average Income Growth during Expansions (including capital gains)
Before I close, let me share with you some thoughts on the future research we are planning to do.
Economic Instability for All: Hidden Cost of Pension Reforms of the Last 30 Years

Economic Bubbles
- Causes
- Consequences

Pensions
- Stabilize economy
- Prevent bubbles

Impact of Pension Reforms
- Contribute to formation of bubbles
- Increase the impact of economic shocks resulting from bursting of bubbles

What Can We Do?
Preserve and expand pensions