



LEAGUE OF WOMEN VOTERS®  
OF LOUISIANA

# *Should We Panic Over Public Pension Costs? Or Not?*

*Issues and Options for  
Louisiana's State Public Pension Systems\**

*Prepared by the Pension Study Team of the  
League of Women Voters of Louisiana  
August, 2014*

\*A study of these systems:

Louisiana State Employees' Retirement System (LASERS)  
Teachers' Retirement System of Louisiana (TRSL)  
Louisiana School Employees' Retirement System (LSERS)  
Louisiana State Police Retirement System (LSPRS)

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## **Origin and Purpose of This Study**

Pension benefits for public employees are a hot political as well as economic issue across the United States. Three-hundred-ninety-nine bills have come before the House and Senate Retirement Committees in just the past four years, including 2014. The League of Women Voters of Louisiana (LWVL,) however, has not been able to respond to these bills because it had not yet undertaken a study nor developed a formal position on the relevant issues .

The delegates to the 2013 League of Women Voters of Louisiana Convention voted to study Louisiana's retirement systems' requirements and laws. This background paper and the LWVLA's final position will assist both the state League and the public to respond effectively to the high volume of retirement bills in each legislative session, to understand the annual budgetary responsibility and impact of Louisiana's state pension systems and benefits, and to evaluate assertions in the media about public sector pensions.

The study's intent is to describe for the League members and the public

- what systems are in place in Louisiana for public sector employees;
- how each system is governed and funded;
- what standards or public policies regarding public pensions are in place;
- what factors affect each system's cost and who determines those factors;
- how the retirement systems compare, "apples to apples," with each other and with private sector retirement benefits;
- why there is an unfunded accrued liability in the systems;
- what best practices have been identified for sustaining pension systems;
- what the budgetary, economic and social impacts of the pension systems are;
- the pro's and con's of various reform options.

## **Methodology**

To answer these questions, the study team reviewed literature from government officials, retirement systems, non-profit research organizations, government, public finance, audit and actuary associations and a variety of other media sources. An effort was made to examine both national and Louisiana sources, as well as a wide array of economic and political perspectives on the issues. The study team conducted interviews with the state retirement systems, a current and a past retirement committee chair, and League resource people.

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Frightening headlines continue to warn of a growing financial threat arising from pension costs, especially public sector pension costs. Since the recession of 2008-2009 and resultant losses within pension plan investments, observers have even questioned the sustainability of public sector pensions at all. Is the alarm justified and is it time to make major changes? And would major changes make matters better - or worse - or accomplish nothing? In 2013, the League of Women Voters of Louisiana committed to studying these issues. We explore the questions, "Should we panic over public pension costs? Or not?"

## **Introduction**

The issues surrounding public sector pensions are especially important in Louisiana. Louisiana has been listed as one of 13 states with the worst financial status for state and local pension plans, and one of five states that have been "bad actors as pension funders" with pensions systems insufficiently funded at present for the benefits they will need to pay in the future. Nationally, it is Louisiana and these other states that fuel the term "crisis" [Munnell, p. 25 and p. 87].

Louisiana is a right-to-work state, one of 24 that prevent unions from mandating membership. The state teacher organizations do not have contracts with the state and do not participate in collective bargaining. Public employees in the four Louisiana state retirement systems (*i.e.* Louisiana State Employees' Retirement System or LASERS; Teachers Retirement System of Louisiana or TRSL; Louisiana School Employees' Retirement System or LSERS; and Louisiana State Police Pension and Retirement System or LSPRS) cannot participate in Social Security and therefore do not receive Social Security benefits when they retire. Their State pensions are usually their only source of retirement income. (There are a very few exceptions where employees have special circumstances).

Only six other states have opted out of the Social Security system for their public employees and of these seven states only Louisiana, Alaska, and Illinois have constitutional responsibility for pension benefits [Munnell, p. 27 and p. 220; Manhattan Institute for Policy Research, p. 1; National Conference on Public Employee Retirement Systems]. In staying out of the Social Security system for public employees, Louisiana is required by federal law to provide retirement benefits at least equal to what Social Security benefits would be. The

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financial health of the State is therefore deeply connected to the health of these retirement programs. States may not, by law, go bankrupt and default on promises, unlike municipalities [National Council of State Governments].

We deal only with pensions in this study and we use the word “pension” because nationally “pension system” or “pension plan” is used more commonly than “retirement system.” Use of the word “pension” also carefully distinguishes monthly guaranteed income replacement payments to retirees from other benefits, such as health insurance, disability benefits, survivor benefits, as well as application of accrued sick leave or annual leave.

### **Overview of this Paper**

We begin with a discussion of how the state employee pension systems affect the state economy and why the issues surrounding these pensions have a significant effect on both the public and private sectors of the state. The paper continues with a discussion of the mechanics of pensions in general.

In addition to the four state systems, there are nine other statewide systems and eight local public pension systems. Because these systems have varying issues and characteristics, we have chosen to limit this report to the four systems for which the state itself has constitutional responsibility. The state Constitution reads, with reference to the four state systems, “... *the state has a contractual relationship [with the members] ... for whom the state shall guarantee pension benefits*” and “*The accrued benefits of members of any state or statewide public retirement system shall not be diminished or impaired.*” Our hope is that this study will provide both a general understanding of the issues and a firm basis for pursuing studies of the statewide and local systems in the future. The text of the Constitution on the state’s responsibilities for public employees is found in Appendix A.

This paper discusses the pressing issue of unfunded accrued liability (UAL). We also review historical, economic, political and government oversight concerns that potentially affect public pension policy. Unfunded pension liabilities continue to be the rationale for a wide range of reform proposals. This paper presents a broad-based overview for the members of the League of Women Voters of Louisiana and the public.

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Finally, we present descriptions of best practices in public pensions as put forth by various professional associations, some of the main options that have been suggested for supporting pension system sustainability along with their pros and cons, and broad conclusions from this study.

## **WHY PUBLIC PENSIONS ARE IMPORTANT TO THE STATE**

As noted above, for most retired employees in the four state government pension systems, their pension is their total retirement income as they cannot receive Social Security through their public sector employment. The reliability of this monthly income is viewed as a stabilizer in economic downturns and a means of preventing a large number of seniors from falling into poverty and therefore costing the state for social services and other assistance.

Retirees of the two largest state pension systems (In 2013, 89% of TRSL retirees [“Investing in Louisiana: TRSL Economic Impact Report”] and 90% of LASERS retirees [LASERS, “Giving Back to Louisiana: 2012 Economic Impact Study”] continue to live and spend their pensions in Louisiana. 95% of LSPRS retirees continue to live and spend their income in Louisiana [interview, Irwin Felps]. They therefore pay state, parish, and municipal property and sales taxes. Analysis across the state and parishes shows the retired TRSL, LASERS, and LASERS public employees make up 1.5-2% of personal income in Louisiana varying by parish [Louisiana Budget Project].

The state pension systems are also “key economic drivers,” says the Louisiana Budget Project and TRSL and LASERS. TRSL’s asset investment in the top ten growth business areas in Louisiana totals \$340 million in 2014 and is 3<sup>rd</sup> in Gross Domestic Product for Louisiana behind accommodation and educational services. [“Investing in Louisiana: TRSL Economic Impact Report”] \$90 million of LASERS’ assets are invested in Louisiana businesses [LASERS, “Giving Back to Louisiana: 2012 Economic Impact Study”].

At the same time, as with most other states, there is growing concern about the cost of public pensions. That cost must be considered in the context of the benefits detailed above, but the sheer size of the systems and their liabilities, as noted earlier, has provoked alarm.

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## **BASICS OF HOW ALL PENSIONS WORK**

### **Why Offer Pension Benefits At All?**

Pensions, one of the main parts of overall retirement benefits along with retiree health care, are offered to government employees for four main reasons:

Government needs to be competitive in the labor market in order to recruit high caliber employees capable of providing effective public services.

- Well-designed pension plans also serve as an incentive for employees to stay in public service, i.e. for the State to retain experienced employees.
- Society has viewed it as a matter of fairness to provide career public servants with a degree of financial security and a regular income in retirement.
- The State has an interest in minimizing the number of seniors, including former public employees, whose incomes are at or near poverty and who will turn to the State in one way or another for assistance.

There is always a certain tension between advocates or employees who naturally want higher compensation, including higher pension benefits, and the employers - various governmental agencies and departments in this case - who have limited budgets and a limited capacity for going to the taxpayers for more revenue.

### **Pension Plan Types**

Two broad categories of pension plans exist. The two types are based on quite different philosophies and priorities. These are “defined contribution” and “defined benefit” plans.

- *Defined contribution plans* are those plans in which the employer (i.e. the particular government entity that actually employs each kind of worker) and often the employee make regular contributions during the employee’s working life. These funds are then invested, often at the direction of the employee. When the employee retires, the amount of money in the accumulated fund at that time is what the employee will receive as a retirement benefit. The employer is thus able to predict exactly what its

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contributions and its employees' contributions will be. The retiree's benefit will be a function of what those contributions were and how well the investment of the funds has performed over time.

- *Defined benefit plans* also involve employer and usually employee contributions with the funds then invested over time. The big difference is how a retirement benefit is calculated. In these plans, the benefit level itself is guaranteed by the employer and is a function of various plan design features and employee characteristics (more detail below.) The employer has the obligation of providing the retirement benefit according to the plan for the rest of the retiree's life, no matter how well the investment of accumulated funds has performed.

In familiar terms, the federal Social Security system is a form of *defined benefit* plan. Benefits are based on years of employment under the system, earnings, and age at retirement, but not on the performance of investments. Private 401(k) plans are *defined contribution* plans. Those benefits are very much dependent on investment performance as well as past contributions. Much, but not all, of the private sector now offers defined contribution plans rather than defined benefits plans. The four state systems all have defined benefit plan designs.

### **Private sector vs. public sector**

In some ways, pensions are quite similar in the private and public sectors. In both sectors, they are used as part of total compensation in order to recruit and retain qualified employees. They are both intended to play some role in ensuring that retirees have a degree of financial security throughout their lives.

There are some major differences, however.

- Public sector employees in Louisiana do not participate in the Social Security System. Virtually all private sector employees DO participate in Social Security and therefore have that level of retirement financial security before considering what their employers offer. Retirees in the private sector generally have income from three sources: Social Security, their employer's private pension plan and their personal savings. Louisiana public sector retirees, however, unless they paid into Social Security through private sector employment, have only the last two as sources of income.

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Employer contributions to Social Security (Old Age, Survivor and Disability Insurance or OASDI) are 6.2% of the first \$117,000 employee income (in 2014) and this amount is matched by the employee. *[NOTE: In addition both employer and employee contribute 1.45% of all employee taxable income to the Medicare Hospital Insurance program or HI. Employees hired after April 1, 1986 all contribute 1.45% to the Medicare program and receive Medicare benefits the same as private sector employees.]*

- In the private sector nationally, 69% of full time employees are now in defined contribution retirement benefit plans [Employee Benefit Research Institute], usually in the form of 401(k) plans. These are generally designed to supplement Social Security and employee personal savings, not to provide all the income an employee will need in retirement.
- Private sector organizations and companies can and do go out of business; governments cannot. Governments therefore know they will need employees in perpetuity and must design compensation programs accordingly.
- Because private companies can go out of business, the federal Employee Retirement Income Security Act (ERISA) was passed by Congress in 1974. ERISA has set standards for pension plans and those standards do not apply to public sector pension programs. ERISA does not mandate that an employer provide a pension, nor the amount if one is provided, but it does set numerous requirements for plans when they are provided. A majority of private employers switched to defined contribution plans or a mix of both defined contribution and defined benefit plans after 1974 because of the increased complexity of administering defined benefit plans under ERISA regulations and to eliminate the employer risk for future pension benefits.
- ERISA also established the Pension Benefit Guaranty Corporation (PBGC) that will pay a certain maximum level of benefits to retirees should a private defined benefit plan be terminated. The PBGC is funded by premiums paid by the sponsors of qualified pension plans, i.e. employers. Premiums are about \$49 per year per employee (\$4.08 per month) in 2014. No such guaranty exists for public sector pensions.

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With these differences, it is difficult to compare public and private pension systems and know that the comparisons are truly apples-to-apples comparisons. Some assert that public pensions are much larger than private pensions (usually because private sector pensions are supplements to Social Security) while others assert the opposite. Also, according to the Brown Center on Education Policy at Brookings [“Are Pensions Keeping Up with the Times?”, p. 3], a higher percentage of public sector total compensation (salary plus pension plus health insurance plus other forms of compensation, if any) is in the form of pension benefits than in the private sector, perhaps to allow government to defer funding to later years in a way the private sector generally cannot.

## **HISTORY OF LOUISIANA’S FOUR STATE PENSION SYSTEMS**

In 1936 TRSL was established, with LSPRS following in 1938 and LASERS and LSERS in 1946. These systems were set up as public trusts.

The four state pension systems were created as separate independent systems serving their own members. The systems do not share assets, liabilities, investments or administration. Each Board of Trustees, with professional staff support, determines its investment strategies and reports earnings quarterly to the legislature. Its benefit structures and costs are quite different. Each system includes a number of sub-plans for different categories of employees within the system, with wide ranges in level of skills and education required. A description of the membership in each system is in Appendix B.

## **Early Lack of Regulation of Louisiana’s State Pension Systems**

Funding for the pension benefits by these systems comes mainly from three sources:

1. Employer contributions
2. Employee contributions as a fixed percentage of salary
3. Investment returns on the assets saved in the public trust

Additional funding for LSPRS comes from the fees and taxes collected by the Motor Vehicle Office within the Department of Safety, as appropriated by the legislature, and TRSL

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receives a small percentage of the parish ad valorem tax [LSPRS Valuation, 2013; TRSL Laws and Regulations—current through June 25, 2009].

Public employees who were already employed at the time of the systems' creation were grandfathered into the new systems and given credit for all their years of service. These benefits were granted without sufficient contributions from employer or employee to fund them. When these employees began to retire, they therefore received the full retirement benefits according to the plans, but at first, too few assets had accumulated from employee and employer contributions to cover those withdrawals. Therefore, an unfunded liability was created almost from the outset.

Little statutory structure and political discipline was in place at the time. At least as early as the 1960s, the public became aware that the legislature was passing benefit increase bills without fully funding them. A series of articles on this issue appeared in the *Times Picayune* in 1965 [District Attorney's Association website].

### **Growth of Regulation in the 1980s**

In 1985, the first Commission on Public Retirement studied the already-large UAL, and in 1987, the constitution was amended to require the state systems to be funded on an actuarially sound basis.

In 1988, the legislature created PRSAC (the Public Retirement System Actuarial Committee) to have major oversight of the public pension systems. That same year the legislature passed the Louisiana Public Retirement Law creating Title 11 of the Revised Statutes, to gather public retirement laws into one place as part of maintaining the public retirement systems “on a sound actuarial basis.” In 1991 and again briefly in 2003 other Commissions on Public Retirement were formed.

The Public Affairs Council of Louisiana (PAR) over the years has continued to make recommendations to the legislature and to the public about pension costs as one of the “big ticket items” in the state budget. Some of PAR's recommendations, along with some of the work of the legislature's 2011 Commission on Streamlining Government, became laws intended to both reduce future costs and better ensure sound systems.

## **Taking Control of Pension Funding**

Louisiana started fairly early, compared to many states, in taking control of its future liabilities and reducing pension costs - through legislation, constitutional amendments and benefit reductions. The Revised Statutes, Title 11: sections 1-3 now containing 3,870 laws are the actual public pension “plan,” in the form of the “Louisiana Public Retirement Law.”

Some of the measures taken include:

- The constitutional amendment in 1987 required the state systems to be funded on an actuarially sound basis.
- A funding system and funding rules were set to amortize the initial (as of 1989) unfunded liability through 2029 so it would be fully paid by that time.
- In 2007, the constitution was amended to require that if the Legislature enacts any retirement plan changes that increase benefits costs and therefore would increase the UAL, it must also identify a funding source (e.g. general fund or employer contribution) and be fully paid within 10 years.
- In 2009, UAL payments were restructured to allow significantly more funds from investment earnings to be used to reduce the UAL.
- As of 2010, a 2/3 vote of the legislature is required to approve any new retirement provisions that carry a cost.
- A constitutional amendment and legislation passed in 2011 required that at least 5% of any “nonrecurring revenue” be paid on LASERS’ and TRSL’s UAL in fiscal years 2013-14 and 2014-15, and at least 10% in fiscal year 2015-2016 and “every fiscal year after.” The Legislative Auditor in the fiscal note stated it is “likely” that nonrecurring revenue would be available.
- By resolution, as of 2011, any bill or resolution pertaining to retirement must be pre-filed at least 45 days before the opening of the legislative session.
- The legislature voted to end pension benefits for any legislator elected after 1997.

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- Part time public officials became ineligible for public pension benefits after 2012.
  
- As of 2014, a higher percentage than previously of the “excess investment returns” will be dedicated to paying down the UAL. (See the discussion of excess investment returns under Cost of Living Adjustments below.)

**Reduction in Benefits and Increase in Options for New Hires**

A number of changes in pension benefits that have reduced their future liabilities have been enacted by the Legislature for new hires. These do not change the pension liability for existing employees. Some of these changes are summarized in the table on the following page.

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**Selected Cost-Reduction Changes in Pension Plans  
 Enacted by the Legislature for New Hires, 1978-present**

Plan Design Element	LASERS	TRSL	LSERS	LSPRS
Employee contribution rate increase	From 7.0% to 7.5% in 1989; to 8% in 2005. From various percentages to 9.5% in 2011 for hazardous duty personnel. From 11.5% to 13% for judges in 2011.	From 7% to 8% in 1987.	From 7.5% to 8% in 2010.	From 7% to 8% in 1989, to 8.5% in 2009, to 9.5% in 2010.
No. of successive final months of salary to be averaged to compute retirement benefit base.	From 36 mos. to 60 mos. in 2006	From 36 mos. to 60 mos. fro those who became members after 1/1/ 2011	From 36 mos. to 60 mos. in 2006	Pre-1978 12 months, to 36 months in 1978, to 36 months and limited to 125% per year for the final 36 months, to 60 successive months in 2011.
Eligibility for benefits: Years of service/ full retirement age	From 30yrs./any age; 25 yrs./age 55; 10 years/ age 60; 20 yrs./any age with actuarially equivalent reduced benefit to 5 yrs./age 60; 20 yrs./ any age with actuarially equivalent reduced benefit. Changes made in 2006. 5 yrs/age 62; 20 yrs./any age, actuarially equivalent reduced benefit for hires on or after 7/1/2015.	From 5 yrs./ age 60; 25 yrs./age 55; 30 yrs./any age; 20 yrs./any age with actuarially equivalent reduced benefit; to 5 yrs./ age 60 or 20 yrs./ any age with actuarially equivalent reduced benefit. Changes made in 2011.	From 30 yrs./any age; 25 yrs/age 55; 10 yrs./ age 60; 20 yrs any age with actuarially equivalent reduced benefits to 5 yrs/age 60; 20 yrs./ any age with actuarially reduced benefit. Changes made in 2006.	From 10 yrs./ age 50; to 12 yrs./ age 55.
Benefit multiplier	2.5% 3.33% for hazardous duty personnel	2.5%	3.3% to 2.5% in 2010	3.3%
Anti-spiking - Annual salary growth capped at a certain % for purposes of calculating retirement benefits.	Reduced to 25% in 1986, to 15% in 2005 for rank and file. From 25% to 15% for judges & hazardous duty personnel in 2011.	Reduced to 25% in 1986, from 15% to 10% in 2011.	Before 1987 no anti-spiking. Reduced to 25% effective 1/1/1987. Reduced to 10% effective 7/1/1993; increased to 15% effective 7/1/2010.	Reduced to 25% in 1986. To 15% in 2011.
Vesting provisions	5 years at 60	5 years at 60	5 years at 60, member on or after 7/1/2010.	12 years at 55

- LASERS employees hired after 2006 may not apply unused annual or sick leave to reach eligibility for retirement.
- Actuarially equivalent adjustments to benefits for those who retire before full retirement age means the earned benefit is calculated for the greater number of years the employee will be retired and is therefore is a smaller annual benefit.
- Hazardous duty “street life” is considered by many to be shorter than many other occupations.

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**Pension options offered in one or more of the state retirement systems**

- **A self-funded COLA option** was created for new retirees to guarantee themselves lifetime cost of living increases by voluntarily reducing the total monthly retirement benefits they receive by an actuarially equivalent amount. The effect is an average reduction in initial retirement benefits of about 20% and roughly 10 years before benefits are the same as what they would otherwise have been had the retiree not elected this option. This has been viewed as unaffordable by many retirees and is an irrevocable retirement decision once made.
- **DROP** (deferred retirement option plan) - Under this optional plan, once an employee reaches retirement eligibility, he or she may elect to continue working for up to three years and collecting a full salary while deferring their retirement benefits. The retirement benefits he or she would have received if he or she had retired are simultaneously paid into an individual DROP account that becomes available and begins drawing interest when the employee ends DROP participation. The employee's retirement benefit is frozen at the time he or she enters DROP so any later salary increases do not increase the benefit. Neither the employee nor his or her employer pays further contributions and the employee does not earn additional service credit during the DROP participation period. The intention in creating DROP was to encourage experienced employees to continue working. DROP is cost-neutral to the retirement systems.
- **ORP** (optional retirement plan in TRSL only) is an alternative defined contribution plan, administered by private, contracted carriers. Those eligible for ORP are academic and unclassified employees of Louisiana colleges, universities, and community colleges and the state education board who are otherwise eligible for TRSL. Vesting is immediate. As of 2011 employees contribute 8% of salary, of which .05% goes to TRSL for administrative costs. The employer's contribution as of July, 2014 will be set by the relevant boards and must be equal to or greater than the "normal" cost which varies from year to year, (or greater than or equal to 6.2% beginning in F/Y 2019) and must also include the required payments to cover the UAL. The account belongs to the employee who has a choice of investment options. The risk related to the return on investments is the employee's. The decision to enter ORP is irrevocable. No disability benefit is provided. TRSL advises

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ORP may be a good option if the employee does not plan to remain in the current job or in Louisiana for more than five years.

- **Initial Lump-Sum Benefit (ILSB) of TRSL, Initial Benefit Option of LASERS, Initial Benefit Retirement Plan (IBRP) of LSERS, and the Initial Benefit Option of LSPRS** are options for members who do not choose the Deferred Retirement Option Plan (DROP) to receive a one-time lump sum benefit of up to 36 months of that employee's maximum monthly benefit, while also receiving a reduced regular monthly benefit for life. The lump sum is placed in an interest-bearing account within the retirement system and receives annual interest at a rate for LASERS and for TRSL (only those in TRSL and LSERS prior to 2004) of the retirement system's rate of return for that year minus .5% less for administration, and for TRSL and LSERS members choosing the option as of 2004 and after, at the liquid asset money market rate less 0.25% administration fee. LASERS allows any member retiring under regular retirement to use the option upon retirement to take the Initial Benefit Option. TRSL's eligibility for the Initial Lump-Sum Benefit is at any age with 30 years of service or at least age 55 with 25 years of service, or at least age 60 with 10 years of service. The lump sum can be withdrawn in portions monthly or annually, in an amount based on the member's life expectancy.

**Recommendations from the Public Affairs Research Council (PAR)**

PAR's 2005 report, "Public Employee Retirement: A Time for Change" proposed a major overhaul of the four pension systems, starting with a new defined benefit plan to be prepared by national consultants. PAR described the "fragmentation of pension plans", the "disparities in benefits" among the plans, and the "leapfrogging" of one system's members to obtain additional benefits provided by the legislature to another system's members [PAR, 2005, p.1, p. 4]. Note that subsequently some plans were consolidated in 2005 and again in 2010.

Another recommendation in the PAR report was to ensure sufficient time for the Legislative Auditor to report and the legislators to review the effect of any amendment to a pension bill. Currently the Legislative Auditor has a 24-hour minimum to respond as to the effects of the amendment. However, it is not uncommon for the report to be given to the House or Senate Retirement Committee members or to the full legislature at the same meeting where they are to vote on the amended bill.

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## **OVERSIGHT AND RESPONSIBILITY FOR THE STATE PENSION SYSTEMS**

As with all aspects of state government, the pension systems are subject to the U.S. Constitution, relevant U.S. laws and rules (I.R.S. rules in the case of pensions) and the Louisiana Constitution plus the relevant actions of the federal and state courts.

By state statute, oversight for Louisiana's public pensions is shared among a wide array of public officials. The comprehensive chart in Appendix C shows the elected and appointed authorities who make the decisions for the pension systems, along with an outline of their specific roles. Minnesota and Wisconsin's joint legislative standing commission and committee are discussed for comparison with the role of PRSAC, as well. Appendix D shows the required make-up of each Board of Trustees, as well as a list of member advocacy groups for each pension system generally participating in public process with the legislature.

## **THE PROBLEM THAT LEADS TO HEADLINES - THE UNFUNDED ACCRUED LIABILITY OR "UAL"**

### **Why care about the UAL?**

It is true that all four state pension systems have significant unfunded accrued liabilities (UALs) and that undoubtedly catches attention. The total number of Google News citations talking about the "crisis" of unfunded pension liability in the states peaked in 2010-2011. [Munneill, p. 2] The articles predicted a "day of reckoning" [Kellogg Insight], that will severely challenge the states' ability to meet their promises. "Unfunded" and "liability" taken together gave rise to headlines like "ticking time bomb" [more than 9 entries on the internet, "fiscal albatross" [*Pelican Post*, February 1, 2011] and "looming public pension crisis" [*Pelican Post*, April, 2011].

- According to Moody's Investor Services, reporting in 2013 on 2011 numbers, Louisiana had the 8th largest pension liability and the 7th highest liability per capita in the nation.

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- According to the Louisiana Legislative Auditor in a March 6, 2013 report, as of the end of Fiscal Year 2012, the UAL had risen to about \$19.3 billion-- up from \$5.8 billion in 1989.
- Again according to the Louisiana Legislative Auditor, the fiscal year 2013 Funded Ratios (the ratios of assets in each system divided by the level of pension obligation or liability in each system) of the 4 state systems were: LASERS, 60.2%; TRSL, 56.4%; LSERS, 62.1%; and LSPRS, 59.44%. These numbers are down from what the Public Affairs Research Council (PAR) reported in 2005 as nearly a 90% average in 2000 across all 15 state and statewide systems (not necessarily a fair comparison according to some of our sources,)

It is tempting to panic. If a household only has about half of the assets needed to cover its liabilities, it would seem to be in bad financial shape. Before concluding that, however, there is more to the picture. We will come back to this household analogy below [p.21].

One note: A “standard” for “healthy’ funding of a pension system commonly cited in media coverage of pension issues and by some academics is a Funded Ratio of at least 80%. By that standard, and in comparison to the Funded Ratios of many other states’ systems, Louisiana looks as if it’s in trouble.

In 2012, however, the American Association of Actuaries published an Issue Brief entitled “*The 80% Pension Funding Standard Myth.*” In it, the Brief argues that “Most plans should have the objective of accumulating assets equal to 100% of a relevant pension obligation” [p. 2]. However, they further state that in order to assess the health of a pension system, other factors must also be included, such as “Funding or contribution policy and whether [state employer] contributions actually are made according to the plan’s policy” and “investment strategy, including the level of investment volatility risk and the possible effect on contribution levels. Each of these factors should be examined over several years....” [pp. 2-3.]

To answer the question of whether we should panic in Louisiana and if so, how much, we considered these other factors and took a closer look at the UAL to understand exactly what it is, how it got there, how and why it grows or shrinks, what has already been done about it in the four Louisiana state systems and what else could be done about it.

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**How the Liability Is Created**

The future liability of a retirement system is based on several factors:

- The composition of the current workforce (age, gender, whether or not engaged in hazardous duty, etc.) and current retirees.
- Life expectancies for that workforce and those retirees.
- Plan design features that the Legislature affects, e.g. normal and early ages for retirement eligibility, how many years' salary are averaged to create the base for retirement benefits, the "multiplier" factor, and policies on applying unused vacation and/or sick leave as qualifying periods of employment. (See Appendix E for a more complete description of how retirement benefits are calculated.)
- Salary structure and projected future salary structure of the workforce.
- Years to vest, i.e. the number of years of employment required for an employee to have a guaranteed right to retirement benefits (be "vested".)
- Estimates of how many employees will leave employment before vesting or before early or full retirement.
- Estimates of future investment earnings on contributed funds. (NOTE: This calculation is based on an estimated rate of return known as the discount rate . The discount rate is a critical estimate as we discuss below on p.22.

**The Unfunded Accrued Liability (UAL) and the Funded Ratio**

In simplest terms, the unfunded liability of a pension system is the percent of funds the state is constitutionally obligated to pay in pension benefits in the future (the liability) that has not yet been accumulated as assets are invested. "Accrued" simply means the amount of liability that has already accumulated at a point in time, based on the workforce at that time. Another way to state this is that the UAL is the difference between a system's already-accrued obligations and the current actuarial value of its assets.

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We described the “Funded Ratio” above and noted that the funded portion of the accrued liability in the four state pension systems in fiscal year 2013 ranged from 56.4% to 62.1%. Therefore the unfunded portion ranged from 37.9% (100% minus 62.1%) to 43.6%.

**What Makes the UAL Grow (Or Shrink?)**

The combined UAL in the four Louisiana state systems in 1987 was \$5.8 billion. It is now in 2014 around \$20 billion. What happened? The answer has two parts.

**Part I - The “Initial UAL” in 1987.** First, in 1987, as described above, the Legislature amended the Constitution to require that the state retirement systems be funded on an actuarially sound basis. Prior to that time, they were not and benefits could be and were approved without adequate funding appropriated. The benefits resulted in accrued liabilities but the funding wasn’t there. The 1987 amendment required, in part, that the UAL at that time, approximately \$5.8 billion, be eliminated. To meet this constitutional mandate, the Legislature established a 40- year amortization (payment) schedule with increasing annual payments beginning July 1, 1988. This UAL is referred to as the initial UAL or IUAL. Under the state Constitution, it must be paid off by 2029 [Office of Louisiana Legislative Auditor, “Overview of Louisiana’s Unfunded Accrued Liability,” May 20, 2011].

**Part II - The UAL Since 1987.** The UAL has continued to increase due to several factors. As it increases, again, the State is constitutionally obligated to meet the increased liability.

As noted above, the 40-year payment schedule for the Initial Unfunded Accrued Liability (IUAL) was designed to have larger contributions in later years. The schedule was further modified in 1992 pushing the necessary later year contributions higher. Until about 2012-2013, the employer contributions were less than the level of interest, so the liability principal continued to grow. In other words, unpaid interest added to the principal each year.

There were investment losses, especially following 9/11/2001 and again following the 2008 economic downturn. Whenever the invested funds fail to grow as anticipated, the UAL increases.

LASERS reported significant decreases in member contributions attributed to the loss of current employees through privatization of some state services with resulting reduction in workforce and both LASERS and LSPRS to state-mandated freezes in hiring and in merit

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pay raises. [LASERS, Comprehensive Annual Financial Report, 2013, page 22; Independent Auditor's Report, LSPRS, 2012, 2013]

Some investment gains of the pensions' assets were approved by the legislature to pay cost-of-living adjustments. These adjustments in turn increased future benefits for the same employees and therefore the state's liability (See below.) At the same time, because of cost-of-living adjustments, the full amount of investment gains could not be used to offset investment losses.

Some expansion of the benefits themselves, mainly in LSERS and LSPRS, were authorized by the Legislature, again increasing the future liability. LASERS' and TRSL's benefits generally have not been expanded other than with cost of living adjustments and, in several cases, have been reduced for new members.

Inevitably, actuarial estimates of the various factors - salaries, number of retirees, those disabled and the number who died - differed from what actually occurred. On balance, these differences have represented losses that increased the UAL.

It is important to note that reforms enacted by the Legislature between 2005 and 2013, and especially Act 399 in 2014, have and will result in significantly faster reduction of the UAL and have strengthened fiscal stability of the systems.

**What's Happening to the UAL Now?**

Each year, the Legislature must appropriate pension contributions according to the formula that represents paying down the UAL. The legislature must also consider the additional accumulated UAL plus the amount to keep up with new liability accrued in the prior year for current employees (the so-called "normal" cost.) In other words, the State is now playing "catch-up" in funding its state pension systems.

We noted that the "normal" cost of benefits now accruing for existing employees has remained fairly stable throughout recent years and is approximately the same as the analogous cost in the Social Security system. This means that the majority of employer contributions now are due to the state's previously unfunded liability and not to the current employee benefit level.

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As a result of this “catch-up” to pay off the UAL and the formula for calculating the annual required contribution for normal costs, the total employer contribution rates in 2014 are: for LASERS (aggregate of all subsystems) 37.4% of payroll; for TRSL (aggregate of all subsystems) 27.7% of payroll; for LSERS 33.0% of payroll; LSPRS 75.2% of payroll. LSPRS has a number of special characteristics that account for this rate including higher risk occupations, shorter careers and therefore longer retirements of members [Public Retirement Systems’ Actuary Committee: Recommended Employer Contribution Rates for Fiscal Year 2014-15, March 25, 2014].

**The Home Mortgage Analogy**

Going back to the analogy of a household, the UAL is somewhat like a home mortgage. At a given point in time, a household probably does not already have available all the money it will ever need to pay the mortgage off. If one or more household members are employed, however, and the payments are being met each month, the lender will know that the mortgage will be paid off on a predictable schedule. The debt is considered to be relatively safe. Similarly, the formula for the state’s paying off its UAL has been locked into state statute since 1989 with a revision in 2002, and the required state employer contributions, calculated according to sound actuarial principles, have been made each year.

Also, at a certain point in the course of paying off a mortgage, the majority of each payment begins to be applied to principal and the household’s “unfunded liability” begins to be reduced significantly. The UAL in the state systems is at a similar point in 2014.

The difference is that with a home mortgage, usually at least a small part of each payment applies to principal from the beginning. With the systems, payments prior to about 2012 in LASERS and prior to 2014 in the other systems have not applied to the principal of the UAL because the payments were not enough to cover the interest that had already accumulated. On the contrary, unpaid interest actually increased the UAL as described above. The result is an increase in the required contribution from the various public entity employers each year.

Starting roughly now (a couple of years earlier in some cases,) as long as the employers make all the required contributions as scheduled, which they must do by law, the principal will be reduced each year until 2029. Employer contributions will rise only slightly over the next few years and will drop after 2029 when the Initial Unfunded Accrued Liability is paid off.

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### **Impact of the Discount Rate Assumption**

The annual required employer contribution (the ARC) rate is derived from all the actuarial factors and assumptions mentioned above under calculating the UAL. The employer contribution calculation is very sensitive to the assumed rate of return on investments, the “discount rate,” and this assumption is the subject of considerable controversy.

The discount rate means, in essence, that we “discount” the level of funds we think we will need to pay future pension commitments by the rate we expect investments of the funds to earn. This calculation impacts the required employer contributions. The more optimistic or higher the estimated rate of earnings of each pension system is, that is the discount rate, the lower the calculated employer required contribution is for the year. Conversely, the more pessimistic the estimated discount rate for each pension system is, the higher the calculated employer required contribution is for that year. *(Note that lower employer contributions as a result of overly optimistic discount rate assumptions will lead to the UAL’s increasing and so will lead to higher contribution rates in the future. Conversely, higher employer contributions as a result of overly pessimistic discount rate assumptions will lead to the UAL’s decreasing faster and so will lead to lower future contributions.)* While the discount rate is just an estimate, once agreed upon by the Public Retirement Systems’ Actuarial Committee (PRSAC), it translates into the real dollars that must be appropriated to the pension funds by law.

The discount rate reflects best-guess expectations of the investment markets of each pension system. Even though the systems employ professional investment consultants who have access to extensive information to advise on the discount rate assumption, it remains an estimate and not a certainty. The real UAL, however, will reflect the actual performance of the relevant markets and the investments. If the discount rate is estimated higher than the markets actually perform, not enough money will be contributed by the employers and the UAL will increase. If it is estimated lower, the UAL will decrease.

The discount rate used by LASERS and TRSL was 8.00% in 2013 and will be 7.75% in fiscal year 2015. The discount rate used by LSPRS is 7.5%. LSERS’ discount rate prior to 7-1-2013 was 7.5%, and effective 7-1-2013, it is 7.25%. The discount rate used by LSPRS as of 6-30-13 is 7.0%. Historically, over several decades, these pension systems’ investments have earned an average return that approximates or exceeded these rates.

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The systems consider these discount rates to be reasonable. The majority of pension systems nationwide use a discount rate of 7.8% to 8.0%. The Louisiana Legislative Auditor singled out LASERS and TRSL as having investment programs that are particularly well-managed by their professional investment consultants and managers but also noted that all of the state systems' programs are very professionally managed.

Others, however, believe these estimated discount rates are too high.

- Some academics have said that the market cannot be relied upon to produce rates of return in the future as high as in the past so past history is not a reasonable basis for setting the discount rate assumption. They argue for the use of a more conservative, lower discount rate [Kellogg Institute, Joshua Rauh].
- A report issued in 2013 by the public policy non-profit organization, State Budget Solutions, asserted that a prudent discount rate would be the 15-year U.S. Treasury bond rate of 3.2% [State Budget Solutions].
- In June, 2013, Moody's Investor Services used a discount rate for Louisiana of 5.67% in its report, based on its assessment of market expectations [Moody's Investors Services, Appendix, Table 1].

Were any of these lower discounts rates actually to be adopted, the annual required employer contribution would rise dramatically. Even though the UAL would decrease faster, without new state revenues, the budgets of state employers would be negatively affected. The Actuarial Standards of Practice [Actuarial Standards Board] state that the discount rate should aim to be genuinely realistic, neither overly optimistic nor pessimistic. Since the funds that public employers contribute to pensions ultimately come from the taxpayers, an overly optimistic rate penalizes future taxpayers and an overly pessimistic rate penalizes current taxpayers.

**Impact of Investment Strategies by the Boards of Trustees and Staff**

The Boards of Trustees and their professional staffs seek to achieve a rate of return on investments that is close to the assumptions used to develop the discount rate. At the same time, they adhere to the standard of "reasonable prudence," against risks.

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The Boards follow the recommended practice of smoothing their asset returns up to five years of gains and losses to reduce the effects of market shifts [Interview and Pension Funding Task Force, 2013].

The Boards of Trustees use professional investment advisors who are independent of the multiple investment managers who, in turn, manage the investment of each different asset category, such as domestic and international stocks, private equity securities, fixed income securities, and other assets. Investment policies and guidelines are developed by the respective systems' Boards of Trustees. Each of the system's Board of Trustees makes its own decisions about which advisors and managers to employ and evaluates their performance at set intervals.

The Legislative Auditor stated, in his 2013 report on "The Funded Status of Louisiana Retirement Systems," that "... the boards of the state systems include taxpayer and employer representation. As a result, state retirement boards have developed investment policies with appropriate checks and balances and have generally produced outstanding investment results compared with similar retirement systems throughout the country."

**Impact of the Multiplier Factor**

The "multiplier" is part of the calculation of retirement benefits for a given employee. The multiplier is just one of many factors used in benefit calculation. See Appendix E for a more complete description of this calculation.

The higher the multiplier, the higher the lifetime retirement benefit is and so the higher the state's liability for that benefit becomes. The multiplier factors in Louisiana are 2.5% in most of the sub-plans in LASERS, TRSL, and in LSERS and 3.3% in LSPRS.

To put these numbers in some context, the table below shows multiplier rates in five states for which we were able to find rates as of 2012. Note that, except for the major systems in Ohio, these states participate in the Social Security system for their employees, so their state pensions are viewed as supplements to Social Security.

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**Multiplier Rates in Selected States as of 2012**

State	Multiplier
Alabama	From 2.0125% to 1.65% with a cap of 80% of final salary for “tier II” employees State police from 2.875% to 2.345%
New York	Teachers, state and local employees: < 25 years service - 1.67% 25-30 years - 2% >30 years - Benefit is 60% of final annual salary plus 1.5% for each year over 30 years.
Ohio	From 2.2% plus .1% for each year over 30 years to 2.2% plus .1% for each year over 35 years
Virginia	From 1.7% to 1.65% for all employees except state or local police or hazardous duty employees.
Wyoming	From 2.125% for first 15 years and 2.25% for years > 15, to 2 % for all. Firefighters remain at 2.5% by law.

Source: National Conference of State Legislatures, “Pension and Retirement Plan Enactments in 2012”

**Cost of Living Adjustments (COLAs)**

The purpose of pension cost of living adjustments is to keep pace with inflation to ensure that retirees maintain the buying power of their retirement income. Whenever a cost of living adjustment is made, it increases the cost of benefits for that year and all future years. Cost of living adjustments are now known officially as Permanent Benefit Increases or PBIs but are still frequently called by the former name, COLAs.

In 1992 the Legislature established an account, known as the “Experience Account,” for funding COLAs. Until 2014, whenever the investment of pension funds earned a higher rate of return than the discount rate, a significant portion of the “excess” earnings was applied to the UAL. Then additional “excess” could be applied to the Experience Account. For example, for LASERS after the first \$100 million of “excess” over the predicted earnings was applied to the UAL, 50% of the additional excess would be allocated to the Experience Account. Because COLAs are fully paid for by the Experience Account, when a COLA was granted, it did not increase the employer contribution.

The funds, as well as investments nationally, experienced especially high losses in the 2001-2003 and 2008-2011 periods and the UAL increased substantially. Some critics were concerned that while all investment losses served to increase the UAL, only a part of

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investment gains over time were available to offset those losses and the accompanying rise in the UAL.

According to the Legislative Auditor, the state used \$2.4 billion since 1989 to provide COLAs. LSERS and LSPRS have not had sufficient gains to credit any funds to the Experience Account between 2007 and 2011. LSERS did make a deposit to the Experience Account in 2012. LASERS and TRSL have allocated gains to the Experience Account since 1992 when possible but have not provided a COLA since 2008. LSERS granted a COLA in 2013. [Louisiana Legislative Auditor, "The Funded Status of Louisiana Retirement Systems, 2013]

**Status of COLAs in 2014 and The Future**

In 2014, the legislature passed and the governor signed into law Act 399. This Act granted a 1.5% COLA in each of the four systems but also made significant changes to the funding of the Experience Account and the possibility of future benefit increases, changes that will result in savings in the long-term and in decreasing the UAL sooner according to the Legislative Auditor's accompanying note. The COLA of 1.5% represents a modest increase, e.g. \$28 per month on average within TRSL.

Prior to 2014, some held the view that no COLAs should be provided in any system until the UAL from the past was completely paid off (i.e. the Funded Ratio was 100%) and the State was contributing only currently accrued ("normal") costs each year. (Normal cost would generally be between 6 and 6.5% of payroll, depending on actuarial factors and the experience of the system.) Others point out that any benefit increase to retirees is likely to be mostly spent in the state thereby stimulating the state's economy and generating a certain amount of offsetting tax revenues. Act 399 struck a compromise between these two points of view.

To put it simply, Act 399 restricts future retirement benefit increases and restricts allocations to the Experience Account that finances those increases, according to a formula that is tied to the systems' Funded Ratios. Until each system's Funded Ratio reaches at least 65% (all four are below that level currently) ALL "excess" earnings (earnings above the estimated rate of return or discount rate) must now be applied to the UAL and to the oldest part of the UAL first for each system. As Funded Ratios reach 75% and again at 80% the formula changes to allow somewhat more flexibility, accumulation of experience account funds and

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the possibility of modest cost-of-living benefit increases. A detailed description of the provisions of Act 399 can be found on the Legislature's website ([www.legis.la.gov](http://www.legis.la.gov)).

**PENSION SOLVENCY, AT WHAT COST?**

Under the constitution and current law, the UAL in Louisiana is being paid down, but to do so, the employer contribution rates are very high. The bulk of the employer contribution rate is due to the UAL and not to the current cost of benefits. To review, the rates recommended for 2014 are for LASERS 37.4% of payroll; for TRSL 27.7% of payroll; for LSERS 33.0% of payroll; LSPRS 75.2% of payroll.

The "employers" in this case again are individual state agencies, departments and programs such as education, natural resources, economic development, public safety, social services, health care and public health, transportation, and others. "Employers" also include individual public school districts, higher education institutions, the Treasurer of Louisiana for the State Police, and any entity whose employees are members of the state retirement systems. TRSL alone lists 208 employers for 2014 and LASERS listed 355 as of 2011.

When employers must by law pay these rates of contribution (percentages of payroll) for their employees AND their budgets remain fixed or are reduced, the inevitable result is a serious tightening of the budget for or elimination of some other programs and services. In the absence of new revenues, every part of government at all levels is squeezed, sometimes severely. Even though employer contribution rates are not expected to increase significantly going forward, the rates that exist today already put pressure on the various employers' budgets.

If the public does not want to accept the resulting changes or reductions in services, the only alternative is to increase revenues to deal with the pension programs' UAL, either by increasing taxes or by issuing pension obligation bonds (POBs,) a strategy sometimes used in other states. POBs are problematic as we discuss under Options below.

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**OTHER ISSUES AFFECTING PENSIONS IN 2014 AND THEREAFTER**

**GASB**

The Governmental Accounting Standards Board (GASB) sets standards for financial reporting by governmental agencies. New standards (GASB Statements 67 and 68) will affect how pension costs are reported beginning in 2014 and 2015 and require governments to recognize pension obligations as formal liabilities.

Under the new GASB standards, governments will be required to calculate their “*net pension liabilities*” and to report that liability directly on their balance sheets (the asset and liability section of their financial statements) rather than in a footnote to their financial statements as they have in the past. *Net pension liability* is the “difference between the total pension liability (the present value of projected benefit payments to employees based on their past service) and the assets (mostly investments reported at fair value) set aside in a trust and restricted to paying benefits to current employees, retirees, and their beneficiaries” [Governmental Accounting Standards Board News Release, June 25, 2012]. The impact of these new standards will be much greater transparency and public visibility of the real liabilities that exist for pensions for current and former government employees. The GASB does not dictate what governments should do about pre-funding those liabilities but will ensure that whatever they do, it will be visible. The impact of that visibility remains to be seen. There is a risk that the new standards will create confusion for the public and legislators as they try to discern what all the new numbers mean.

**BEST PRACTICES**

There is broad-based agreement in best practice reports by the professional associations reviewed on several key points. Public pension benefit design must balance multiple needs:

- the need for funds in the future to meet promised commitments;
- the need for doing so at a cost the public is willing to pay;
- the need for fairness to those in public service;

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- the need of the state for sufficient incentives to hire and keep effective and efficient public employees.

Pension best practices are based on sound actuarial principles and standards of good government. The goal is a thoughtful, pro-active rather than re-active, very public process involving all stakeholders and using an actuarially valid approach.

As we have noted above, many if not most of these best practices have already been put into practice in Louisiana. The State has diligently made all required payments to the retirement systems since 1989, for example, and discount rate assumptions have been lowered.

Here is a summary of best practices we found in the literature.

**Be disciplined and make the necessary actuarially determined contributions.**

- Keep politics out of this obligation.
- When there are savings from pension reforms, they should not go into the general fund but should accrue to the pension systems.
- If the state's required payments are not made, public employees should be prepared to sue to force the state to do what is necessary to protect their pension programs' solvency.
- Monitor assets, investment performance, and the system's ability to pay normal costs regularly.
- Gather and disseminate verified longitudinal data on a system's performance.
- Base contribution calculations on a discount rate that is a best estimate, neither overly optimistic nor overly pessimistic, to be certain that programs do not become underfunded in a poor market nor employers and taxpayers overcharged in a good market.

**Be pro-active in identifying potential risks and taking steps to reduce the impact of adverse events.**

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- Take steps to ensure the state’s ability to deal with market losses in a recession.
- Do a “stress test” on each system by projecting what would happen if the assets earned a much lower rate than anticipated.

**Make employer costs a consistent percentage of payroll.**

- Smooth the contribution rate calculation to reduce year-to-year fluctuation.

**Be transparent. Report publicly all costs, actual results and strategies being used to handle the results.**

- Set and require a standard of openness, public access, and clear and objectively presented reports. Be sure the public knows how and when the pension plan(s) will be fully funded.

**Pay now for the future benefits of current employees within the plan. Maintain “generational equity.”**

- “The contribution-allocation procedure should include a funding target based on accumulating the present value of benefits for members by the time they retire, and a plan to make up for any variations in actual assets from the funding target within a reasonable time period” [American Academy of Actuaries, “ Objectives and Principles for Funding Public Sector Pension Plans,” p. 1].

**Offer retirement benefits that are “adequate” and “fair” from multiple perspectives.**

- Benefits should be sufficient to provide a solid foundation for retirement security for retirees.
- Benefits need to be effective in recruiting *and* retaining high quality employees for a stable workforce.
- Benefits need to be fair to taxpayers, including making sure other vital public services are not displaced by pension costs.

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- Benefits need to be compatible with a changing workforce and demographic trends.

**Recommendations of the Louisiana Legislative Auditor**

In line with these best practices the Legislative Auditor in his 2014 Legislative Report states:

*“Because of the concern for sufficient funding in the future to meet the obligations of the state’s retirement systems, it is imperative to establish actuarial assumptions that are more likely to produce favorable outcomes rather than new UAL. While a more conservative approach will cause employer contributions to be larger in the short term, funded ratios will increase and the systems will become sounder.*

*By calling these issues to the attention of lawmakers, agency management, and the public, the Legislative Auditor hopes to encourage open, transparent discussion on how best to address these concerns, and, ultimately, to improve the efficiency and effectiveness of government for all of the state’s residents.”*

The Legislative Auditor’s specific recommendation to lower the discount rate assumption has been the subject of much discussion within PRSAC. Doing so would increase the required employer contribution and exacerbate problems of displacing or diminishing other government services in the absence of new revenues. Nonetheless, the best practices we have identified do suggest using a discount rate assumption that represents a best guess estimate of future earnings, erring only on the side of a low level of risk, i.e. a lower rate.

**OPTIONS**

**A Legal Opinion on Federal and State Constitutionality**

In 2012 the Louisiana Legislative Auditor requested legal research by Strasburger Attorneys at Law in order to write the actuarial reports for seven proposed bills under consideration by the legislature. Six of the bills were to make changes in the benefits for current employees and new hires. The seventh bill proposed a study on consolidating the systems.

The legal opinion found the change-in-benefit bills for current employees likely to be held by the courts in violation of either the state or federal constitution since they would reduce benefits already earned by those in the retirement systems. The system merger bill also

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proposed a study on merging the assets of the LASERS and TRSL, and the legal opinion was that such a merger of assets also appeared to violate constitutional requirements for actuarial soundness since the systems are funded differently [Louisiana Legislative Auditor, Memorandum].

**Changes in Benefit Features - New Hires**

Overall, benefit changes for new hires do very little to reduce the UAL, the largest problem affecting employer contribution rates and therefore costs to the employers. This “con” is true of all the following options.

- **Raise the full retirement age**
  - **Pro** Employees contribute over a longer period and therefore contribute more toward funding the liabilities of the program. Delays the payout of employees’ benefits.
  - **Con** Raising the retirement age is a benefit reduction. Creates an incentive for older employees to stay on the job, reduces job opportunities for younger workers. There may be higher costs for disability benefits. Employees with hazardous duty and physically demanding jobs may well not be able to work until higher ages. From the employee perspective, benefits are received over a shorter period.
  
- **Increase the number of years of service required for full retirement benefits.**
  - **Pros and Cons** are similar as for raising the retirement age.
  
- **Establish a minimum replacement of lower salaries to ensure that long-term, low-paid workers’ benefits stay above the poverty level when they retire.**
  - **Pro** Provides for some level of basic economic security for long-term workers as a matter of fairness. May reduce state costs for social services for these retirees.
  - **Con** Pension costs are higher.
  
- **Increase employees’ contribution rates (note that in terms of current, “normal” cost, employees already pay a higher percentage than employers.)**
  - **Pro** Helps reduce the UAL faster.
  - **Con** Lowers employees’ take-home pay and therefore may reduce the effectiveness of pension benefits as a recruitment and retention tool and reduces the state’s competitiveness against the private sector in the labor market.

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- **Index COLAS to a “chained” consumer price index as has been proposed (but not enacted) at the federal level.** The federal Social Security system now increases benefits annually based on the Consumer Price Index for Urban Wage Earners and Clerical Workers known as the CPI-U. That index is created from the increase in prices of a market basket of goods and services typically purchased by urban consumers and is intended to ensure that benefits are not eroded by inflation. The idea of a “Chained CPI” refers to indexing COLAs to a price increase measure for a different market basket in which substitutions have been taken into account, assuming retirees lower their expenditures by making such substitutions and therefore need less.
  - **Pro** Decreases the level of future COLAs and therefore provides compounded savings as to the present calculation of COLAs. May allow for some COLAs if the alternative under existing rules is none at all.
  - **Con** Does not reduce the existing UAL. Some have argued at the national level that a chained CPI index for COLAs will systematically lower the real buying power of retirees and that chained CPI does not reflect the actual inflation faced by retirees.
  
- **Prohibit any COLAs until the prior UAL is paid down or is paid to a specified level.**
  - **Pro** Avoids increased future costs. (Note: Act 399 of 2014 essentially does this.)
  - **Con** May be perceived as unfair to retirees, especially if inflation increases and therefore their real buying power diminishes.
  
- **No longer provide retirement benefits for part-time workers**
  - **Pro** Lowers employer costs
  - **Con** Weakens the ability of employers to recruit and retain part-time workers.
  
- **Lower the higher salaried employees’ defined benefits by placing a cap of an amount as the final salary base for their defined benefit pension.** (Note: Act 399 in 2014 enacted a cap of \$60,000, indexed.)
  - **Pro** Reduces cost of pensions for higher salaried employees. Encourages other forms of employee savings.
  - **Con** Reduces incentive for skilled, and therefore higher paid, workers to remain in public sector service to full retirement age.

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### **Changes in Funding**

- **Issue Pension Obligation Bonds to raise funds to reduce the UAL**
  - **Pro** Provides an influx of cash into the pension funds and therefore reduces the UAL by the amount of the bond issue and increases the funded ratio. May allow investment of these new funds at a rate of return that is greater than the interest to be paid on the bonds and so increase the assets of the system.
  - **Con** Increases risk for the state and cost in the case of adverse markets if the rate of return on system assets is lower than the interest rate on the bonds. Likelihood of political pressure to increase benefits if the systems become fully funded, thereby increasing long-term costs. Could lower the state's credit rating, although both Moody's and Standard and Poor's have stated that substituting one kind of debt for another in this way would not necessarily lower credit ratings, all other factors being equal. The Public Affairs Research Council advises against Pension Obligation Bonds.
  
- **Raise taxes to reduce the UAL**
  - **Pro** As long as taxes are applied to the UAL specifically, reduces the UAL and improves the Funded Ratios without displacing other public services. Taxes could be raised to provide for all state needs, including reducing the UAL.
  - **Con** Some consider any tax increase to represent a drag on the overall state economy and a weakening of the ability of the state to attract investment and employment. Could be difficult to ensure that any new revenues intended to be dedicated to paying down the pension UAL were not absorbed into the general fund.

### **Changes in Benefit Design Structure – New Hires**

- **Merge the administrations of the state retirement systems.**
  - **Pro** May save overall personnel costs for any duplicative pension system staff. Creates a larger asset pool for investment, which may allow more aggressive investment for higher returns and diversification to mitigate the risk.
  - **Con** Merging the assets of the systems may be in violation of constitutional requirements. There is no indication that any of the systems are poorly run, and in fact, they have been acknowledged to be very well run with effective investment

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strategies. History and constituencies of the systems differ so much that the current number of staff might still be required, i.e. few or no economies of scale.

- **Join the Social Security system**
  - **Pro** More than eighty percent of other states are now part of the Social Security system for their employees. Joining could allow the state to reduce its liability for new employees since state pensions would then be a supplement to Social Security benefits rather than the full retirement benefit for those retirees.
  - **Con** This would lock the state into the Social Security employer contribution rates. Current Louisiana public employees' retirement "normal costs" are lower in many cases, so this would represent an increase in costs. There are also significant negative transition issues (see our suggested readings for more detail.)
  
- **Create a new defined benefit plan** This was the recommendation of the Public Affairs Research Council (PAR) - that a new plan be created and designed by outside consultants ["Public Employees Retirement: A Time for Change, March, 2005].
  - **Pro** Creates an opportunity to make pension plans more uniform and reduce of the number of plans offered and the disparities among the plans. Would reduce "leapfrogging" of one system's members to obtain additional benefits offered in another system's plan.
  - **Con** Cost to design and implement the plan. Potential loss of employees not yet vested in current systems during the planning stage. Would still need mechanisms to avoid unbalancing the plan through additional legislation specific to particular employee groups.
  
- **Convert the defined benefit plans to defined contribution plans** for new hires.
  - **Pro** Eliminates the state's future liabilities for the covered employees. The state's obligation would only be to make the required employer contributions, though the obligation for the existing UAL would remain and not be alleviated by this option.. Simpler for the state to administer. Vested benefits could be portable for employees who change jobs to the private sector or who move out of state.
  - **Con** From the employee's perspective, places all the investment risk on the employee. Without the Social Security benefits provided by the majority of other states, the state would still be required to pay at least the equivalent of the employer's share for Social Security. Fewer employees would be paying into the current retirement systems, further increasing the UAL. May not provide an adequate retirement income for some employees. Experience shows many

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employees withdraw their benefits in a lump sum at retirement, and in the absence of Social Security, may leave some public retirees below the poverty level. Loss of ability to recruit and retain employees competitively unless salaries are increased. Lessens incentive for experienced employees to remain in Louisiana throughout their careers.

- **Create a “Stacked” Hybrid Option** This option would consist of a Defined Benefit plan based on a pre-determined salary cap and a mandatory Defined Contribution plan beyond that cap.
  - **Pro** Provides a fully defined benefit plan for many of the public employees with lower pay. Exposes the state to less pension liability in the case of investment losses. The state does not need to pay the cost of a fully defined benefit pension for top executives with high levels of salary. Provides a protected pension base for higher earners.
  - **Con** The plan’s constitutionality must be examined first. May be tempting to reduce the defined benefit part of the plan to a level that does not provide an adequate retirement income for lower paid employees. Employee bears some of the investment risk for the portion of the pension that is under a defined contribution plan. A category for hazardous duty personnel may need to be established separately [Munnell, pp. 206-208; Center for Regional Politics, pp. 15-16].
  
- **Create a “Cash Balance” Plan** This is the plan proposed by the Governor of Louisiana in 2012 for new hires in LASERS and higher education members of TRSL, passed by the legislature but subsequently declared in violation of the constitution because it did not pass by a  $\frac{2}{3}$  vote. Benefit calculation based on the actual earnings of the required contributions (8% employee and 4% employer) and not on final salary. State guarantees contributions will not lose value. At retirement, they may be annuitized or taken as a lump sum.
  - **Pro** May mean savings for the state whose guarantee is based on what the accounts actually earn in the market. Avoids salary “spiking” to increase defined benefit plan benefits. For employees, their account is guaranteed not to lose value and is portable.
  - **Con** As passed in 2012, minimal disability or survivor benefits. Requires building a consensus that does not exist at present on what a fair benefit level is, given that employees do not participate in Social Security. State is at risk for losses in a bad market, therefore could create an unfunded liability. Legislative Auditor claimed there

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would not be significant savings for the state for new employees vis-a-vis the existing plans as they have been modified for new employees. Less incentive for experienced employees to remain in public service. Legislative Auditor claims benefit would be lower for employees with more than 20 years service but higher for shorter term employees than the current plan [Public Affairs Council of Louisiana, “ Governor’s Cash-Balance Plan Offers Advantages But Questions Remain about Its Ultimate Impact,” April, 2012].

### **Changes in Procedure**

- **Create a written set of principles and pension goals to guide policy** The most likely entity to undertake this would be PRSAC.
  - **Pro** Provides guidelines and benchmarks to compare proposed pension legislation. May avoid short-term measures having long-term negative consequences and help counter special interest pressures. Allows consideration of equity across systems or sub-plans where appropriate. Suggests need for in-house study before action.
  - **Con** Time consuming and would require considerable use of staff resources to develop and reach consensus.
  
- **Establish PRSAC as the preliminary body of review for all proposed pension legislation**
  - **Pro** Given the complex financial nature of pensions, the intended and unintended consequence of proposed pension bills and their amendments can be vetted by a careful, informed review and revision where needed.
  - **Con** Slows down the legislative process.
  
- **Ensure sufficient time for Legislative Auditor and legislators to analyze and review any amendment to a pension bill**
  - **Pro** Would provide due consideration of the effects of any amendment to pension systems and for public input, beyond the current 24-hour minimum delay before voting. Would provide the Office of Legislative Auditor more than 24 hours to report to the legislators and would provide the legislators time to read and consider the Legislative Auditor’s report.
  - **Con** Slows down the legislative process

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General positions that are relevant to public pension policy and that are already supported by the League of Women Voters of Louisiana and the League of Women Voters of the United States are listed in Appendix F.

## **CONCLUSION**

The question we posed was “Should we panic about public pensions or not?” Significant constitutional and statutory reforms to make use of actuarial principles implemented between 1987 through 2014 have brought Louisiana’s unfunded accrued pension liabilities under greater control and have established a sound payoff schedule. They have reduced benefits and increased employee contributions for new hires and increased employee pension options. Each of the four state retirement systems has adjusted its discount rate assumptions to be more conservative and to better reflect actual experience in the market. However, the current cost of pension and payments on the prior unfunded liabilities continues to constrict the budgets of public employers—the individual school districts, higher education institutions, and departments of state government.

There are many variables – demographic, market, and benefit design – that affect the cost of public employee pensions. Reforms are not always immediately visible. Neither is the effect of the work of public service employees always immediately visible. Whether the structures that have already been put in place in Louisiana to deal with the unfunded liability are deemed to be adequate depends on one’s political and economic beliefs about increasing state revenues, the value one places on the functions of the public sector and one’s level of confidence in future market performance and legislative behaviors.

There are additional procedural, structural, funding and benefit design options that have been suggested to make improvements in the systems. Many have already been implemented and of those that remain, each has both positive and negative considerations. The policies and reforms that are proving effective in another state may not translate to Louisiana’s constitutional and statutory requirements and non-participation in Social Security.

There is a certainly a case to be made for ongoing education and understanding and continued vigilance, review, and adjustment as necessary as the future unfolds. The guiding principles should be actuarial soundness and long-term solvency, cost effectiveness, fairness to both public employer and employee, effective recruitment and retention of competent public employees, and broad public engagement.

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**SOURCES**

**Interviews by Study Team Members**

Cagle, Stuart, Deputy Director; Katherine Whitney, Attorney; and Lisa Honore, Public Information Director; *Teachers' Retirement System of Louisiana*.

Felps, Irwin, Director, *Louisiana State Police Retirement System*.

Gauthreaux, Butch, former chair of the *Louisiana Senate Retirement Committee*.

LeBlanc, Maris, Deputy Director and Chief Operating Officer; Trey Boudreaux, Deputy Director and Chief Administrative Officer; and Chris Walters, Policy Analyst, *Louisiana State Employees' Retirement System*.

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Carolyn N. Forbes, Assistant Director, Louisiana School Employees' Retirement System (LSRS).

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**APPENDIX A**

**LOUISIANA CONSTITUTION, Article X, Section 29**

**§29. Retirement and Survivor's Benefits**

Section 29.(A) Public School Employees. The legislature shall provide for retirement of teachers and other employees of the public educational system through establishment of one or more retirement systems. Membership in such a retirement system shall be a contractual relationship between employee and employer, and the state shall guarantee benefits payable to a member or retiree or to his lawful beneficiary upon his death.

(B) Other Officials and Employees. The legislature shall enact laws providing for retirement of officials and employees of the state, its agencies, and its political subdivisions, including persons employed jointly by state and federal agencies other than those in military service, through the establishment of one or more retirement systems. Membership in any retirement system of the state or of a political subdivision thereof shall be a contractual relationship between employee and employer, and the state shall guarantee benefits payable to a member of a state retirement system or retiree or to his lawful beneficiary upon his death.

(C) Retirement Systems; Change; Notice. No proposal to effect any change in existing laws or constitutional provisions relating to any retirement system for public employees shall be introduced in the legislature unless notice of intention to introduce the proposal has been published, without cost to the state, in the official state journal on two separate days. The last day of publication shall be at least sixty days before introduction of the bill. The notice shall state the substance of the contemplated law or proposal, and the bill shall contain a recital that the notice has been given.

(D) Compensation for Survivors of Law Enforcement Officers and Firemen. The legislature shall establish a system, including the expenditure of public funds, for compensating the surviving spouses and dependent children of law enforcement officers, firemen, and personnel, as defined by law, who die, or who died after June 30, 1972, as a result of injury sustained in the performance of official duties or in the protection of life or property while on or off duty.

(E) Actuarial Soundness. (1) The actuarial soundness of state and statewide retirement systems shall be attained and maintained and the legislature shall establish, by law, for each state or statewide retirement system, the particular method of actuarial valuation to be employed for purposes of this Section.

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(2) For public retirement systems whose benefits are guaranteed by this constitution as is specified in Paragraphs (A) and (B) of this Section:

(a) The legislature shall, by law, determine and set all required contributions to be made by members. However, until the unfunded accrued liability referenced in (c) below is eliminated, this determination and setting shall not cause the ratio of employee contributions to total contributions, on the basis of each particular plan or classification within each particular retirement system, to exceed such ratio as it existed on January 1, 1987. Upon elimination of the unfunded accrued liability referenced in (c) below, this determination and setting shall not cause a member's contribution to exceed an amount contributed on his behalf as an employer contribution.

(b) The legislature shall, in each fiscal year, by law, provide an amount necessary to fund the employer portion of the normal cost, which shall be determined in accordance with the method of valuation established under (1) above.

(c) The legislature shall, in each fiscal year, by law, provide for the amortization of the unfunded accrued liability existing as of June 30, 1988, which shall be determined in accordance with the method of valuation selected in (1) above, by the year 2029, commencing with Fiscal Year 1989-1990.

(d) Amounts provided for under (b) and (c) above are hereby guaranteed payable, each fiscal year, to each retirement system covered herein. If, for any fiscal year, the legislature fails to provide these guaranteed payments, upon warrant of the governing authority of the retirement system, following the close of said fiscal year, the state treasurer shall pay the amount guaranteed directly from the state general fund.

(3) For statewide public retirement systems not covered by Paragraphs (A) and (B) of this Section, the legislature shall determine all required contributions to be made by members, contributions to be made by employers, and dedicated taxes required for the sound actuarial maintenance of the systems, including the elimination of the unfunded accrued liability as of the end of the 1988-1989 Fiscal Year, under the method of valuation selected under (1) above, by the year 2029, commencing with Fiscal Year 1989-1990.

(4) For all state and statewide public retirement systems, neither the state nor the governing authority of such system shall take any action that shall cause the actuarial present value of expected future expenditures of the retirement system to exceed or further exceed the sum of the current actuarial value of assets and the actuarial present value of expected future receipts of the retirement system, except with respect to the following:

(a) Normal business operating expenses of the retirement system.

(b) Capital outlay expenditures of the retirement system.

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(c) Management of investments of the retirement system.

(d) Cost-of-living increases to retirees, as provided by law, provided the retirement system is approaching actuarial soundness as provided by law, and the granting of such increase does not cause an increase in the actuarially required contribution rate.

(5) All assets, proceeds, or income of the state and statewide public retirement systems, and all contributions and payments made to the system to provide for retirement and related benefits shall be held, invested as authorized by law, or disbursed as in trust for the exclusive purpose of providing such benefits, refunds, and administrative expenses under the management of the boards of trustees and shall not be encumbered for or diverted to any other purpose. The accrued benefits of members of any state or statewide public retirement system shall not be diminished or impaired.

(F) Benefit Provisions; Legislative Enactment. Benefit provisions for members of any public retirement system, plan, or fund that is subject to legislative authority shall be altered only by legislative enactment. No such benefit provisions having an actuarial cost shall be enacted unless approved by two-thirds of the elected members of each house of the legislature. Furthermore, no such benefit provision for any member of a state retirement system having an actuarial cost shall be approved by the legislature unless a funding source providing new or additional funds sufficient to pay all such actuarial cost within ten years of the effective date of the benefit provision is identified in such enactment. This Paragraph shall be implemented as provided by law.

(G) Forfeiture of Retirement Benefits; Felony Convictions. The receipt of a public retirement benefit shall be expressly conditioned upon the rendition of honorable service by the public official or employee. Notwithstanding any provision of this constitution or of any home rule charter to the contrary, the legislature may provide for the forfeiture of all or part of the benefits from a public retirement system, plan, or fund in this state by any person who holds or held any public office or employment and who is convicted of a felony associated with and committed during his service in such public office or employment. The legislature may provide for the application of all or part of any forfeited benefits to the unfunded accrued liability of the system, plan, or fund. The provisions of this Paragraph shall be applied only to persons employed, re-employed, or elected on or after January 1, 2013. The provisions of this Paragraph shall be applied only to benefits earned on or after January 1, 2013.

*Amended by Acts 1987, No. 947, §1, approved Nov. 21, 1987, effective December 24, 1987; Acts 2007, No. 484, §1, approved October 20, 2007, effective November 19, 2007; Acts 2010, No. 1048, §1, approved November 2, 2010, effective December 1, 2010; Acts 2012,*

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*No. 872, §2, approved November 6, 2012, effective December 10, 2012; Acts 2012, No. 868, §2, approved November 6, 2012, effective December 10, 2012.*

**§29.1. Part-time Public Officials**

Section 29.1.(A) Except as provided in Paragraph (B), the following elected or appointed officials are hereby deemed to be part-time public servants who, based on such part-time service, shall not participate in, or receive credit for service in, any public retirement system, fund, or plan sponsored by the state of Louisiana or any instrumentality or political subdivision thereof:

- (1) Any legislator or any member of a school board, levee board, police jury, or parish council.
- (2) Any member of a city council, city-parish council, or town council or any alderman or any constable.
- (3) Any member of a board or commission established by the state of Louisiana or any instrumentality or political subdivision thereof unless authorized by law enacted by two-thirds of the elected members of each house.
- (4) Any person holding or serving in any other elected or appointed position or office defined to be part-time public service by law enacted by two-thirds of the elected members of each house.

(B) The provisions of Paragraph (A) shall not apply to any person who is serving on January 1, 1997, in any elected or appointed position set forth in Paragraph (A) and who is also a member on January 1, 1997 of a retirement system covering that position.

(C) The provisions of this Section shall not apply to participation in the Louisiana Public Employees Deferred Compensation Plan, or its successor.

(D) This Section shall become effective on January 1, 1997.

*Added by Acts 1996, 1st Ex. Sess., No. 99, §1, approved Nov. 5, 1996, eff. Jan. 1, 1997.*

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**APPENDIX B**

**Description of Membership within the Four State Pension Systems**

The membership demographics (e.g. gender, longevity) among the systems - and within the sub-plans - vary widely because different public services require employees with different levels of education, different kinds of certification, and different experience and skills.

Benefit structures are designed to match the needs of the different kinds of employees who may have very different overall life expectancies. On-the-job risks plus long-term career paths and career opportunities also differ among job categories and affect the average length of retirements. All these differences have major implications for each system and sub-plan's pension costs.

Following is a general outline of the membership in the plans of these four systems:

**LASERS** - Includes full and part time employees (employees with 20 hours/week or with fewer who have 10 or more years of service)

**Number of sub-plans - 19**

All state employees unless exempted by law. For example,

- Non-management workers, professionals in various state agencies
- Skilled trade workers
- Judges/Court Officers/Clerks
- Hazardous duty personnel, e.g. corrections, peace officers, arson investigators, alcohol and tobacco control, bridge police, etc.
- Elected state officials
- Legislators, enrolled prior to 1997.

**TRSL** - Includes only full time employees (offers some provisions for part-time workers  
·Number of sub-plans - 4

- Pre-K-12 - regular teachers, other professionals and school food service workers in parish and city school systems (excluding bus drivers, janitors and maintenance personnel)
- Unclassified personnel in public colleges, universities, community and technical colleges (Hired after 7/1/91)

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- Pre-K-12 teachers and other professionals in charter schools electing to join TRSL
- Unclassified employees of boards governing elementary, secondary and higher education employed on or after 7/1/91 if not already members of LASERS: (e.g. Board of Elementary and Secondary Education, Board of Regents, Board of Supervisors for LSU, Board of Trustees for the University of Louisiana System, Board of Supervisors for Southern University.)

**LSERS** -- Non-instructional personnel of the Louisiana public school system who work more than 20 hours/week.

**Number of sub-plans - 2**

- School bus drivers (most of the drivers of parish-owned buses and contracted buses work about 21 hours/week, which is considered full-time for these members)
- Janitors, custodians, maintenance employees (almost all work 40 hours/week)
- School bus aides, monitors and attendants and other regular school employees who actually work on school buses helping with the transportation of school children

**LSPRS** – Limited to sworn, commissioned law enforcement officers

**Number of sub-plans: 2**

- \* Sworn, commissioned law enforcement officers of the Office of State Police of the Department of Public Safety and Corrections who have satisfactorily completed the State Police Training Academy Course of Instruction, are licensed law enforcement officials for the state, and wear a badge of the State Police. Serve in the areas of gaming enforcement; criminal intelligence investigations; special investigations; counterterrorism; highway patrol; emergency services; internal affairs investigations within the Department of Public Safety; transportation safety; weights and standards; protection of the governor and governor's immediate family, and the lieutenant governor, and other dignitaries. Various education and training needs required.
- \* The Secretary and Deputy Secretary of the Department of Public Safety, if they are sworn, commissioned state police officers who have graduated from the State Police Academy.
- \* There are no part-time employees. No overtime pay is calculated into final retirement benefit.

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**APPENDIX C**

**State Level Entities With Roles in Overseeing and Affecting Public Pensions**

Statewide Officials	Legislature, Senate and House of Representatives			Courts	Retirement Systems' Boards of Trustees
Governor	Senate Retirement Committee	House Retirement Committee	Joint Legislative Committee	Supreme Court	LASERS
State Treasurer			PRSAC	District Courts	TRSL
Secretary of State			LAAC		LSERS
Commissioner of Administration			Budget Committee		LSPRS
Superintendent of Education	Legislative Auditor				Members - Employees and Retirees - Elect Systems' Trustees
Superintendent, Office of State Police					
The Public					

**The Governor**

The Governor selects the Speaker of the House and the President of Senate who, in turn, appoint and remove, at the governor's suggestion, the chairs and members of the House and Senate Retirement Committees. The Governor also appoints the **Commissioner of Administration**, who sits *ex-officio*, along with the two Retirement Committee chairs or their designees, on the Board of Trustees of each pension system.

The Board of Elementary and Secondary Education (BESE) Board appoints the **Superintendent of Education**. The Governor does not officially recommend candidates

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but may make unofficial suggestions. The Superintendent then sits *ex-officio* on the TRSL Board of Trustees. The Governor appoints the **Superintendent of the Office of State Police** who is a voting member of the LSPRS Board.

As with all legislation, the Governor has the power of veto over retirement bills passed by the Legislature.

### **The State Treasurer**

The State Treasurer is a voting member of PRSAC (see below,) and an *ex-officio* member of the TRSL, LASERS, LSERS and LSPRS Boards of Trustees.

### **The Secretary of State**

The Secretary of State is an *ex-officio* member of LSER's Board of Trustees.

### **The Legislature**

The overall role of the Legislature is to consider and pass bills that become the laws or constitutional amendments pertaining to all aspects of the pensions systems:

- the funding methods and assumptions utilized by the state and statewide public retirement systems to determine actuarially required contributions each year
- the amortization schedule of each system's UAL and revisions of the original schedule
- the design of all pension benefits (eligibility, formulas, etc.) both for each system and for specific employee groups within each system.

These three things together, along with the actuarial factors of size, demographics, salary levels and employment longevity of the workforce, create the total cost and liabilities of the pension systems.

### **Legislative Committees**

The Senate and the House each have retirement committees where all bills pertaining to pensions are first heard. The chairs of the House and Senate Retirement Committees often

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steer bills they feel appropriate through passage or encourage rejection based on their larger and more focused understanding of pension issues.

In addition, the Legislature has two joint committees with roles in public pensions. These are the Public Retirement Systems' Actuarial Committee (PRSAC) and the Legislative Audit Advisory Council (LAAC.)

### **LAAC and the Legislative Auditor**

The Speaker of the House and the Senate President each appoint half of the members of the 10 members (5 senators and 5 representatives) of the Legislative Audit Advisory Committee.

The LAAC provides oversight to the **Legislative Auditor** who is elected by a majority vote of the two houses of the Legislature. The Legislative Auditor is the only constitutional state officer not elected directly by the general public. LAAC also recommends the budget for the Office of the Legislative Auditor.

In general, the Legislative Auditor fosters accountability and transparency in Louisiana government by providing the Legislature and others with audit services, fiscal advice, and other useful information. He specifically advises the Legislature on retirement matters, as one of his roles, including issuing a public annual actuarial report on each of the retirement systems and an annual general report to the Legislature. He also provides analyses of pending bills that affect state finances, including employee pensions.

The Office of the Legislative Auditor is intended to be as non-political and objective as possible. Thus, he or she may only be removed by a  $\frac{2}{3}$  vote of each house of the Legislature.

### **PRSAC**

The Public Retirement Systems Actuarial Committee, PRSAC, was created in 1988. The Legislature's stated intent was "... to insure orderly and consistent strategies for continuing development and growth that will attain and maintain the soundness of the systems, plans, and funds.... " [R.S. 11:121(B)]

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PRSAC serves as a key advisor in matters of the state pension systems. The fact that a quorum in PRSAC is six of the seven members underlines its importance. Those members are the State Treasurer, the Commissioner of Administration, the Legislative Auditor, the President of the Senate or his/her designee, the Speaker of the House or his/her designee, an actuary representing the four retirement systems, and an actuary representing the nine statewide systems.

PRSAC is one of almost two dozen such state pension commissions across the United States. Its duties are to

“...review and study, on a continuing basis, actuarial assumptions, funding methods, the unfunded liability determined by those methods, the amortization methods to reduce such unfunded liability, and such other matters as the committee deems appropriate. It shall make recommendations, subject to the unanimous approval of the committee, to the retirement systems, plans, and funds and to the House and Senate committees on retirement and the Joint Legislative Committee on the budget.” [R.S. 11:127(A)]

Each year PRSAC approves and submits to the Senate and House retirement committees a single valuation for each retirement system that includes the employer contribution rate (now known formally as the Actuarially Determined Contribution or ADC) and the actuarial assumed rate of return (the discount rate.) This, in turn, will determine the actual pension cost to each employer within the government. It is based on PRSAC’s review of all the above factors and assumptions as provided by the systems’ actuaries and the Legislative Auditor’s actuaries.

### **Joint Legislative Budget Committee**

This committee reviews and approves the annual operating budgets of all the state retirement systems.

### **Pension Systems’ Boards of Trustees**

The Boards of Trustees of TRSL, LASERS, LSERS and LSPRS have responsibility for safeguarding and managing the assets held in trust to provide retirement income for system members. They must report quarterly their investment performance to the legislature and to the Legislative Auditor. They adopt policies and procedures for pension administration,

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including investments. The boards are composed of elected representatives of both active and retired members and, in some cases, officials or their representatives of advocacy organizations or public officials or their representatives. (See Appendix D.)

The Boards may take positions supporting or opposing proposed legislation but do not lobby legislators. In some cases professional staff of the systems are called upon by a legislative sponsor to assist in developing a bill.

Retirement bills currently under consideration are accessible on the pension systems' websites and are generally easy to understand. If a Board of Trustees has taken a position on a bill, that position is indicated on the website as well.

**Advocacy Groups**

Employee and retiree advocacy organizations exist at the state, member district, and parish levels for members who choose to join. The advocacy groups serve as *de facto* watchdogs and liaisons with employees and retirees. These organizations keep their members informed of proposed changes, lobby the Legislature on upcoming bills, distribute newsletters to members and hold statewide meetings of organization delegates. They also may bring lawsuits to challenge retirement laws when they deem necessary. The main groups are:

Retirement System Members	Member Advocacy Organization
Teachers	LA Retired Teachers Association LA Association of Educators LA Federation of Teachers (the last two for active members)
State Employees	Retired State Employees Association
School Employees	LA School Bus Operators Association
State Police	LA State Troopers Association Central State Troopers Coalition

## **Oversight in Other States**

Simply for comparative purposes, we describe how two other states have organized public pension policy oversight.

**Minnesota** The Minnesota Legislative Commission on Pensions and Retirement was established as an on-going joint legislative commission in 1967. This Commission's pension policy guidelines are on its website and are fairly short. The Commission's policy guidelines preamble states that the Commission :

“...recommends the following statements of principles which have been developed since 1955, as the basis for evaluating proposed public pension legislation. Problems can be avoided or minimized if a sound set of principles is used as a guideline in developing the various public pension funds and plans.”

Louisiana does not have any comparable, succinct statement of principles against which to measure pension proposals as they arise.

The Minnesota Commission reviews most proposed retirement pension bills prior to any other committee hearing and recommends forwarding about half of those bills, frequently after amending them. It generally meets weekly during the legislative session and develops policy memos on bills based “significantly” on the Commission's Principles of Pension Policy and including technical or content problems in the bill. The Commission studies particular pension topics in greater depth during the session interims.

**Wisconsin** Wisconsin's Joint Survey Committee on Retirement Systems, begun in 1947, has a diverse membership similar to PRSAC. Before a vote on any retirement bill or any amendment “...which would create, modify, or in any way provide for the retirement or payment of pension to public employees....” the Committee must provide a written report to the legislature. The report is to include a description of the effect of the bill, the probable dollar cost and the percentage of the affected employer's total annual payroll, the likely effect on the actuarial soundness of the pension system, and “whether the bill is desirable as a matter of public policy.” [State of Wisconsin Department of Employee Trust Funds].

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The Committee may not introduce retirement legislation or amendments, but may indicate good public policy amendments to a proposed bill. Every two years the Committee staff compares the system other major state retirement systems and contracts for actuarial studies as needed.

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**APPENDIX D**

**COMPOSITION OF THE BOARDS OF TRUSTEES OF LOUISIANA’S STATE PENSIONS SYSTEMS**

<b>TRSL</b>	<b>LASERS</b>	<b>LSERS</b>	<b>LSPRS (4)</b>
1 rep. for active members in higher ed. 1 rep. each of Districts 1-7 2 reps. For all retired members 1 rep. for School food Service Employees 1 rep. for active Superintendents (city or parish)	6 reps for active members 3 reps for retired members	Reps. For Districts 1-4, four elected at large by active members and two by retired members from Div. 1 & 2.	-1 rep. for active/retired members -2 reps. for active members -1 rep. for retired members -President of the La. State Troopers Assn. -1 rep for surviving spouses -the Superintendent, Office of State Police -1 rep. of Central State Troopers Coalition,
<b>Ex-Officio:</b> State Treasurer State Superintendent of Education Commissioner of Administration Chair of Senate and Chair of House Committee on Retirement	<b>Ex-Officio:</b> State Treasurer Commissioner of Administration Chair of Senate and Chair of House Committee on Retirement	<b>Ex-officio:</b> President of the Louisiana School Bus Operators' Association (LSBOA) Commissioner of Administration Chair of Senate and Chair of House Committee on Retirement Secretary of State State Treasurer	<b>Ex-Officio:</b> State Treasurer Commissioner of Administration Chair of Senate and Chair of House Committee on Retirement
<b>Term of Office</b>	<b>Term of Office</b>	<b>Term of Office</b>	<b>Term of Office</b>
Staggered 4 years	Staggered 4 years	Staggered 4 years	Staggered 5 years

## APPENDIX E

### Calculation of the Retirement Benefit in a Defined Benefit Plan

A retiree's pension benefit in a defined benefit plan is calculated at the time of retirement based on a formula. Several factors go into the formula.

- Number of years of service
- Age at retirement
- Sometimes a specified combination of age and years of service
- Final salary
- Average salary over some specified number of recent years, typically 3 to 5
- A "multiplier" factor

A retiree's pension benefit, which will be received for the rest of the retiree's life (unless a subsequent Cost of Living Adjustment is passed,) is determined by multiplying the employee's final average salary by the multiplier factor and by the employee's total years of service.

Any of the variables in the formula can be adjusted by the employer, i.e. the required number of years of service to be eligible for full or partial retirement benefits, minimum retirement age for full or partial benefits, the multiplier factor, and the number of final years' salaries to be averaged for the formula.

To use an example, an employee whose annual salary averaged \$50,000 during the last three years of service after a 30-year career, at a multiplier of 2% would receive an annual retirement benefit of \$30,000.

$$\$50,000 \times 30 \times .02 = \$30,000.$$

Annual benefits may be capped by the employer either at specified dollar levels or at specified percentages of final salary.

## APPENDIX F

### Relevant Positions Supported by the League of Women Voters

**The League of Women Voters of Louisiana** has already studied and supports the following positions that are relevant to the governance and funding of public pensions:

#### **The Constitution**

Should be fundamental law, free of statutory material  
Should be written in clear and simple language

#### **Ethics**

Ensure the existence of and allocation of resources necessary for strong, effective, independent watchdog agencies, such as the Louisiana Ethics Administration, the Louisiana Legislative Auditor, and the Office of State Inspector General.  
Require a transparent, competitive, and clearly defined state contract selection process.

#### **State Finances**

A diversified revenue system that is equitable, progressive, stable, responsive and simple  
Achievement of policy goals through direct expenditures rather than deductions, exemptions and credits  
Local services mandated by the State should be accompanied by state appropriations

**The League of Women Voters of the United States** has already studied and supports this position that is relevant to the design of public pensions:

#### **Meeting Basic Human Needs**

- Support programs and policies to prevent or reduce poverty and to promote self-sufficiency for individuals and families.

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**LWVLA Board, 2013-2015**

Sandra Slifer, President

Molly Morgan, Vice-President

Thetis Cusimano, Secretary

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***The League of Women Voters of Louisiana*** is a non-partisan organization of women and men that encourages informed and active participation in government, works to increase understanding of major public policy issues, and influences public policy through education and advocacy. There are local Leagues or units in Caddo-Bossier, Lafayette, Lake Charles, Natchitoches, New Orleans, and St. Tammany. For more information, visit [www.lwvofla.org](http://www.lwvofla.org).

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