SCPP Risk Assessment

Issue

The Executive Committee of the SCPP identified managing the future health of the retirement systems as a strategic priority for the 2009 and 2010 interims. The Executive Committee further recommended the SCPP undertake an assessment of the health risks facing the state's retirement systems and develop recommendations to the 2011 Legislature for managing those risks. Included in the assessment is building an actuarial risk model to measure and analyze health risks facing the retirement systems.

Background

This issue is the result of a convergence of a strategic planning effort and an actuarial assessment of retirement systems health. In June 2009, the Executive Committee created a strategic planning "subgroup" to further define and clarify a proposal related to strategic planning. At the same time, the Office of The State Actuary (OSA) prepared a report on the financial condition of the retirement systems as part of the statutory process for recommending economic assumptions. In the report, the state actuary noted the declining health of the retirement systems and recommended a risk assessment to several bodies–including the subgroup.

The strategic planning subgroup met during the summer and considered many challenges and risks facing the retirement systems. Ultimately, the subgroup selected managing the future health of the retirement systems as its top strategic priority. The subgroup recommended the SCPP take up the state actuary's proposed risk assessment and create an advisory group to provide input to the state actuary. .

The key goals for the Risk Assessment include:

- Educating stakeholders and improving understanding of the health risks faced by the retirement systems.
- Developing new tools to measure heath risks, manage health risks, and evaluate future changes to the retirement systems.
- Identifying root sources of health risks and options for managing the future health of the retirement systems.
- Informing future budget discussions.

The Risk Assessment is expected to span two interims. During the 2009 Interim, OSA staff worked with the advisory group to identify health risks and set health measures for the retirement systems. During the 2010 Session, staff will build the actuarial risk model. During the 2010 Interim, staff will measure and analyze risks, and work with the SCPP to develop

options for managing health risks and a decision aid for evaluating the options. It is expected the SCPP will share recommendations and findings from the risk assessment with the 2011 Legislature.

Committee Activity

OSA reported on the financial condition of the retirement systems at the September SCPP meeting. Also in September, the strategic planning subgroup reported on its strategic planning proposal to the Executive Committee. The Executive Committee adopted the subgroup's proposal and created the Risk Assessment Advisory Group for the 2009 Interim.

Staff briefed the full SCPP on "Managing the Future Health of The Retirement Systems" during October and November. In December, staff provided an update on the status of the Risk Assessment.

The Risk Assessment Advisory Group met once during November and once during December.

Next Steps

OSA staff will build the acturial risk model during the 2010 Session. Staff will report results of the preliminary health risk measurement and analysis to the SCPP during the 2010 Interim.

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Advisory Group Input on Risk and Health Measures

Introduction

The Risk Assessment Advisory Group of the SCPP met on November 16th and held a discussion on risk and health measures. As part of this discussion, the group conducted a structured brainstorming exercise where each member responded to the following three questions posed by staff:

1. What does a healthy pension system look like?
2. What things might prevent achieving the healthy pension system envisioned above?
3. What specific outcomes do you want to avoid?

The purpose of the exercise was to gather input from the group that will help staff identify risk and health measures for the SCPP risk assessment project. The questions were designed to gather information on risk and health factors from different perspectives. During the exercise, members took turns responding to the questions until they had given all their responses. Responses were not discussed or critiqued during the exercise.

The responses provided by members are documented below. Due to the nature of the exercise, there is some duplication and overlap in the responses.

Question #1

What does a healthy pension system look like?

1. Pension system guaranteed
2. Honesty and integrity in actuarial assumptions and funding
3. Provide stability in retirement
4. A fulfillment of a promise for the particular pension system
5. Would be funded
6. Fully funded (in prudent political terms)
7. Stable and predictable

8. Attract and retain key skills for employers
9. Contribution rate stability
10. Would align with clear policy goals
11. Allows for growth and challenges of inflation and distressed economy
12. Rewards long term service
13. Simple in structure
14. Competitive with other states
15. Funding system stable and reasonable
16. Flexible and portable
17. Sustainable
18. Provides for adequate living expenses
19. Clear and credible in its decision-making
20. Relevant to a new generation of young workers
21. Provides a recruitment tool
22. Promised benefits need to be protected by the State
23. Would enhance personal retirement plans
24. Provides an excellent return on investment
25. Flexible, adapting to broad changes in economic climate
26. Aligns system's investment strategy with the payout strategy
27. Neither political nor partisan
28. Can be tailored to individuals
29. Targeted to address differences in different career paths
30. Affordable – for both employees and employers
31. Incents overall life cycle employment costs

32. Does not entertain retroactive benefit improvements
33. Responsive to changes in investment environment and to constituent concerns regarding fairness
34. Well managed
35. Provides an equitable approach to distribute deficits and surpluses
36. Considered a well-run business by taxpayers and voters
37. Good years to cover for the bad years
38. Always looking long term
39. Would not implement benefit improvements via leapfrogging
40. Understandable by non-expert legislators
41. Legislators recognize the importance of a healthy pension system and the importance of funding it
42. Under-promises and over-delivers
43. Provides a guaranteed benefit in retirement
44. Conforms to actuarial best practices
45. Addresses the age 53-65 gap and the problem of retirement after age 65
46. Cannot provide for everything in retirement, only a part
47. Fairly distributes costs
48. Cross-connects with other strategic concerns of taxpayers (health care, child care, etc.)
49. Clearly defines its benefits and its contributions
50. Recognizes this is a tool to address the broader aging population
51. Transparent to public
52. Funded as a State obligation – similar to a debt paid outside of operating budgets
53. Its benefits are financed during working lifetime of participants and thereby its funding should therefore be protected for the beneficiaries

54. Robust enough to weather short-term budget priorities

55. Bounded by parameters, keep it safe from short-term budget priorities

56. Model to other systems

57. Maybe should have constitutional protection for the pension systems

Question #2

What things might prevent achieving the healthy pension system envisioned above?

1. Economic recession

2. Enhancing benefits beyond the capability of fully funding those enhancements before retirement

3. Current authorizing environment for benefit improvements

4. Lack of funding

5. Another crash or depression

6. Lack of honesty and integrity in funding and analysis of pensions

7. Investment volatility

8. Public opinion – pension envy

9. Mismanagement of investments

10. Failing to solve (address) the current funding problems

11. Lack of political will – risk avoidance

12. Lack of economic growth

13. Inflation

14. Not adhering to sound actuarial recommendations

15. Expedient budget decisions that burn bridges to long term recovery

16. Lowered priorities for expectations of pensions

17. Pulling more funds into the general fund budget

18. Rising health care costs
19. Playing politics with the pension system
20. Legislative overreaction: PERS 401(K)
21. Losing credibility with beneficiaries and the public
22. People living longer than funding assumptions
23. Implementing benefit improvements through leapfrogging
24. Over-promising and under-funding
25. Funding retroactive benefit improvements
26. Failure of coherent legislative governance/failure of SCPP process
27. Lack of collaboration between policy-makers and stakeholders
28. Lack of a clear policy direction for the pension system
29. Failure to build sufficient reserves during the good times
30. Individual constituencies pulling for their own self-interest
31. Ignoring the experts
32. Lack of positive labor relations
33. Lack of legislative understanding of the funding of pensions
34. Governor's budget priorities becoming disconnected from actuarial reality
35. Untimely responses to changing environments
36. Failure to protect a high quality Office of the State Actuary
37. Small gains taken at the expense of huge pension bow waves
38. Complexity of the current pension system
39. Perception that pensions are the end-all for everything in retirement
40. Volatility of State revenue
41. Ineffective or intermittent communication about the pension system

42. Failure to complete this new risk assessment process
43. Including pension funding in the general fund budget
44. Not understanding when a retirement system or plan needs to be closed

Question #3

What specific outcomes do you want to avoid?

1. Not being able to deliver the promise to the beneficiaries
2. End this process without overall policies for the pension system
3. Being forced to close Plans 2
4. Moving away from a defined benefit
5. Passing the problems on to future State leaders
6. Underfunding
7. Plan closure for fiscal expedience
8. Running out of money
9. Precipitous increase in plan contributions
10. Further complicating the pension system
11. Pension payments by employers that are unaffordable
12. Further fracturing the pension system
13. Loss of defined benefits
14. Further politicizing the pension system
15. Excessive rate volatility
16. Adding benefits that cannot be funded
17. Sense of entitlement
18. Underfunding – puts all pension systems at risk

19. Damaging the quality of our career workforce
20. Plans oriented only at the aging workforce
21. Overpromising
22. Breaking faith with existing retirees
23. Going to all cash system – pay as you go
24. Leapfrogging
25. Retroactive benefit improvements
26. Killing the messengers

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