Contribution Risk and Public Pension Reform

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Context: retirement plans matter for state and local governments

- State and local retirement plans:
  - Cover 19.5 million members and 8.6 million beneficiaries (2011 Annual Survey of Public Pensions), and
  - Control **$4.6 trillion in assets** (Investment Company Institute, 2013 & Isaacs, 2013).

- **93%** of these members are covered in **defined benefit plans**.

- Consume about 5% of state budgets and about 9% of local budgets (Pew Center on the States, 2013).

And they have been generating headaches for their sponsors

The sky really is falling. The people of Jacksonville need to know this. When they look at the roads that are crumbling. When they look at the neglected infrastructure. When they look at certain ZIP codes that have had little to no investment, promises that were made in years gone by that haven't been kept. It's because we don't have the cash to do it because our budget is being eaten alive by these unfunded pension liabilities.

– Mayor of Jacksonville (FL), Lenny Curry

What the paper examines

- Several states have engaged in reforms to their defined benefit public pension plans
  - Increased employee contributions
  - Reduced benefits
  - Started Defined Contributions (DC)/ hybrid plans
- Research Question: What factors induce state governments to enact these reforms?
- Hypothesis offered: A higher degree of variability in the contributions states make to their pension plans makes them more likely to enact reforms
- Data used: 114 plans from the Public Plans Database for the period 2001 - 2013

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Summary of findings

- Variability of contributions made by states is positively and statistically significantly correlated with
  - increases in employee contributions and
  - enactment of any reform
- Coefficient is positive when examining the reduction in employee benefits but statistically insignificant
- Coefficients turn out to be larger in magnitude than the coefficient on unfunded liabilities in five of the six specifications

Comment - Alternative ways of capturing variability of contributions

- The variability of contributions should be measured w.r.t. the fiscal capacity of the state
- Possible ways of addressing this: examining how variable the contributions are relative to the revenue base/ tax base
- Also the effects are likely to vary based on whether states are losing people or adding people

Comment - Politics matters; play closer attention to it

- Currently, the effect of politics is being captured through the variable, “whether or not a government is Republican controlled”
- Do more: look for more possibilities: e.g. Republican-controlled House; Democratic-controlled Senate; and Republican governor (essentially $2^3 = 8$ possibilities $\longleftrightarrow$ 7 dummy variables)
- Political competition matters for funding and generosity of pension benefits (Bagchi, 2016) so consider ways of incorporating
- Unions may matter as well so consider variations in strength of public-sector unions

Minor comments

- A change in employee contributions is a change in employee contributions but the magnitude of change matters
- A bit of additional description about the sample - what kinds of plans are getting included (e.g. plans for legislators/ judges?)
- Consider changes in bond ratings - they may provide a proximate cause for reform as well (example of Illinois)