Why PERA Being Only 71% Funded Is Not Enough

As of 2018, the New Mexico Public Employees Retirement Association (PERA), the largest public pension system in New Mexico, reported to have about \$0.71 cents for every dollar it needs to fully fund pension benefits promised to municipal and county employees.



Is not being fully funded a real problem for PERA? While the governor and the PERA Pension Solvency Tack Force believe it's a serious problem to tackle, some argue that the state has enough money to pay today's retirees and several decades to catch up on payments. However, this view fails to account for the added costs and risks associated with holding an unfunded liability and a funded ratio less than 100 percent.

1. Financing PERA pension debt is expensive.

- PERA has at least \$6.1 billion in pension debt and potentially more if its current actuarial assumptions are too aggressive, which is likely.
- The system has annually underperformed its assumed investment return 11 times since 2001 on an actuarial basis, adding to the growth of unfunded liabilities.
- Billions in required annual pension debt payments over time could instead be used to support other public priorities, pay public employees more or reduce the tax burden.
- Over \$1.9 billion in PERA pension debt payments have been made since 2003.

2. Maintaining a funded ratio of less than 100% jeopardizes intergenerational equity.

- Any pension plan less than 100 percent funded holds pension debt that requires "unfunded liability amortization payments."
- Because of compounding effects, missing the assumed rate of return in any year will require supplemental contributions over several years.
- Carrying pension debt means future taxpayers must eventually pay for today's public sector retirement benefits.

3. The actuarial community agrees, 70% percent funded is *not* healthy.

- * The idea that a pension system less than 100 percent funded is healthy is a myth.
- On the reverse side are quotes from the actuarial community on why pension plans with less than 100 cents on the dollar to pay promised benefits need to improve their long-term solvency.

Conclusion: Pension plans must be 100 percent funded to prevent expensive, intergenerational inequality. Anything less won't do for New Mexico public employees or taxpayers.

Pension Integrity Project Contacts —

- Leonard Gilroy, Vice President (<u>leonard.gilroy@reason.org</u>)
- Steven Gassenberger, Policy Analyst (<u>steven.gassenberger@reason.org</u>)

The Pension Plan Actuarial Community on Fully Funding Benefits



"[A pension] plan's funding goal should always be 100 percent of the plan liability calculated assuming median expected future investment returns."

-Society of Actuaries

- The Society of Actuaries (SOA) is the world's largest actuarial professional organization.
- SOA's Blue Ribbon Panel on Public Pension Funding advises that a plan should not settle for any level of funding below 100 percent, and should always guide their fund to reach full funding within a reasonable timeframe and under a median level of possible longterm returns.
- Read for yourself: <u>https://www.soa.org/blueribbonpanel/</u>

"A plan with a funded ratio above 80 percent (or any specific level) might not be sustainable if the obligation is excessive relative to the financial resources of the sponsor, if the plan investments involve excessive risk, or if the sponsor fails to make the planned contributions."

-American Academy of Actuaries

- The American Academy of Actuaries advises that an 80 percent funded ratio is not a reliable indicator of pension fund health, especially if the fund is allocating its investments in more risky assets and not making the full actuarially required payments.
- Read for yourself: <u>https://www.actuary.org/files/80 Percent Funding IB 071912.pdf</u>

"Underfunded pension plans ... generally violate the principle of intergenerational equity."

-Pension Finance Institute

- The Pension Finance Institute warned that anything below full funding represents intergenerational theft, meaning current employees and employers aren't putting enough into the system to pay the amount promised, which will result in future generations having to pay for benefits they will not receive.
- Even if PERA is on a path to full funding within 30 years, future generations bear the financial risk if all market expectations are not met. To protect their future, New Mexico policymakers ought to do anything in their power to expedite the path to full funding.
- Read for yourself: <u>http://www.pensionfinance.org/papers/PubPrin.pdf</u>