UIC Center for Urban Economic Development
UNIVERSITY OF ILLINOIS AT CHICAGO
COLLEGE OF URBAN PLANNING & PUBLIC AFFAIRS

The Keystone Research Center
412 North Third Street
Harrisburg PA 17101
www.keystoneresearch.org

An Unbalanced Pension Proposal

"Universities" Proposal Would Erode Retirement Security, Weaken Schools' Ability to Retain Talented Teachers, and Create New Threat to Financial Sustainability of Illinois Pension Funds

By Stephen Herzenberg and Howard Wial[1] | August 14, 2013

Executive Summary

The "Universities" proposal to alter public employee pension systems in Illinois would significantly undermine the retirement security of teachers and state workers.[2] An estimated 80 cents on the dollar of pension system savings from the plan would be borne by retirees through a reduction in cost-of-living increases over the course of retirement. These benefit cuts would make it more difficult for Illinois public schools and the state to recruit and retain qualified college-educated employees. Additionally, the plan would create a new threat to the financial sustainability of the state's existing public pension systems, in part by diverting a third of funds contributed by new employees away from defined benefit pension pools to individual retirement accounts. The plan could result in a drop in investment returns on the state's pension assets with state taxpayers left to make up the difference.

The Universities pension proposal, first advanced in March by Jeffrey Brown of the University of Illinois at Urbana-Champaign and four co-authors, has received increasing attention in recent months.[3] While

---

[1] Stephen Herzenberg is executive director of the Keystone Research Center (www.keystoneresearch.org), a Pennsylvania-based research and policy institute, and holds a Ph.D. in economics from the Massachusetts Institute of Technology (MIT). He has written on state retirement security issues in Pennsylvania and Florida. Howard Wial is executive director of the Center for Urban Economic Development at the University of Illinois at Chicago (www.urbaneconomy.org), where he is also an associate research professor. He is a nonresident senior fellow of the Brookings Institution's Metropolitan Policy Program. From 2000 through 2002, he was an economist at the U.S. General Accounting Office, where he specialized in retirement income security issues. He holds a Ph.D. in economics from MIT and a law degree from Yale University.

[2] The plan is known as the Universities proposal because the presidents and chancellors of Illinois' 14 public universities have endorsed it. See "University presidents endorse pension plan," April 10, 2013, available online at http://capitolfax.com/2013/04/10/university-presidents-endorse-pension-plan/.

[3] See Jeffrey Brown, Steven Cunningham (Northern Illinois University), Avijit Ghosh (University of Illinois at Urbana-Champaign), David Merriman (University of Illinois at Chicago), and Scott Weisbenner (University of Illinois at Urbana-Champaign), *Six Simple Steps: Reforming the State Universities Retirement System*, online at http://igpa.uillinois.edu/system/files/Six-Simple-Steps-for-Reforming-SURS.pdf. Brown, an economist, served in 2001 on President George W. Bush's Commission to Strengthen Social Security and periodically traveled with President Bush in 2005 in his campaign to promote changes to Social Security. Cunningham is an educator and university administrator. Ghosh is also a university administrator; his research interests include marketing and retail strategy and locational analysis. Economist David Merriman specializes in state and local public finance. Economist Scott Weisbenner has published academic articles on defined contribution pension plans, is a former editor of the *Journal of Pension Economics*, and has been a consultant to the Social Security Administration.

the details of the Universities proposal address the State Universities Retirement System (SURS), the authors note that "our suggestions are relevant for the other [public employee] pension systems as well." Thus, the rest of this brief considers the impact of the Universities proposal on all of the main Illinois public pension plans, focusing not only on SURS, but also on the State Employees' Retirement System and the Teachers' Retirement System.[4]

This briefing paper uses the following criteria to examine the Universities proposal as a framework for changing Illinois' three largest pension plans:

- equity in the sharing of sacrifice among pension system stakeholders;
- the impact on retirement security of Illinois pension plan members;
- the ability of employers who participate in Illinois pension plans to attract and retain high-quality employees; and
- the impact on taxpayers.

We find that the Universities proposal makes some important contributions to the state pension debate. For instance, the proposal endorses a system in which the state makes fixed payments into the pension system (similar to a mortgage). This would ensure that the state does not make contributions that are too small in the next few years, and would steadily improve the pension systems' funding ratios. The Universities plan, however, also has several major flaws:

- **It would be highly inequitable in its distribution of costs.** According to its authors, approximately 80% of the projected savings from the Universities proposal would come from reducing the inflation-adjusted benefits of current and former Illinois employees.
- **It would undermine the retirement security of Illinois public-sector retirees, and especially harm those who live a long retirement**. The Universities proposal would cut the annual Cost-of-living adjustment (COLA) in the Illinois pension plans from a fixed 3% to one half the annual percentage increase in the Consumer Price Index (CPI). Assuming an inflation rate of 3% per year, the Universities proposal would cut in half (from 3% to 1.5%) the annual inflation adjustment to retiree benefits under the Illinois pension plans. This translates into a 31% reduction in pension benefits for 25-year retirees. The Universities proposal would protect the retirement income of Illinois public-sector retirees against inflation only half as much as Social Security benefits are protected against inflation.[5] (Social Security benefits are indexed to the Consumer Price Index.) The deep resulting cut in retirement benefits for older seniors would

[4] As noted in the text, the details of the Universities proposal address SURS. Some of the flaws in the Universities plan as applied to the Teachers' and State Employees' Retirement Systems appear to reflect the fact that it was customized to SURS and to some of the specific characteristics of universities and their faculty.

[5] Participants in the Illinois Teachers' Retirement System and State Universities Retirement System do not participate in Social Security. While most active members in the Illinois State Employees' Retirement System (SERS) do participate in Social Security, many SERS retirees do not. An estimated 57% of benefits paid out to SERS retirees in the year ending June 12, 2012 went to members "not coordinated with Social Security." (Source: State Employees' Retirement System of Illinois, *Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2012*, pp. 58 and 60; online at https://www.srs.illinois.gov/PDFILES/oldAnnuals/sers2012.pdf.)

particularly threaten retirement security for lower-income state workers, for school teachers (who do not participate in Social Security and thus do not benefit from its COLA protection), and for retired Illinois state workers who did not participate in Social Security during their public employment.

Under the Universities proposal, we estimate that Illinois public sector retirees who do not participate in Social Security would have inflation protection in their retirement income inferior to the average retirement income inflation protection enjoyed by all but a portion of the richest fifth of all U.S. retirees 65 and over. The inflation protection provided to these Illinois retirees in the Universities proposal would also be as bad as or worse than that in all but two of the other 19 non-Illinois state pension plans across the country (in 10 states) in which pension plan members do not participate in Social Security.

Additionally, the Universities plan would require new employees (and allow existing employees) to enroll in a hybrid pension plan that combines a smaller defined benefit pension with a 401(k)-style individual savings accounts. The combination of the reduction in the defined benefit and a lower cost-of-living adjustment would reduce retirees' benefits by more than half (53%) for 25-year retirees compared to current Illinois pension plan participants who joined the system before 2011 ("Tier 1" employees). On the defined contribution portion of their retirement savings, Illinois public-sector retirees would now bear the financial market, or investment, risk of saving for retirement. Retirees would also risk outliving their savings in the defined contribution portion of the plan — which, unlike the defined benefit portion, would offer them only a lump sum in their investment account rather than an annual payment. The defined contribution portion of the plan would also likely provide future employees with lower investment returns than the current defined benefit plans and would come with higher fees, further reducing the growth of retirement savings.

- **It would hamper the ability of Illinois public employers to attract and retain qualified college-educated employees, including teachers.** Public sector salaries for college-educated public sector workers already trail private salaries for comparable employees (with similar education, experience, and other characteristics). This makes good quality retirement benefits pivotal to retaining talent (as the authors of the Universities proposal acknowledge with respect to higher education). Especially for Illinois teachers, some of whom could get better retirement benefits in non-teaching jobs in the private sector (from Social Security plus an employer-based savings plan), the deep cut in the pension COLA could make the overall school compensation package non-competitive. This could increase the challenge of attracting and retaining outstanding teachers for Illinois public schools.

- **It would introduce a new risk to Illinois taxpayers.** The proposal would reduce funds going into the state's existing defined benefit pools and increase the share of defined benefit pension obligations owed to retirees and to older active employees. This could lead plan managers to invest in more conservative and liquid assets, reducing future investment returns for the existing pension plans and increasing the state's unfunded liabilities, with taxpayers having to make up the difference.

The rest of this brief evaluates in more detail the Universities proposal using our four criteria. In the spirit of "slow and steady wins the race," we argue in the last section for (a) extending the period of time it takes Illinois to fully fund pensions and (b) making sure that adequate contributions are made in the near term so that the plans begin to move to a sound financial footing.

A Lack of Shared Sacrifice

Retirees in Illinois' three main public employee pension plans currently receive a 3% compounded annual cost-of-living increase. Under the Universities proposal, the benefits of current and future retirees in the plans would increase annually by one-half of the unadjusted percentage increase (but not less than zero) in the Consumer Price Index for All Urban Consumers (also known as "CPI-U") over the previous 12 months.

In testimony before the Illinois Senate Executive Committee on June 18, 2013 and the First Conference Committee on Senate Bill 1 on July 3, 2013, the authors of the Universities plan stated that 80% of savings projected under the plan result from lowering benefits through the reduced cost-of-living adjustment.

An Erosion of Retirement Security

The reduction proposed by the Universities plan in Illinois pensions' annual cost-of-living adjustment (COLA) would undercut retirement security in several ways.

The proposal would deeply cut retiree benefits, especially for long-term retirees. The Universities plan authors do not calculate the impact of their proposed COLA modification on pension benefits under any specific inflation scenarios. Calculating this impact drives home how deep a cut in benefits would result. Over the past 30 years (ending June 2013), the CPI-U has increased at a compound annual rate of 2.89%.[6] Assuming for the sake of simplicity a steady future inflation rate of exactly 3%, the Universities COLA proposal would cut the annual inflation adjustment exactly in half — from 3% to 1.5%. The difference between a 1.5% and a 3% annual inflation adjustment quickly compounds to sizable cuts in benefits over time. Ten years after retirement, retirees would receive 14% less in benefits. By 20 years, the cut would be 25%. By 25 years, a length of time for which an increasing share of retirees draw benefits, the cut would be nearly a third (31%).[7]

The Universities proposal would give most Illinois public-sector retirees less protection against inflation in their retirement income than the average inflation protection enjoyed by most other U.S. retired seniors. How would the inflation protection of the retirement income of Illinois public sector workers under the Universities proposal compare with that of other groups of U.S. seniors? Here we compare the retirement income inflation protection of Illinois retirees not covered by Social Security (most Illinois state pension plan retirees) with the same protection enjoyed by two comparison groups: first with other state pension plan workers not in Social Security and, second, with all U.S. non-working seniors 65 and over.

---

[6] Calculated from CPI-U data downloaded from http://data.bls.gov/cgi-bin/surveymost?bls. (To download these data, check the box next to "CPI for All Urban Consumers (CPI-U) 1982-84=100 (Unadjusted) - CUUR0000SA0.")

[7] If future rates of inflation are lower than 3%, of course, the Universities proposal would cut benefits more deeply for current Tier 1 retirees. At an annual inflation rate of 2.5%, the Universities proposal would reduce benefits by 35% for a 25-year retiree.

Outside Illinois, according to the Boston College (BC) pension data base, participants in 19 public employee pension plans in 10 other states do not participate in Social Security. In 13 of these 19 state pension plans, the inflation protection in the state plan is superior in most circumstances to the protection that Illinois workers would have using the proposed Universities plan COLA.[8] In only two of those state plans, the Louisiana State Employee Retirement system and the Texas Teachers' Retirement System, is the COLA typically lower than it would be in Illinois under the Universities plan COLA. We judge the COLA in four of the 19 plans to be roughly "tied" with the Universities plan COLA, on average, across all retiree groups and plausible economic circumstances. (Appendix A details the COLAs in these other state pensions and the sources for the information on their COLAs.)

Turning now to all U.S. non-working seniors, the overwhelming majority of this broader group – including retirees from jobs in the private sector and in the 39 states within which all state pension plans are coordinated with Social Security – enjoy protection against inflation in at least the Social Security benefit portion of their retirement income. (Social Security benefits increase each year based on the Consumer Price Index for all Urban Wage Earners and Clerical Workers, also known as the CPI-W.[9]) As a result of the strong inflation protection in Social Security, the inflation protection under the Universities plan would be inferior to the average retirement income inflation protection enjoyed by four fifths of U.S. retirees 65 and over. Even compared to the remaining (richest) fifth of all U.S. retirees 65 and over, Illinois retirees not in Social Security would at best have similar inflation protection in their retirement income (under the Universities proposal).[10]

[8] This statement is based on the most recent information we were able to find on each plan's COLA, usually from official pension plan documents online. For details and sources, see Table A1.

[9] This index for each month from January 1974 to June 2013 is online at http://data.bls.gov/cgi-bin/surveymost?cw. (To download these data, check "U.S. All items, 1982-84=100 - CWUR0000SA0.") The annual percentage changes in the CPI-W index used by the Social Security Administration and the CPI-U index, referred to in the Universities proposal, differ by no more than 0.5 percentage points in every year since 1947. The average difference between the annual inflation rates shown by the two indices over the period 1947-2012 is 0.0 percentage points.

[10] For all but the richest fifth of non-working seniors, Social Security accounts, on average, for three or more times as much of seniors' income as does "other retirement income." Therefore, even if the other retirement income has no inflation protection at all, the overall COLA for Social Security plus other retirement income is well over half the percentage increase in the CPI-W.

In more detail, Social Security, on average, constitutes between 62% and 90% of 65+ non-working seniors' incomes for the bottom four income quintiles while other retirement income amounts for 2% to 23% of retirement income (source: 2012 Current Population Survey). For the second-richest quintile, Social Security accounts, on average, for 62% of income and other retirement income for 23%. Thus, the average inflation protection for fourth quintile retirees, if their other (non-Social Security) retirement income has no inflation protection, is 0.73 times the CPI-W (0.73 equals 62% as a share of 85% (62% plus 23%)). Even top quintile seniors, on average, get only a modestly larger share of their income from "other retirement income" (40%) than from Social Security (30%). Thus, for the richest fifth, if non-Social Security retirement income has zero inflation protection, the average inflation protection from Social Security plus other retirement income would be 0.43 CPI-W. If the inflation protection for top-fifth non-Social Security retirement income averages 0.13 CPI-W or better, then even the top income quintile enjoys better average inflation protection in its overall retirement income than Illinois public sector workers with no Social Security income would enjoy under the Universities half-CPI proposal. (We thank Nari Rhee of the National Institute on Retirement Security for providing us with 2012 CPS data by quintile on the income of non-working U.S. seniors 65 and over.)

The Universities plan's COLA reduction is more than four times larger than a proposed adjustment to the Social Security inflation index perceived by many as an unacceptable erosion of retirement security. At the federal level, there has been extensive discussion on the merits of adopting the so-called "chained CPI" to set future COLAs for Social Security benefits. A top concern about this change for Social Security has centered on the fact that neither the CPI nor the chained CPI accurately measure the inflation of the goods and services consumed by seniors.[11] Thus, if an adjustment is to be made, the federal government should introduce a chained CPI that accurately measures changes in prices for seniors.

Most relevant in the current context is that a switch to chained CPI without a modification to recognize the higher inflation for the goods and services seniors consume would result in an estimated 0.3% annual cut in inflation-adjusted Social Security benefits. Using a chained CPI price index results in a 5.4% cut in Social Security benefits over 20 years.[12] By comparison, the Universities COLA plan would cut the pension benefits of public-sector retirees in Illinois by more than four times as much as chained CPI would cut the Social Security checks of American retirees.

The particular importance of *not* doing what the Universities plan proposes — in other words, taking care not to weaken the benefit inflation protection of public pension plan participants who do not participate in Social Security — has been recognized in "AARP in the States," a joint publication of the American Association of Retired Persons (AARP) and the National Institute on Retirement Security (NIRS), which states:

> "COLAs are an especially important part of the pension benefit for those employees who do not participate in Social Security, because they are likely to have no other retirement income that increases with inflation. Without a COLA, their purchasing power will steadily decline as they get older. This means that middle class retirees may find themselves struggling to afford even the basics—food, healthcare, housing, and transportation—in their advanced years."[13]

The attempt to dress up the proposed Universities COLA proposal as a balanced compromise is not credible. The Universities plan claims that the proposed COLA provision would better protect retirees against inflation during periods of high inflation. To provide an example to illustrate this hypothetical, the authors go back three decades, to 1973-1982. The economy today is profoundly different, and much less inflation-prone, than the economy of the 1960s and 1970s. That economy had relatively limited price competition, with many core manufacturing industries dominated by a small number of firms (for example, the Big Three in the auto industry). Relative wages were also fairly rigid in the private sector as

---

[11] As noted in "Economist and social insurance expert statement on Social Security COLA: No empirical basis for reducing the Social Security COLA," (online at http://www.epi.org/files/2012/EPI_COLA_Letter.pdf) indices based on the spending patterns of workers or the general population likely understate the impact of cost increases faced by Social Security beneficiaries. Seniors and people with disabilities spend a greater share of their incomes on out-of-pocket medical expenses than do other consumers, and health costs have risen faster than overall inflation in recent decades. This has been documented in the Bureau of Labor Statistics' (BLS) CPI-E inflation measure, which uses consumption weights specific to the elderly. It had 0.2% faster inflation from 1982 to 2007 than the measure currently used to index Social Security benefits. See more at [LOOK FOR A TITLE] http://www.epi.org/blog/chain-chain/#sthash.wLZgadD4.dpuf. See also, Larry Mishel, "To Chain or Not to Chain," http://www.epi.org/blog/chain-chain/

[12] Josh Bivens, "A Protection, Not a Windfall," Briefing Paper #320 (Washington, DC: Economic policy institute, 2011), online at http://w3.epi-data.org/temp2011/BriefingPaper320.pdf

[13] "AARP in the States: Cost of Living Adjustments (COLAs)," a joint brief published by the American Association of Retired Persons, National Retired Teachers Association, and the National Institute on Retirement Security, no date.

a result of collective bargaining and COLA-adjusted wages in core manufacturing sectors, and increases in the minimum wage that tracked inflation and productivity growth (until 1968). These structural features of the economy meant that the oil price shocks of 1973 and 1979 tended to trigger, or accelerate, inflationary spirals. By 1983, however, the deep recession engineered by Federal Reserve Chairman Paul Volcker had wrung inflation out of the economy, and the Federal Reserve Board has since then been committed to keeping inflation to no more than 2%.[14] More fundamentally, the U.S. limited-price-competition, rigid-wage national economy was supplanted by the less inflation-prone, price-competitive, flexible-wage global economy of today.[15]

To be sure, conditions can change. But the structural bias towards low inflation in the current economy is strong, and the evidence and analytics suggest that there is little chance of renewed and consistent high inflation.

The inflation assumptions currently used by the Illinois pension plans and Social Security Administration underscore the implausibility of a rise above 6%. The State Employees' Retirement System assumes a 3% inflation rate and the Teachers' Retirement System assumes inflation of 3.25% annually.[16] The Office of the Chief Actuary for the Social Security Administration currently assumes that cost-of-living adjustments will average 2.8% between 2019 and 2086.[17]

The proposal's hybrid defined benefit-defined contribution plan (see Box 1 below) *would have additional downsides for retired public-sector workers*. Future Illinois public-sector employees would bear increased financial market, or investment, risk in their retirement plan because of the shrinkage of the defined benefit multiplier under the hybrid plan from 2.2% to 1.5%. (In defined benefit pension plans, the initial (or "base") pension benefit (before any adjustments for inflation over the course of retirement) equals the "multiplier" times years of service times the salary used in computing pension benefits, often the average salary over the last few years of service. Thus someone who works 30 years with a multiplier of 2.2% receives a base pension benefit equal to 66% of salary. With a multiplier of 1.5% this benefit drops to 45% of salary.)

The combination of a lower multiplier and a lower COLA would mean a reduction in retiree benefits of more than half (53%) compared to current Illinois pension plan participants who were in the system since before 2011 (i.e., "Tier 1" employees). Retirees would also risk outliving their savings in the defined contribution portion of the plan, which, unlike the defined benefit portion, would offer them

---

[14] Two percent became the formal target in 2012 and was the informal maximum before that.

[15] See, for example, J. Bradford DeLong, "Should We Fear Deflation," *Brookings Papers on Economic Activity*, 1:199, pp. 225-253, online at http://www.brookings.edu/~/media/projects/bpea/spring%201999/1999a_bpea_delong; Michael Piore and Charles F. Sabel, *The Second Industrial Divide: Possibilities for Prosperity* (New York: Basic Books, 1984); and Frank S. Levy and Peter Temin, *Inequality and Institutions in 20th Century America*, MIT Department of Economics Working Paper No. 07-17, online at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=984330.

[16] State Employees' Retirement System of Illinois, *Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2012,* p. 30; online at https://www.srs.illinois.gov/PDFILES/oldAnnuals/sers2012.pdf. Teachers' Retirement System of the State of Illinois, *Comprehensive Annual Financial Report 2012 for the Fiscal Year Ended June 30, 2012*, p. 90; online at http://trs.illinois.gov/pubs/cafr/FY2012/actuarial.pdf. We were unable to find the inflation assumption used by the SURS system in its 2012 Annual Financial Report, online at http://www.surs.com/annual-financial-report.

[17] Office of the Chief Actuary, Social Security Administration, *Long-Range Economic Assumptions for the 2012 Trustees Report,* available on line at http://www.ssa.gov/oact/TR/2012/2012_Long-Range_Economic_Assumptions.pdf, p. 5.

only a lump sum in their investment account rather than an annual payment. The defined contribution portion of the plan would likely provide participants with lower investment returns than the current defined benefit plans and would require participants to pay higher investment fees, which further reduce the growth of retirement benefits. (Below, in Box 2 and the surrounding text, we provide additional details and references regarding the lower investment returns and higher fees of defined contribution plans.)

Box 1. The Universities Plan Proposed Hybrid Pension

The Universities proposal would replace the existing defined benefit pension plan with a "hybrid" plan that includes both a defined benefit and a defined contribution component. The multiplier in the defined benefit plan would fall to 1.5% from the current 2.2%. In addition, individual defined contribution accounts would be established into which one third of employee contributions would go. In the case of SURS, to which employees currently contribute 8% of salary, 2.67% of salary would be diverted from the defined benefit pension plan to employees' individual accounts.[18] The Universities proposal would give existing employees a six-month window to shift into the new hybrid plan. Younger employees are probably more likely than more senior employees to switch to the hybrid plan because younger employees are less certain about whether they will remain in state employment for the rest of their careers. By lowering the defined benefit pension of new employees (and for a disproportionately younger group of current employees), the Universities proposal will age the profile of pension obligations owed by the state's defined benefit pension plans. The reduction in the defined benefit pension COLA would also age the pension obligations of the Illinois pension plans: the reduction in benefits because of a lower COLA will be smaller for older retirees than younger retirees (and for future retirees) because older retirees have a shorter life expectancy in their remaining retirement and hence a shorter period of time in which the lower COLA will erode their benefits.

Undermining the Recruitment and Retention of College-Educated Employees, Including Teachers

For employers, private as well as public, retirement plans are not simply a cost: they are also a critical component of human resource policy. Retirement plans, in combination with salaries, health care plans, and other benefits, must be competitive enough with other job opportunities to enable employers to attract and retain high-quality and productive employees. The Universities proposal recognizes this when it expresses concern about the inadequacies of "Tier 2" pensions (established for employees hired after January 1, 2011) to enable higher education in Illinois to compete with out-of-state peers for talent. Specifically, the authors say:

[18] Under the Universities proposal, universities would also make a mandatory annual contribution equal to 1% of total pensionable pay to the DC account of each employee. In addition, each university would have the flexibility of requiring additional employer/employee contributions to the DC plan. The authors of the Universities plan explain this last feature of their proposal (p. 5) as follows: "Employers will have the flexibility to vary the contribution amounts in order to optimize their human resource goals related to their own workforce recruitment and retention needs in a manner consistent with all applicable laws." The additional mandatory and voluntary employer contributions to University employees' individual accounts may help universities avoid recruitment and retention challenges under the Universities proposal. If the state and schools do not make similar additional employer contributions to their employees' individual accounts, then these features cannot help the state and schools recruit and retain their employees.

> "The inadequacies of the Tier II system put Illinois public universities at a serious disadvantage compared to their out-of-state peers and threaten the continued vitality of higher education in Illinois; no pension reform plan would be complete without addressing Tier II reform."

On page 4 of their proposal, the authors add: "No pension reform will be complete without rectifying the problems in the Tier II plan that went into effect on January 1, 2011."

Having twice noted the inadequacies and problems of Tier 2, however, the authors of the Universities proposal then go on to propose a plan that could be as bad as or worse than Tier 2 because of the reduction in the defined benefit portion of the plan from a 2.2% multiplier to 1.5%.[19]

For college-educated public-sector state and school employees, such as teachers, the Universities proposal could lead to a level of retirement benefits and overall compensation that is non-competitive with private sector non-teaching jobs. National studies show that the average compensation (wages plus benefits) of state and local public-sector workers with a college degree trails the private sector by 25%.[20] (To our knowledge, no study of the public-private wage and benefit gap in Illinois has been published recently.) Given the compensation gap, and the even larger wage and salary gap (i.e., the gap before taking benefits into account), good pension and health care benefits in the public sector play a critical role in attracting and retaining high-quality and experienced college-educated workers.

Under the Universities proposal, however, retirement benefits in Illinois are unlikely to be better for many college-educated public-sector workers — especially for K-12 school teachers who do not participate in Social Security — than those that many college-educated workers could obtain in the private sector. In the private sector, employees can enjoy a combination of Social Security benefits and, in some cases, an employer-based defined contribution or defined benefit retirement plan. Thus, the overall pay package for Illinois public school teachers could become increasingly non-competitive. This would compound the challenges of attracting and retaining a great teacher for every Illinois public school classroom.

---

[19] The Universities plan inflation proposal (half CPI) is slightly better than the Tier 2 COLA, which equals the lower of 3% or half the Consumer Price Index, non-compounded. The University proposal authors also appear to view their hybrid plan as superior to Tier 2 for some University employees because it is more portable (with slightly shorter vesting periods and the portability of the defined contribution portion of the plan) and because universities make additional (mandatory and voluntary – see the previous footnote) employer contributions to employees' self-managed defined contribution pension plans. School districts are unlikely to make additional contributions and portability is also less valuable to elementary and secondary school teachers, who move across state lines much less than University faculty.

[20] Jeffrey Keefe, *Debunking the Myth of the Overcompensated Public Employee: The Evidence* (Washington, D.C.: Economic Policy Institute, September 15, 2010), Table 2, online at http://www.epi.org/files/page/-/pdf/bp276.pdf. Keefe has also done a number of state-specific studies, including for states similar to Illinois such as Wisconsin and Pennsylvania, with the results similar to those found in the national study.

The Impact of the Universities Proposal on Taxpayers

The debate about Illinois pensions has been waged largely in the name of fiscal responsibility. Despite this, three aspects of the Universities proposal could result in higher costs to taxpayers, lowering or eliminating projected savings from the plan.

- As explained in Box 1, the Universities proposal would reduce funds going into the state's existing defined benefit pools and change (i.e., make older) the age profile of the pension obligations owed by the pension systems. These shifts could erode future investment returns for the existing pension plans and increase the state's unfunded liabilities.

- The proposed hybrid pension plan represents a partial shift from defined benefit pensions to less efficient defined contribution accounts which deliver less retirement security for any given level of employee plus employer contributions. Employees are not the only stakeholders hurt by a switch to less efficient retirement plans. Especially if lower-quality retirement benefits make the overall compensation package unattractive to current or potential employees, taxpayers may pay a price as well: to offset lower-quality (and inefficient) retirement plans and retain the caliber of employee they want, public employers may have to raise wages and salaries, increasing taxpayer costs.

- The Illinois courts may well rule the reduction in the COLA formula constitutionally impermissible. If the courts take several years to rule while Illinois banks pension savings that the courts then reject, the pension system will end up in even more difficult financial straits.

Lower investment returns and a higher unfunded liability. As noted, the Universities proposal would shift new employees into a hybrid pension plan that shrinks the defined benefit plan multiplier to 1.5% from 2.2%. Taking into account this reduction and the lower COLA for new employees, the defined benefit pension obligations for new employees would decline by roughly 40%.[21]

When defined benefit pensions close completely, the actuarial consensus from studies in other states is that the aging of remaining plan participants leads to a substantial erosion in investment returns and an increase in defined benefit pension plan unfunded liabilities. The reasons for this include a shrinkage of the time horizon of the pension plan and also an increasing need for liquidity as pension plans pay out a rising proportion of their assets in pension checks.[22] The impact on investment returns under the

[21] The decline from 2.2% to 1.5% is a reduction of 32%. If we assume that the average public-sector retiree from the state pension system lives 20 years, then the lower COLA erodes benefits by another 14%. The combination of a 32% decline and a 14% decline is a drop of 41%. This calculation does not consider any other (smaller) reductions in benefits in the Universities proposal.

[22] For more detail on how changing the age profile of defined benefit pension plan participants impacts investment returns, see Stephen Herzenberg and Sarabeth Snuggs, *A Misguided "Solution to a Nonexistent Problem*, Keystone Research Center, March 26, 2013, online at http://keystoneresearch.org/publications/research/florida-pensions, pp. 3-6. Two new actuarial studies in Pennsylvania recently reached similar conclusions about the transition costs of moving from a defined benefit to a defined contribution pension: see "Letter from Dana Spangher, Consulting Actuary, Buck Consultants, to PSERS Executive Director Jeff Clay, Transmitting an Actuarial Note on HB1350 (Printer's No. 1760)," June 11, 2013; and Hay Group, "Actuarial Cost Note Regarding H.B. 1350, P.N.1760," May 2013, p. 4. These two actuarial studies are summarized in Public Employment Retirement Commission, "Actuarial Note Transmittal: House Bill 1352," online at http://www.pasbo.org/PERCActuarialNoteHB1352.pdf; and Stephen Herzenberg, *A $40 Billion Dollar Oversight: Actuarial Studies Document High Cost of Governor Corbett's Pension*

Universities proposal could be an attenuated version of the erosion of investment returns that would result from closing the defined benefit plans entirely. Until the funded ratios of Illinois pension plans improve, Illinois pensions may be particularly vulnerable to lower investment returns because of a need to keep a high proportion of assets in liquid forms.

A dozen states that considered closing their defined benefit plan chose not to do so because of the taxpayer costs that result when investment returns on plan assets fall.[23] Actual experience in three states that have closed defined benefit plans also shows that unfunded liabilities can grow.[24] Given the size of the Illinois pension plan unfunded liabilities, state policymakers should be particularly cautious about any proposal that has the potential to lower investment returns on pension plan assets.

A Partial Shift to Less Efficient Pensions. According to the National Institute on Retirement Security , defined benefit pension plans deliver about twice as much retirement income for any given level of employer and employee contributions.[25] Taxpayers can be hurt when any given level of retirement security becomes more expensive if, partly as a result of this inefficiency, the overall wage and benefit package for certain employees (e.g., teachers) becomes uncompetitive with the private sector. In this circumstance, public employers have to improve wages and or benefits to achieve competitive compensation, resulting in higher costs to taxpayers.

Defined contribution plans are less cost-effective for a number of reasons:[26]

- They have higher administrative costs because of the need to manage individual accounts and higher marketing (or educational) costs incurred to educate plan participants about their investment options.

- They deliver lower investment returns because individuals making investment choices do not match the returns of investment experts who manage defined benefit pooled funds.

- They have higher financial management and trading fees.

- They do not pool “longevity risk.” When individuals convert their accumulated savings into an “annuity” — a fixed payment until they die — their annuity payment is lower because the provider of the annuity knows that there is a reasonable chance that the individual may live much longer than average. Since Illinois’s defined benefit plans do pool longevity risk — across hundreds of thousands of plan members — they know that plan participants, *on average*, will

---

Plan, KRC pension primer #7, online at http://keystoneresearch.org/publications/research/pension-primer-7-40-billion-dollar-oversight.

[23] For an annotated bibliography and online links to studies conducted in these dozen other states, see Herzenberg and Snuggs, *A Misguided “Solution to a Nonexistent Problem*, Appendix B.

[24] For more information on these three states see the discussion of Alaska, Michigan, and West Virginia and the original sources cited in Herzenberg and Snuggs, *A Misguided “Solution to a Nonexistent Problem*, Keystone Research Center.

[25] Beth Almeida and William B. Fornia, *A Better Bang for the Buck*, National Institute on Retirement Security, August 2008, online at http://www.nirsonline.org/index.php?option=com_content&task=view&id=121&Itemid=48.

[26] See Almeida and Fornia, *A Better Bang for the Buck*. See also, Robert Hiltonsmith, *The Retirement Savings Drain: The Hidden and Excessive Costs of 401(k)* (New York: Demos ; online at http://www.demos.org/sites/default/files/publications/TheRetirementSavingsDrain-Final.pdf.)

live exactly the expected number of years. Thus, annual benefit payments do not need to be pared back to insure against a longer drawdown of benefits. Furthermore, defined benefit plans provide their low-cost annuities to all retirees. Defined contribution plans do not offer annuities, so retirees from defined contribution plans have to buy the higher-cost annuities on their own — something that very few retirees currently do.

In May 2013, the human resources firm Towers Watson published an update on the investment returns of defined benefit pensions compared to defined contribution retirement plans. It found that defined benefit pension plans outperformed defined contribution plans by nearly 3 percentage points in 2011 and by 0.76 percentage points from 1995 to 2011.[27] Among the largest one-sixth of plans, the group into which the Illinois pension plans fall, defined benefit pensions outperformed defined contribution plans by 0.99 percentage points. *Forbes* magazine succinctly summarized the Towers Watson research by saying "Pension Plans Beat 401(k) Savers Silly."[28] In Florida, public employees have had the option over the past decade to participate in a state-administered defined contribution account or the state's defined benefit pension. The results of this "natural experiment" line up closely with the Towers Watson findings: the investment returns of the Florida defined-benefit plan so far exceed those in the aggregate of all individual accounts by 0.76 percentage points per year.

Box 2. Just How Good Are 401(k)-type Defined Contribution Retirement Plans?

A growing number of recent reports and news stories note that defined contribution plans are a bad deal for workers, providing much less retirement security than defined benefit pension plans. Defined benefit pension plans tend to beat 401(k)s on investment returns, reducing employer and employee costs for the same level of retirement security. 401(k)s come with higher fees and often don't provide the retirement security promised to workers.

"How Defined Benefit Retirement Plans Outperform Defined Contribution Plans"
Teresa Ghilarducci and Joelle Saad-Lessler
July 17, 2013, online at
http://www.huffingtonpost.com/teresa-ghilarducci/how-defined-benefit-retir_b_3605720.html

> "A recent report from the Employee Benefit Research Institute (EBRI) sheds light on how badly lower income workers fare under the new defined contribution (DC) system compared with the defined benefit (DB) plans of old. For workers with 31 to 40 years of plan eligibility, their returns under the DC system are 10-13% worse than they would have been under a DB system…Sadly, this picture will likely be even worse for lower income workers because the report uses unrealistically rosy assumptions."[29]

[27] Brendan McFarland, "DB Versus DC Investment Returns: The 2009 – 2011 Update," *The Insider*, May 2013, online at https://www.towerswatson.com/en-US/Insights/Newsletters/Americas/insider/2013/DB-Versus-DC-Investment-Returns-the-2009-2011-Update
http://www.towerswatson.com/en/Insights/Newsletters/Americas/insider/2013/DB-Versus-DC-Investment-Returns-the-2009-2011-Update

[28] Mitch Tuchman, "Pension Plans Beat 401(k) Savers Silly," Forbes, June 4, 2013, online at http://www.forbes.com/sites/mitchelltuchman/2013/06/04/pension-plans-beat-401k-savers-silly-heres-why/.

[29] For a more comprehensive academic treatment of the limitations of 401(k)-style individual accounts, see Teresa Ghilarducci, *When I'm Sixty Four: The Plot Against Pensions and the Plan to Save Them* (Princeton, NJ: Princeton University Press, 2008).

[Pension Plans Beat 401(k) Savers Silly -- Here's Why](http://www.forbes.com/sites/mitchelltuchman/2013/06/04/pension-plans-beat-401k-savers-silly-heres-why/)

Forbes, June 4, 2013, online at http://www.forbes.com/sites/mitchelltuchman/2013/06/04/pension-plans-beat-401k-savers-silly-heres-why/

> "Towers Watson, the global human resources consultant, found that pension-style plans beat 401(k)-style offerings by nearly 3 percentage points in 2011, the latest study year. Pensions made investment returns of 2.74% while defined contribution plans lost money, banking -0.22%. It's no fluke. Pension plans often beat 401(k) plans. … Part of the reason is mutual fund fees. Mutual funds in the plans studied had weighted average expenses of 65 basis points in 2011, a drag which reduced overall returns by 31 basis points. Nearly half of the 401(k)-type plans were composed of mutual funds, compared to just 14% in the pension-style plans."

Retirement Gamble: Frontline's Powerful Case for Taking Control of Your Financial Future

Time Magazine, April 23, 2013, online at http://business.time.com/2013/04/23/retirement-gamble-how-fees-and-poor-results-destroyed-your-401k/#ixzz2Ws85q2E6

> "Traditional pensions have been supplanted by 401(k) plans, which have proved to be massively ineffective as a primary source of retirement security. Billions of dollars in savings have leaked out of these plans over the years and trillions were wiped away in the market collapses of 2000 and 2008."

Abolish the 401(k): The real crisis facing America's aging society is not Social Security, but private retirement plans

Salon.com, April 4, 2013, available online at http://www.salon.com/2013/04/04/abolish_the_401k/

> "But the risks, including risks from poor investments and the chance that you will retire during a stock market downturn, fall entirely on the individual. Even worse, many working-class and middle-class Americans with 401Ks are stealthily fleeced by money managers, who charge high and often difficult-to-find fees for allocating retirement money among stocks, bonds and other assets."

The Greatest Retirement Crisis In American History

Forbes, March 20, 2013, available online at http://www.forbes.com/sites/edwardsiedle/2013/03/20/the-greatest-retirement-crisis-in-american-history/

> "Americans also know the great 401k experiment of the past 30 years has been a disaster. It is now apparent that 401ks will not provide the retirement security promised to workers. As a former mutual fund legal counsel, when I recall some of the outrageous sales materials the industry came up with to peddle funds to workers, particularly in the 1980s, it's almost laughable—if the results weren't so tragic."

What Will Replace the 401(k)?

Time Magazine, March 21, 2012, available online at http://business.time.com/2012/03/21/what-will-replace-the-401k/#ixzz2Ws9a3Kir

> "With little or no return for more than a decade—and just as baby boomers begin to retire—the savings crisis has pushed us to new levels of despair. More than half the population has less than $25,000 saved for retirement, according to the Employee Benefits Research Institute."

The Universities COLA proposal could well be constitutionally impermissible. The authors of the Universities proposal state: "In our view, it would be constitutionally permissible to reduce the expected average future increase in exchange for the valuable insurance protection that individuals would receive during periods of high inflation." In our view, it could well be constitutionally impermissible simultaneously to require 2% more in Tier 1 contributions phased in over four years, and cut annual cost-of-living adjustments so that benefits by the end of a typical retiree's life falls by roughly a third — all in exchange for purported protections from periods of high inflation which have very little chance of occurring for the next generation of retirees.

Rethinking Sustainability

In closing, this briefing paper makes two recommendations regarding the sustainability of the Illinois pension systems.

First, giving employers and employees the right to enforce the state's pension funding obligation through the legal system should be explored. This idea is raised in the Universities plan as a trade for the employee sacrifices in that plan. While we do not endorse the specific sacrifices proposed in that plan, we acknowledge that some sacrifices may be needed. In light of the threat that state underfunding poses to the ability of the pension systems to pay promised benefits, if sacrifices can be defined that do not violate the strong retirement benefit protections in the Illinois Constitution, giving employers and employees a legal right to enforce the state's pension funding obligations would have merit.

Second, level-dollar funding (similar to a mortgage) should be considered as a way of ensuring steady improvements in the funding ratio of the Illinois plans. This could be coupled with extending the time taken to get to 100% funding. While some debates about public pensions highlight the need to get to 100% full funding as quickly as possible, and certainly within 30 years, a more important goal is to ensure sufficient near-term funding to get Illinois on a stable path to higher funding ratios.[30]

The Universities proposal makes a similar point about the greater importance of getting on a path to full funding as compared to doing this in a particular period of time.

> "An important aspect of pension reform is for the state to fill up the hole left by past underfunding by amortizing the unfunded liabilities…To instill confidence in the pension system, the state must ensure a steady flow of funds in accordance with an agreed-upon schedule of payments. Some have suggested the payment schedule passed by the legislators in 1995 with one that achieves 100% funding in 30 years. While this is a laudable goal, what is more

[30] There are two rationales that apply specifically to Illinois for stretching the time that it takes to get to full funding. First, the Illinois pension plans ordinarily substitute for retirement income provided to state pension plan members in other states by the combination of Social Security and their state pension plan. While other states aim to fully fund their pension plans, Social Security is a pay as you go system. Therefore, expecting Illinois plans to get to 100% pre-funding is to hold them to a higher standard (in terms of pre-funding) than are held the combination of Social Security and a state pension plan in other states. Second, some observers see underfunded pensions as a form of intergenerational inequity, with underfunded pensions an unfair burden passed onto future generations. Even if one accepts this argument, generational inequity arguably *increases* if a state pays down too quickly unfunded liabilities, because this imposes the costs on a single generation of taxpayers (or portion of one). It would increase equity to stretch over more than one generation the time to get to 100% funding.

> important than the 30-year timeline is a steady stream of funding at an agreed upon rate and improving the funding ratio steadily.
>
> "Regular and full payments in accordance with an agreed upon payment schedule that steadily improves the funding ratio will raise confidence in the system even if it takes longer to achieve 100% funding. It is important, however, that the payment schedule is calculated based upon a straight-line amortization of the current unfunded liabilities. . . ."

As the authors explain, straight-line amortization means equal payments each year, as with a home mortgage, and makes sure that payments are not back-loaded in a way that "kicks the [state pension funding] can down the road" again.

In a similar vein, Ralph Martire of the Center for Tax and Budget Accountability (CTBA) recently endorsed a "level dollar approach" to paying down the state's unfunded liability and a stretching out of the period over which the state approaches full funding (i.e., Martire proposes reaching "well over" 80% funded by FY2059).[31]

In closing, Illinois needs a balanced approach to resolving its pension crisis. It needs to achieve financial sustainability of state retirement systems. But Illinois also needs to avoid eroding retirement security to the point that its oldest public-sector retirees experience drops in their living standards and its schools offer pay and benefits inadequate to retain the most effective teachers, jeopardizing the quality of education that Illinois children deserve and the state's long term economic future requires.

---

[31] Ralph M. Martire, "Written Summary of Oral Testimony Provided to the Pension Conference Committee," July 3, 2013; online at http://www.ctbaonline.org/New_Folder/Pension/7.3.2013%20CTBA%20Pension%20Committee%20Testimony.pdf

Table A1. Cost-of-Living Adjustments in Other State Pension Plans in Which Members Do Not Participate in Social Security			
#	**Planname**	**Cost-of-Living Formula**	**Higher or Lower COLA than Half-CPI Proposal for Illinois**
1	Alaska Teachers*	75% of the cost-of-living increase in the preceding calendar year or 9%, whichever is less, if the recipient is at least age 65 or on TRS disability on July 1 ; in addition, if you reside in Alaska after you retire, COLA equal to 10% of your base benefit	Higher
2	Alaska PERS*	75% of the cost-of-living increase in the preceding calendar year or 9%, whichever is less, if the recipient is at least age 65 or on PERS disability on July 1	Higher
3	California Teachers	2% per year, not compounded. Since 2008 the TRB has been authorized to provide "Supplemental Benefit Payments", to increase the COLA to no less than 80% and no more than 85% of your initial payment.	Higher if CPI is less than 4% and for long-term retirees
4	Colorado State	Varies by date of hire, automatic 2% unless negative investment return in previous year, then lesser of CPI-W or 2%, compounded	Higher in most circumstances if CPI is less than 4%
5	Colorado School	Varies by date of hire, automatic 2% unless negative investment return in previous year, then lesser of average monthly CPI-W or 2%, compounded	Higher in most circumstances if CPI is less than 4%
6	Colorado Municipal	Varies by date of hire, automatic 2% unless negative investment return in previous year, then lesser of average monthly CPI-W or 2%, compounded	Higher in most circumstances if CPI is less than 4%
7	Connecticut Teachers	Retired before 9/1/92: CPI-linked (Range: 3%-5%). Retired on/after 9/1/92 and members before 7/1/2007: pension benefit adjustments are made that are consistent with those provided for Social Security benefits on January 1 of the year granted, with a maximum of 6% per annum. If the return on assets in the previous year was less than 8.5%, the max increase is 1.5%. Members after 7/1/2007: pension benefit adjustments are made that are consistent with those provided for Social Security benefits on January 1 of the year granted, with a maximum of 5% per annum. If the return on assets in the previous year was less than 11.5%, the max increase is 3% and if the return on assets in the previous year was less than 8.5%, the max increase is 1%.	Higher for most workers in most circumstances. Less for retirees since 7/1/07 if return on assets less than 8.5% and CPI more than 2% and for earlier retirees with same returns and CPI over 3%
8	Kentucky Teachers	Automatic 1.5% compounded; In addition to the standard one and one-half percent (1.5%) COLA, KTRS asks the Governor and General Assembly each biennial budget period for an additional “ad hoc” COLA to help retirement allowances keep pace with inflation (e.g., 0.8% COLA effective July 1, 2006, and 0.6% COLA effective July 1, 2007).	Lower if CPI exceeds 3%; higher if CPI is less than 3%

9	Louisiana Teachers	Subject to approval by the legislature and contingent upon funding available in COLA account consisting of excess investment returns; COLA lesser of 3% or CPI-U if investment returns equal at least 8.25%; if investment returns are less than 8.25%, COLA lesser of 2% or CPI, if system at least 80% funded and zero otherwise; COLA applies only to first $70,000 of benefit, indexed to CPI; participants may elect retirement option providing an actuarially reduced benefit with auto annual 2.5% COLA beginning at age 55	Higher for most retirees (with benefits up to $70,000) if funds available and legislature approves
10	Louisiana SERS	No COLAs have been awarded since 2008. Cost-of-living adjustments (COLAs) are funded through excess investment earnings, which are earnings above the LASERS expected actuarial return, and above the hurdles that have been legislatively established to help reduce the debt owned to the system. The expected return was recently lowered from 8.25 percent to 8 percent. Prior to 2008, lesser of 2% or CPI, plus up to 1% additional based on investment return.	Lower since 2008. Could be higher in some future years depending on investment returns and especially if CPI is less than 4%
11	Massa-chusetts Teachers	Cost-of-living adjustments are granted to MTRS benefit recipients by vote of the Massachusetts Legislature. Every year, the Public Employee Retirement Administration Commission (PERAC) files with the Legislature a report detailing the increase or decrease in the Consumer Price Index (CPI). The Legislature then votes whether to grant a COLA based on the increase in the CPI or 3%. Since 1999, 3% every year on first $12,000 or $13,000 (starting 2012) of benefits	Likely lower for employees with starting benefits over $26,000; higher for employees with starting benefits under $26,000 if inflation 3% or above
12	Massa-chusetts SERS	Cost-of-living adjustments are granted to MTRS benefit recipients by vote of the Massachusetts Legislature. Every year, the Public Employee Retirement Administration Commission (PERAC) files with the Legislature a report detailing the increase or decrease in the Consumer Price Index (CPI). The Legislature then votes whether to grant a COLA based on the increase in the CPI or 3%. Since 1999, 3% every year on first $12,000 or $13,000 (starting 2012) of benefits	Likely lower for employees with starting benefits over $26,000; higher for employees with starting benefits under $26,000 if inflation 3% or above
13	Nevada Police Officer and Firefighter	All percentages compounded annually. Cost-of-living increases are provided after three full years of benefits at the rates of 2% in each of the fourth, fifth, and sixth years; 3% in years seven, eight, and nine; 3.5% in years 10 and 11; and 4% in year 12 and each year thereafter. Post-retirement increases can be reduced if benefit outpaces inflation and is based on a rolling three-year average of the Consumer Price Index.	Lower for employees retired in the previous three years. Higher in most circumstances for other retirees.
14	Nevada Regular Employees	All percentages compounded annually. Cost-of-living increases are provided after three full years of benefits at the rates of 2% in each of the fourth, fifth, and sixth years; 3% in years seven, eight, and nine; 3.5% in years 10 and 11; and 4% in year 12 and each year thereafter. Post-retirement increases can be reduced if benefit outpaces inflation and is based on a rolling three-year average of the Consumer Price Index.	Lower for employees retired in the previous three years. Higher in most circumstances for other retirees.

15	Ohio Teachers	Members retired before July 1, 2013 (including those already retired) will not receive a COLA during the 2014 fiscal year (July 1, 2013–June 30, 2014). Members who retire effective July 1, 2013, will not receive a COLA on July 1, 2014. After missing one COLA, these retirees will resume COLAs at 2% per year. Members retiring Aug.1, 2013 or later, will also receive a 2% COLA, but it will not begin until the fifth anniversary of retirement.	Lower for one year upcoming for retirees effective on or before July 1, 2013; lower for first five years for retirees on 8/1/13 or later. Higher otherwise as long as CPI is less than 4%.
16	Ohio School Employees	3% non-compounded	Higher if CPI is less than 6%
17	Ohio Police & Fire	Current retirees and those with 15 years experience with OP&F as of 1/1/13 receive a non-compounded 3%; those with less than 15 years experience and new hires receive the lower of 3% and the CPI	Higher if CPI is less than 6%
18	Ohio PERS	Non-compounded 3% for retirees who retired by 1/7/13; 3% until 12/31/18 for people who retired after 1/7/13, then CPI thereafter	Higher for most retirees if CPI < 6% and for some retirees above that level
19	Texas Teachers	The TRS retirement plan does not provide for regular cost-of-living increases to the amount of your annuity. Any post-retirement increase in benefits must be authorized by the Texas Legislature.	Ordinarily lower

*The Alaska pension plans closed to new members in 2006.

Sources.

List of state plans exempt from Social Security based on Boston College pension data extracted from *http://pubplans.bc.edu/pls/apex/f?p=1988:22:8035009569023::NO:RP::*

1. http://doa.alaska.gov/drb/trs/employee/faqs/
2. http://doa.alaska.gov/drb/pers/retiree/plan/prpa.html
3. Milo Gwosden, A Capital Rabbit's Guide to CALSTRS Pensions, June 3, 2012
4. http://www.wikipension.com/wiki/Cost_of_Living_Adjustment; corroborated by http://online.wsj.com/article/SB10001424052748704463504575301032631246898.html
5. http://www.wikipension.com/wiki/Cost_of_Living_Adjustment; corroborated by http://online.wsj.com/article/SB10001424052748704463504575301032631246898.html
6. http://www.wikipension.com/wiki/Cost_of_Living_Adjustment; corroborated by http://online.wsj.com/article/SB10001424052748704463504575301032631246898.html
7. http://www.ct.gov/trb/lib/trb/formsandpubs/cola.pdf
8. http://ktrs.ky.gov/02_retired_members/01_retirement_benefits.htm
9. http://www.trsl.org/main/inside.php?section=retirees&tables=y&page=what_is_pbi
10. http://lasersonline.org/site.php?pageID=168
11. http://www.mass.gov/mtrs/benefit-recipients-retirees-and-survivors/your-benefit-payment/cost-of-living-adjustments/
12. See previous line plus http://www.massbudget.org/report_window.php?loc=Pension_3_11.html
13. http://slge.org/wp-content/uploads/2011/12/State-DB-Plan-Fact-Sheet_Nevada.pdf

14. http://slge.org/wp-content/uploads/2011/12/State-DB-Plan-Fact-Sheet_Nevada.pdf
15. https://www.strsoh.org/pdfs/brochures/20-101.pdf
16. Ohio School Employee Retirement System, Service Retirement Guide entitled *Destination: Retirement--Reaching Your Destination*, revised 1/1/13, p. 32, available online at http://www.ohsers.org/retiree-publications
17. http://www.op-f.org/Information/SenateBill340FAQ.aspx#
18. http://www.youtube.com/watch?v=7358uSpmIuw
19. TRS Benefits Handbook December 2011, p. 38; http://www.trs.state.tx.us/benefits/documents/benefits_handbook.pdf#Home