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Vermont Treasurer: Pension problem needs to be a priority in 2014

By Nancy Remsen

MONTPELIER — Treasurer Beth Pearce had a hard act to follow when she stood before House and Senate members recently to urge them to solve a thorny pension problem when they reconvene in January.

Lawmakers, in Montpelier for an update on issues prior to the 2014 session, had already been told by their economic consultant that tax revenues were stable. But Tom Kavet also advised legislators that revenues weren't growing nearly fast enough to keep pace with spending trends, creating a potential $72 million shortfall. Legislators also learned that property tax rates would need increase again next year because property values had yet to recover from the recession. And they were reminded that federal funding was sure to shrink.

Pearce pitched yet another problem which she said had to be a priority in the coming session. The financial integrity of the teacher pension fund is threatened by the absence of a source of funding to cover health care costs for retirees, she told lawmakers. The expense — projected to rise to $28 million for the next budget year for 7,700 retired teachers — eats a hole in the money being set aside for pensions.

Couple this unfunded liability with investment losses during the recession and the several years when policymakers skimped on contributions and it adds up to a teacher pension fund that has only 60.6 percent of the money it needs to meet its projected obligations, Pearce said.

The pension fund loses more ground each year that the health care problem remains unresolved, she added, despite improved discipline in meeting contribution targets and revised expectations about investment income.

"The bottom line for me is we need to find a funding source for teacher retiree health care," Pearce said. At least $20 million would need to be set aside this year, increasing with inflation in the future. This amount would be in addition to the annual contribution the state makes to the teacher pension fund — projected at $73.9 million next year.

"This is not going to be easy," the treasurer acknowledged to the legislative audience. "I know this is a difficult year. I know we have had a number of difficult years."

Still, ignoring the problem again — she has issued past warnings — only makes it more difficult to solve, she advised. "There is some urgency in resolving this. The longer you delay, the more expensive it is."

House Republican Leader Don Turner of Milton applauded Pearce's presentation. He had wanted the Legislature to address the problem last session, but it wasn't a priority. Now, he said, "Beth is pushing harder and people are starting to listen."

Pearce has done more this year than make a plea at the Legislature's pre-session briefing. She convened a group that includes representatives from the Vermont National Education Association, legislative leaders and their financial staff and representatives from the Shumlin administration and challenged them to join her in coming up with recommendations by January.

"We have to address this at some point and I think it is this year," House Speaker Shap Smith, D-Morristown, said last week. He has been participating in the brainstorming sessions. He agreed that finding a remedy everyone can swallow may prove difficult.

"Everything is going to be on the table," Smith said. "We are going to have pretty tough conversations."

“At this point there is not clear path,” Darren Allen of the Vermont NEA confirmed.

The union is committed to finding a solution because the sustainability of the pension fund is at stake, he said. “We have to essentially find $20 million to ensure that promised benefits are paid for.”

Pension challenges

Pensions have come under increasing scrutiny in recent years in Vermont and elsewhere as governments — and the private sector — wrestle with the effects of the recent recession on investment income and budgets, and prepare to grapple with the impact of a looming bubble of baby-boomer retirees. Vermont responded with studies of its teacher and state employee pension systems that led to a series of statutory revisions to benefits and contributions. The changes to the teacher pension system approved in 2010 generate $15 million in annual savings. Changes to the state system in 2011 produce $5 million in annual savings.

Pearce said her office has been able to make several other changes in the teacher system without legislative action that produce savings. One change takes advantage of a federal Medicare prescription drug program and saves the state about $2.3 million a year on prescriptions medicines for retired teachers.

“The cost savings come from leveraging pharmaceutical discounts and government subsidies,” Pearce explained in an August news release about the plan.

In addition to annual cash savings, converting drug coverage for retired teachers to this program results in a new calculation of the post-employment benefit liability. The unfunded total liability for retiree health care shrinks by $203 million to $704 million because of the projected future savings from the drug program. Helpful, Pearce said, but not sufficient to eliminate the drag that the ongoing unfunded health care expense puts on the pension fund.

Remedies

Democratic House Speaker Smith and House Republican Leader Turner agree — for now — that raising new taxes shouldn’t be seen as the way to find the $20 million a year to fund retired teacher health care. “The taxpayers can’t afford that,” Turner said.

“My preference would be to do it without raising new revenue,” Smith said.

Smith also rejects stripping benefits away from teachers who have already retired or have been teaching for years under the expectation they would have health coverage when they retire.

Turner suggests, however, “I think you have to go back to the negotiating table and figure out a better way going forward.”

There might be other ways to save money, Pearce said.

For example, Maine assesses some pension costs to federal grants that fund some of its teachers. Vermont might be able to do that, but it would require policy changes and would have to be phased in, she noted.

The state might also revise its plan to pay down the unfunded liability in the teacher pension fund. If the state made bigger payments now, it would save interest costs — which amount to millions of dollars through the 2038 pay-down date set in law.

“While review of federal funding and revisions to amortization schedules will assist in remediating the problem,” Pearce noted in the final slide of her presentation, “the single most important step is an immediate and significant increase in funding.”

That’s why she wanted the teacher pension problem on the same priority list as the projected budget shortfall and property tax increase. When it comes time for lawmakers to start allocating the state’s money pie for next year, Pearce said she hopes retired teacher health care would be considered for a bigger slice.

“It is time,” she said.