Testimony before the

New Hampshire House Special Committee on Public Employee Pensions Reform

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Presented by

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Chairman Hawkins, Vice Chair Sendensky, members of the House Special Committee on Public Employee Pensions Reforms and guests, thank you for the opportunity to present testimony today on behalf of AARP regarding retirement income security and the New Hampshire Retirement System (NHRS). First, let me say that I applaud New Hampshire for conducting debates on the status of public employee retirement in an open, transparent, and inclusive manner.

Since the beginning of the recession the majority of states have reviewed their pension promises, making changes both modest and large to their retirement systems to ensure that these plans are able to provide a significant source of retirement income for generations to come.

AARP is the largest nonprofit, nonpartisan organization representing the interests of Americans age 50 and older, and their families, in the State of New Hampshire. Nearly half of our 227,000 New Hampshire members are employed full or part-time, and as such, AARP is *greatly* concerned about their retirement security, whether they have access to Social Security, an employer sponsored defined benefit plan, an employer sponsored defined contribution account, and/or other personal retirement savings.

Assuring that 50+ Americans have more secure retirement benefits and savings and have improved options and information to make key decisions about their retirement benefits is a critical concern for AARP and is a key component of our retirement income security advocacy agenda.

AARP has a long history nationally and in the states of advocating for strong retirement income policies. In 2011, AARP state offices in New Hampshire and in North Dakota provided testimony in support of maintaining defined benefit retirement systems for state and local employees. In Hawaii, Michigan and Georgia state offices worked to ensure that retirement income of all retirees was not unfairly taxed, and in Rhode Island our state office engaged in a strenuous campaign to insure that current retirees would not lose their cost-of-living adjustments (COLAs) as the state made significant changes to Employees' Retirement System of Rhode Island (ERSRI).

The basic principles underlying AARP's state level public pension efforts is to ensure that any reforms made to state pensions safeguard the financial security of current and near-retirees, that state and local government employees continue to have access to defined benefit plans, and finally that retirees continue to have access to inflation protection through the provision of cost-of-living adjustments. These principles fit within AARP's national policy agenda, which asserts that we all have a right to be self-reliant and live with dignity in retirement.

AARP believes that all workers need access to a retirement plan that supplements Social Security's foundation. For those employees who do not participate in Social Security, such as New Hampshire's own Group II police and fire personnel, their retirement plan becomes their main source of income during retirement and often their sole source of inflation protection in retirement. AARP believes that New Hampshire's public employees should continue to have access to defined benefit plans, which provide a predictable monthly retirement benefit to employees, operate in a low-fee environment, and offer professional management of retirement assets. Defined benefit plans are also more efficient – that is, they cost less to achieve a particular level of retirement income than defined contribution plans and provide economic support to state and local communities.

While defined contribution plans are valuable to many, and are an important component to overall retirement income security as a supplemental savings vehicle, as primary retirement savings vehicles they force employees to bear most if not all investment risk, inflation risk, and longevity risk, the risk of outliving one's retirement nest egg. The shift of all of these risks to individual employees in concert with other factors could leave many retirees financially unprepared for retirement. For example:

- According to data compiled by the Federal Reserve and analyzed by the Center for Retirement Research at Boston College, the median household headed by a person aged 60 to 62 with a 401(k) account has less than one-quarter of what is needed in that account to maintain its standard of living in retirement.
- The Employee Benefits Research Institute (EBRI), which routinely estimates 401(k) plan asset allocations, account balances and loan activity, estimates in its 2010 analysis that the average 401(k) account balance was $109,723 at year-end 2009 for those who held accounts continuously from year-end 2003 through year-end 2009; further EBRI estimated that the median (or midpoint, half above and half below) 401(k) account balance increased to $59,381 at year-end 2009.
- According to the Current Population Survey, among the 152.6 million Americans who worked in 2010, just 49.2 percent of them had access to either a defined benefit pension plan or a defined contribution retirement account. Of the 75 million workers with access to a plan, 81 percent of them participated, according to the Current Population Survey.[i]
- A sizable percentage of workers have virtually no money in savings and investments. Among workers providing this type of information for EBRI's Retirement Confidence Survey, 56 percent reported that the total value of their household savings and investments (excluding the value of their primary home and any defined benefit plans), is less than $25,000. (See also EBRI October 2011)
    - Current retirees' total savings & investments in 2011 (not including residence or DB plan) breakdown as follows:
        - Less than $1,000: 28%
        - $1,000-$9,999: 14%
        - $10,000-$24,999: 12%

    - $25,000-$49,999: 6%
    - $50,000-$99,999: 11%
    - $100,000-$249,000: 12%
    - $250,000+: 17%
- For a 65 year old male, and account balance of $100,000 will yield an annuity valued at roughly $650 per month.

These facts provide a small snapshot of the lack of retirement readiness that many people face. Limited retirement savings also mean that more and more Americans are living in retirement primarily on Social Security income, so that:

- Today, more than half of all older Americans rely on Social Security for more than 50 percent of their family income; and
- 36.8% of those aged 65 or older have 90% or more of their income coming from Social Security (EBRI's Craig Copeland).

Transitioning to a defined contribution plan raises difficult issues that the Committee should consider. First and foremost, any changes should not harm the funding of the current defined benefit plan or undermine the State's ability to meet the benefit promises it has made to current employees or endanger the retirement income of current retirees.

As the analysis prepared by GRS (Gabriel, Roeder, Smith & Company) for the NHRS shows, closing the current plans to new hires will harm current defined benefit plan participants by lowering the total amount of contributions coming into the plan and it will also force current plan participants into the 414(h) plan under consideration. As a result of closing the defined benefit plan, investments will need to be more liquid and conservative, and likely less diversified, thereby potentially lowering investment returns and increasing necessary contributions by the State, local governments and/or current employees to maintain the funding level of the existing plan. In addition, because these defined benefit plans will still need to be administered for current retirees and employees, the State will continue to incur costs associated with operating both systems for decades to come.

Current and near- retirees do not have the opportunity to pivot their retirement strategy and should not be asked to shoulder the burden of changes to the retirement system. These workers and retirees have spent their lives working hard, paying into the retirement systems and making tough, personal financial decisions so that they could have a retirement income they can count on. Requiring near-term retirees to participate in a 414(h) plan and closing their access to the current defined benefit plan is likely to result in litigation and will undermine the reforms made by the New Hampshire legislature over the last several years to improve the funded status of the NHRS over time.

The impact of contemplated changes to state and local employees who do not receive Social Security is of particular concern to AARP. The lack of a secure source of defined benefit retirement income will mean that these retirees could outlive their retirement savings, and without cost-of-living-adjustments they would have limited or little inflation protection, making it a virtual certainty that the purchasing power of their retirement income will diminish over time. The provision of COLAs as part of a defined benefit plan insures that purchasing power is maintained as retiree's age. Without COLAs, *middle-class* retirees may find themselves struggling to afford even the basics- food, healthcare, prescriptions, housing, and transportation—in their advanced years, as the cost of these basic necessities rise.

The consequences of cutting COLAs are stark not only for retirees, but also for the State's balance sheet. If retiree income remains static while the cost of basic essentials rises, the state could see a dramatic increase in the cost of many social safety net programs. COLAs are a critical component of a state retirement system and, like defined benefit plans, they provide a stabilizing force in an uncertain economy.

In most states, changes to COLAs have been prospective, impacting only new employees. However, as states have recently come to the conclusion that superior cost savings can be achieved by cutting COLA's for *current* retirees, more states have considered the elimination of COLAs for current retirees who have completed the work phases of their lives. These changes are of grave concern to AARP. The lack of inflation protection is a real threat to retirees and the income erosion that results from a significant reduction in COLAs or from the elimination of these benefits is a real threat the economic independence of retirees.

While many have lauded the efforts of the Rhode Island Legislature's recent actions to alter that state's retirement plan, little has been reported on the impact of these changes on current retirees, who bore the brunt of the cuts enacted in 2011. The initial proposed legislation offered by Rhode Island Governor Lincoln D. Chafee and Treasurer Gina M. Raimondo included a projected 19 year freeze on cost-of-living adjustments (COLAs) for *current* retirees and the adoption of a combination plan, which includes a reduced defined benefit plan for current and future workers, and a new mandatory defined contribution plan. The legislation also included other changes to the underlying defined benefit plan, including an increase in the retirement age.

The contemplated "savings" associated with these changes as originally drafted were as follows: slashing the COLA - 70% of the estimated savings, raising the retirement age - 20%, and savings associated with all other changes, including the combination plan - 10%. Efforts by our state office to ascertain from state legislators the precise amount of "savings" contemplated to be achieved by the combination plan went unanswered throughout the debate on the legislation. The original proposal would have reduced anticipated retirement income of the average employee over the 19 year period by close to 50%. Proponents of the measure claimed that this was not a benefit cut, but let me put it in simpler, more understandable terms—middle class seniors who are currently able to buy four bags of groceries with their public pension income today would in time be able to afford only two bags of groceries under the bill as introduced. Cutting COLAs is akin to slashing retirement income that has been *earned*. Again, these current retirees have limited means to pivot their retirement income and over time will see their buying power diminish.

In closing, I would like to emphasize that while New Hampshire's pension debate is complicated by a multitude of numbers and statistics—public pension reform is really about people—retirees , workers, their families, taxpayers and communities. We hope that as you consider additional changes to the NHRS that the retirement income security of system participants remains a key consideration. As we have seen retirement income security diminish for private sector workers, States as employers have continued to play an important role in the maintenance of retirement systems that provide a significant source of retirement income through shared funding mechanisms that allow retirees, including many of our members, to be self-reliant and live with dignity in retirement. AARP hopes and trusts that as New Hampshire legislators undertake their work on revisions to the NHRS, they will continue to maintain and preserve these important values.

Respectfully submitted,

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[i] EBRI October 2011 Issue Brief: http://www.ebri.org/pdf/briefspdf/EBRI_IB_10-2011_No363_Ret_Part.pdf)