# The Truth about the Wisconsin Retirement System

For decades, the Wisconsin Retirement System (WRS) has provided benefits for state agencies and local employers to use in attracting and retaining employees needed to fulfill critical government duties. The system covers state and local public employees, including the University of Wisconsin System, local police and firefighters, and all public school teachers in the state. Those not included are employees of the City of Milwaukee and Milwaukee County, who are covered under separate retirement systems. While the WRS has existed since 1982, pension coverage for local government employees has been in place since 1891, when the legislature required Milwaukee to create a pension fund for retired and disabled police and firefighters. Since that date, the legislature has extended pension coverage to other public employees, along with creating group life and health insurance programs (Fiscal Year (FY) 2009 Comprehensive Annual Financial Report (CAFR), p. 2). Today the System covers over 72,000 active state employees and 195,000 local employees. These workers provide a wide range of services and support for Wisconsin residents, performing jobs ranging from snow plow operator to social worker. In FY 2009 the average annual pay for all members of the System was $43,107. For General members, average pay was $35,722 (FY 2009 CAFR, p. 90).

## The System Efficiently Provides Career Employees with Modest, but Meaningful, Benefits

The WRS provides pension benefits to over 150,000 retired state and local employees and their beneficiaries. The average annual pension for a WRS member is $24,488 (this includes all employee classes as well as core and variable plan members) (FY 2009 CAFR, p. 4). Employees who retire at or after age 65 (54 for protective occupations and 62 for elected officials and executive service retirement plan participants) are eligible for a retirement benefit based on a formula factor, their final average earnings, and creditable service. Vested participants may retire at or after age 55 (50 for protective occupations) and receive an actuarially-reduced benefit. Earlier retirement ages are consistent with other public sector plans, and are sound policy because many public employees hold physically or emotionally demanding positions in which they are directly responsible for safety and health in the communities they serve. Participants contribute five percent of each paycheck to the System. In many cases, employees have negotiated with the employer to "pick-up" that contribution in exchange for employees foregoing pay raises.

As part of the formula used in calculating benefits, pension plans use a service credit multiplier. For general members WRS benefits are based on a service credit multiplier of 1.6 percent per year of service; significantly below the national average of 1.95 percent for public plans and much less than the multiplier used for other categories of WRS members. General member benefits are also capped at 70 percent of an employee's final average salary. To illustrate, the benefit for a hypothetical 25-year employee with a final average salary of $40,000 would be calculated in the following manner:

**$40,000 *x* 25 years of service *x* service credit multiplier of 1.6 percent = $16,000**

Most public pension plans provide retirees with cost-of-living adjustments to protect the purchasing power of annuities against inflation. Unlike most plans, however, WRS retirees whose annuities are paid from the "core" fund receive annual cost-of-living adjustments tied to whether reserve surpluses are sufficient to generate an increase. In addition, the annual adjustment may result in a benefit reduction if losses are severe (although the benefit may not fall below the initial annuity upon retirement). Annuitants with core fund annuities saw their benefit decrease by 2.1 percent in 2009, see (FY 2009 CAFR, p. 4).

Because participating employers can calculate each employee's benefit, employers can efficiently manage the workforce. On the other hand, 401(k) plan participants may invest too little, or their investments may provide insufficient returns, thus preventing employees from retiring. A recent calculation done by the Center for Retirement Research for Retirement USA shows that the real retirement crisis in our country is the $6.6 trillion gap between current savings and what Americans should have today to maintain their standards of living in retirement (The Retirement Income Deficit, Retirement USA, October 2010). As a result, millions of U.S. workers have already delayed, or are likely to delay, their retirement dates. This can complicate the employer's role, forcing decisions with unpleasant consequences for everyone. Even for those employees who have accrued what they believe may be sufficient savings, there is often little incentive to retire.

Defined benefit plans have access to professional investment managers who are trained in developing ongoing, long-term investment strategies that include an optimum mix of growth potential and risk. Participants and taxpayers benefit from the favorable investment performance of pooled pension fund assets, as well as fees and expenses that are significantly lower than those of defined contribution savings plans. The wide range of investment options open to large pension plans, such as foreign and domestic stocks and bonds and venture capital, also improve investment returns. Furthermore, WRS investments are not affected by the retirement timing of a particular employee so the investment horizon never has to be shortened.

Plan investments not only help keep costs down for plan sponsors, but are also a critical part of the economic fabric of the state. According to the National Institute on Retirement Security, each dollar in taxpayer contributions to Wisconsin's state and local pension plans supports $7.47 in long-term economic activity in the state. Retiree expenditures stemming from state and local pension plan benefits support nearly 33,000 jobs in Wisconsin. These figures reflect the fact that taxpayer contributions are, in the long run, a highly efficient source of financing for retirement benefits that ultimately provide income and jobs for others (Pensionomics: Measuring the Economic Impact of State and Local Pension Plans, National Institute on Retirement Security, February 2009).

## WRS is Financially Sound

There have been some recent claims that retirement systems covering public employees are facing a financial crisis. These claims are rarely true, and they are not true of the Wisconsin Retirement System. In fact, according to a recent study from the Pew Center on the States, "Wisconsin is a national leader in managing its long-term liabilities for both pensions and retiree health care and other benefits. It has funded nearly 100 percent of its total pension bill – well beyond the 80 percent benchmark that the U.S. Government Accountability Office says is preferred by experts – by consistently meeting its actuarially required contributions," *The Trillion Dollar Gap: Underfunded State Retirement Systems and the Roads to Reform, Pew Center on the States, February 2010.*

As of December 31, 2009, the System held pension assets with an actuarial value of $78.9 billion and had accrued liabilities of $79.1 billion (FY 2009 CAFR, p. 66). In other words, WRS already has 99.8 of the money it will need to pay accrued pension benefits in upcoming years. (Recent surveys show that the average funding level for large public sector plans is in the range of 70 to 75 percent). This ratio of assets to liabilities is simply a snapshot that captures a plan sponsor's ongoing effort at one point in time to fund its pension obligation; any unfunded liabilities can be made up over many years. If the plan sponsor is consistently making its annual required contribution, its pension plan can have a funded ratio below 100 percent yet still be on track toward full actuarial funding.

Plan actuaries project that over the long term the System will earn an average of 7.8 percent each year on its investments. In some years returns will be below that rate and in others returns will exceed it. When returns are strong and above the actuarial assumed rate, the employer's level of contributions will generally be lower than when investment returns lag the actuarially assumed rate. When returns are less than projected, those actuarial losses are amortized through increased employer contributions. Current funding of defined benefit plans reduces long-term costs through the compounding of contributions and investment earnings. To a large extent investment earnings will dictate the level of contributions needed to keep a plan funded at a healthy level because those returns provide the bulk of revenues. Since 1995, investment returns have provided nearly $60 billion, or three-fourths of total revenues, for WRS.

**WRS Revenues by Source, 1995 - 2009**

| Year | Employee Contributions | Employer Contributions | Investment Income/(Loss) | Other Income | Total Revenue/(Loss) |
|---|---|---|---|---|---|
| 1995 | $388,642,000 | $591,796,000 | $6,846,397,000 | $113,000 | $7,826,948,000 |
| 1996 | 405,857,000 | 663,265,000 | 5,414,556,000 | 160,000 | 6,483,839,000 |
| 1997 | 416,989,000 | 660,812,000 | 7,241,025,000 | 179,000 | 8,319,004,000 |
| 1998 | 437,097,000 | 654,664,000 | 7,037,489,000 | 231,000 | 8,129,480,000 |
| 1999 | 449,065,000 | 721,626,000 | 9,235,371,000 | 205,000 | 10,406,268,000 |
| 2000 | 511,661,000 | 547,515,000 | (1,033,753,000) | 184,000 | 25,607,000 |
| 2001 | 506,712,000 | 631,052,000 | (1,985,961,000) | 211,000 | (847,987,000) |
| 2002 | 526,149,000 | 914,575,000 | (5,880,598,000) | 4,082,000 | (4,435,793,000) |
| 2003 | 564,754,000 | 1,737,816,000 | 12,043,429,000 | 3,563,000 | 14,349,563,000 |
| 2004 | 605,184,000 | 644,649,000 | 7,512,872,000 | 3,082,000 | 8,765,787,000 |
| 2005 | 640,229,000 | 605,163,000 | 5,492,548,000 | 2,338,000 | 6,740,278,000 |
| 2006 | 670,254,000 | 617,263,000 | 10,962,280,000 | 1,905,000 | 12,251,702,000 |
| 2007 | 705,804,000 | 655,128,000 | 6,495,914,000 | 1,823,000 | 7,858,669,000 |
| 2008 | 736,149,000 | 683,520,000 | (22,744,110,000) | 1,618,000 | (21,322,822,000) |
| 2009 | 736,689,000 | 705,997,000 | 13,024,986,000 | 1,117,000 | 14,468,790,000 |
| ***Total*** | ***8,301,235,000*** | ***11,034,841,000*** | ***59,662,445,000*** | ***20,811,000*** | ***79,019,332,000*** |

*Source: Annual Financial Reports, FYs 2001 - 2009*

It should come as no surprise that the 2008 market downturn adversely impacted all investors. What is surprising is that some individuals fail to account for the fact that defined benefit plan funding is structured to be carried out indefinitely. WRS is designed for the long haul and does not have an investment horizon like defined contribution plans that cover individual employees. As a prime example, investors who stayed the course enjoyed returns well in excess of projected levels in 2009. Like most public sector plans, WRS uses a smoothing method to help avoid wild swings in required contribution levels, so these strong returns will help reduce deferred investment losses from 2008. State and local government employer pension costs for all public pension plans in Wisconsin amounted to just 1.35 percent of all state and local government spending in 2008 (Issue Brief: State and Local Government Spending on Public Employee Retirement Systems, National Association of State Retirement Administrators, January 2011).

## Other Post-Employment Benefits

Certain long-term employees are eligible for retiree health care benefits through WRS. For many years employers have been contributing substantially toward WRS' retiree health care program to "pre-fund" those benefits. According to the Pew Center on the States, "Wisconsin has a relatively limited long-term liability of $2.2 billion for retiree health care and other benefits. It has set aside $536.8 million to cover that bill coming due." This is extremely important, as most public employers in the U.S. have set aside little, if any, money to pre-fund retiree health care programs. The vast majority continue to pay retiree health care costs on a pay-as-you-go basis. Employers providing retiree health care benefits can cut their long-term costs substantially by pre-funding those obligations: contributions can be invested like assets in a pension plan and investment returns then provide the bulk of revenues used to pay premiums and other costs.

AFSCME believes in a society of opportunity where all workers not only earn a living wage, but can afford to see a doctor when they are sick. AFSCME believes we all should have the opportunity to reach our full potential in our chosen careers and to retire with dignity when our work is done. For decades, WRS has provided workers and their beneficiaries with secure retirement benefits. There is no reason to believe it will not continue to be able to do so.