

December 2010

## Boston Weathers Pension Funding Crisis

*Planned perfect storm comes together to avert significant cost increase in FY12*

The Menino Administration, working closely with the State-Boston Retirement Board (SBRB), has successfully averted a significant increase in its pension appropriation starting in FY12. A series of actions taken over the past few years came together to mitigate what could have been a budget increase of over \$47M or 35% in a year in which Boston will face state aid cuts for the fourth consecutive year, the loss of ARRA federal stimulus funds and escalating health insurance cost increases. Instead, next year's pension expenses will increase by approximately \$21.4M or 16.2%.

The SBRB originally had adopted a schedule to fully fund its pension liability by 2028 but has been more aggressive than required under Massachusetts state law and the system was scheduled to reach full funding in 2023.

However, the volatile investment market in 2008 resulted in retirement systems across Massachusetts and the nation posting significant investment losses. The composite return in 2008 for all 106 Massachusetts retirement systems was -28.6% and Boston's loss was -24.2%. With the City's pension cost projections based on annual investment returns of 8%, this loss was projected by the Research Bureau in a May 2010 report to require the City's pension appropriation in FY12 to increase by as much as \$70M if no other changes occurred.

The Commonwealth had been directly funding teacher pensions on an actuarial basis for all municipalities except Boston which was reimbursed by the state for actual pension

expenses of the prior year. Prior to 2008, the City and Commonwealth had begun discussions about shifting the management of teacher pension assets to the state PRIT fund and for the state to pay Boston's teacher pensions consistent with other municipalities.

Two main factors were combined at this time to enable the City to mitigate what would have been a significant increase in its pension appropriation in FY12. They are:

- Legislation enacted in 2010 required the state to fund Boston teacher pensions on an "actuarial" rather than "pension payroll reimbursement" basis with the last reimbursement of \$126.9M applied to reduce Boston's pension liability
- Reserves totaling \$82M that had been previously established to address pension liability issues were applied now

The application of these funds to reduce the City's pension liability enabled the SBRB to approve a new funding schedule as of July 1, 2010 as part of an updated actuarial valuation that extended the schedule to reach full funding by only two years to 2025. Recent legislation had allowed municipalities to extend schedules as far as 2040. Reaching full funding by 2025 in light of the 24.2% asset loss in 2008 is a significant achievement that will have long-term financial benefits for the City. The State-Boston Retirement System's non-teacher unfunded pension liability as of July 1, 2010 is estimated at \$1.3B.