



333 Washington Street, Suite 854, Boston, MA 02108
T(617)227-1900 F(617)227-2815 www.bmr.org

Testimony of the Boston Municipal Research Bureau
Before the
Boston City Council's Committee on Government Operations

July 31, 2017

Regarding: Docket #1002 – Order approving an increase in the cost-of-living adjustment (COLA) base from \$13,000 to \$14,000 for all retirees and beneficiaries of the Boston Retirement System

Mr. Chairman and Members, my name is Samuel R. Tyler, President of the Boston Municipal Research Bureau, and I am here to oppose the City increasing the COLA base to \$14,000. However, we do support the 3% annual COLA in fiscal 2018 based on the \$13,000 base. Raising the COLA base to \$14,000 will increase the City's pension liability by \$25.4 million according to estimates from the Retirement Board's actuarial firm, Segal Consulting. With the City's pension liability only funded at 69.4% based on the market valuation as of January 1, 2016, now is not the time to increase the pension liability unnecessarily. Increasing the liability moves the City in the wrong direction.

The Boston Retirement System (BRS) is on schedule to reach full funding of the unfunded pension liability of \$1.5 billion by 2025, less than eight years from now. The Research Bureau believes that any policy decision should prioritize maintaining this funding schedule. The Bureau's recommendation is based on the importance of maintaining the 2025 funding schedule, concern about recent annual BRS investment returns, the trend of negative net Cherry Sheet state aid for Boston and the uncertainty of federal funding.

COLA Base Increase

The Research Bureau opposes the increase in the COLA base to \$14,000 because it would increase the City's total unfunded liability by \$25.4 million. The annual COLA would be based on 3% of the first \$14,000 of a retiree's or beneficiary's pension. The Research Bureau is very concerned about the City of Boston's sizeable long-term unfunded pension and retiree health insurance liabilities and their growing cost implications for future city services. Based on the current actuarial valuation and review report for the Boston Retirement System as of January 1, 2016, Boston's annual pension appropriation will increase from \$221.2 million in fiscal 2018 to an estimated \$393.8 million in fiscal 2025 as it reaches full funding, a total increase of \$172.6 million or 78% over seven years.

The City's pension funding schedule is very aggressive, but it should be manageable as long as the total liability is not further increased unnecessarily. The City's pension appropriation increased by 11.0% in fiscal 2018, far greater than the City's total General Fund budget increase of 4.9% this year. In the Mayor's resubmittal budget approved by the City Council, the pension appropriation increased by \$3.0 million in anticipation of the increase in the COLA base to \$14,000. That \$3.0 million could have supported other important city services.

Other factors that led the Research Bureau to make this recommendation include the following:

- The aggregate investment market return over the four years from 2013 to 2017 was 6.28% which is below the assumed annual rate of return of 7.75%.
- In a December 2014 Special Report on the BRS and Board operations, the Research Bureau recommended that the BRS and City not approve a COLA base increase until the BRS reached a funded ratio of 80%. Several states have adopted a policy that no COLA increase, annual or otherwise, would be approved until the pension system reached the 80% funded ratio. As of January 1, 2016, the BRS's funded ratio based on market valuation was 69.4%.
- The Commonwealth's defined benefit pension system is very generous by today's standards in light of changes in private sector pension benefits to reduce future liabilities. Several states are moving to defined contribution plans for new members to control pension costs. Also, Boston retirees enjoy very favorable health insurance benefits during retirement.

3% COLA Increase

Since an annual 3.0% COLA increase on the \$13,000 base is calculated into the existing funding schedule, the Research Bureau does support the 3.0% COLA increase for fiscal 2018.

Conclusion

The COLA impact on the City's pension liability must be considered in conjunction with financial demands of departmental services and the looming cost of the retiree health insurance liability (OPEB) of \$2.26 billion as of June 30, 2015. Reaching full funding of the pension liability in 2025 would enable the City in fiscal 2026 to allocate a portion of the resources previously used to fund the annual amortized pension liability to the pension fund to help maintain full funding. The balance of the available funds could be allocated to address the OPEB liability at a higher level going forward.

The Research Bureau believes that with the fiscal uncertainties ahead, both at the state and federal levels, increasing the COLA base is not fiscally prudent at this time and should not be approved by the Boston City Council. The City's annual pension appropriation increases are already aggressive and increasing the pension liability by \$25.4 million moves the City in the wrong direction.