

# **Population Aging and State Pensions in New England**

NEPPC Research Report 10-1

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# Financial Pressure on Pension Plans

- Baby boom generation aging into 60s.
- Life expectancy at age 62 is 19 years for men and 22 years for women.
- Historic underfunding.
- Financial market declines.
- Economic pressure on government budgets.

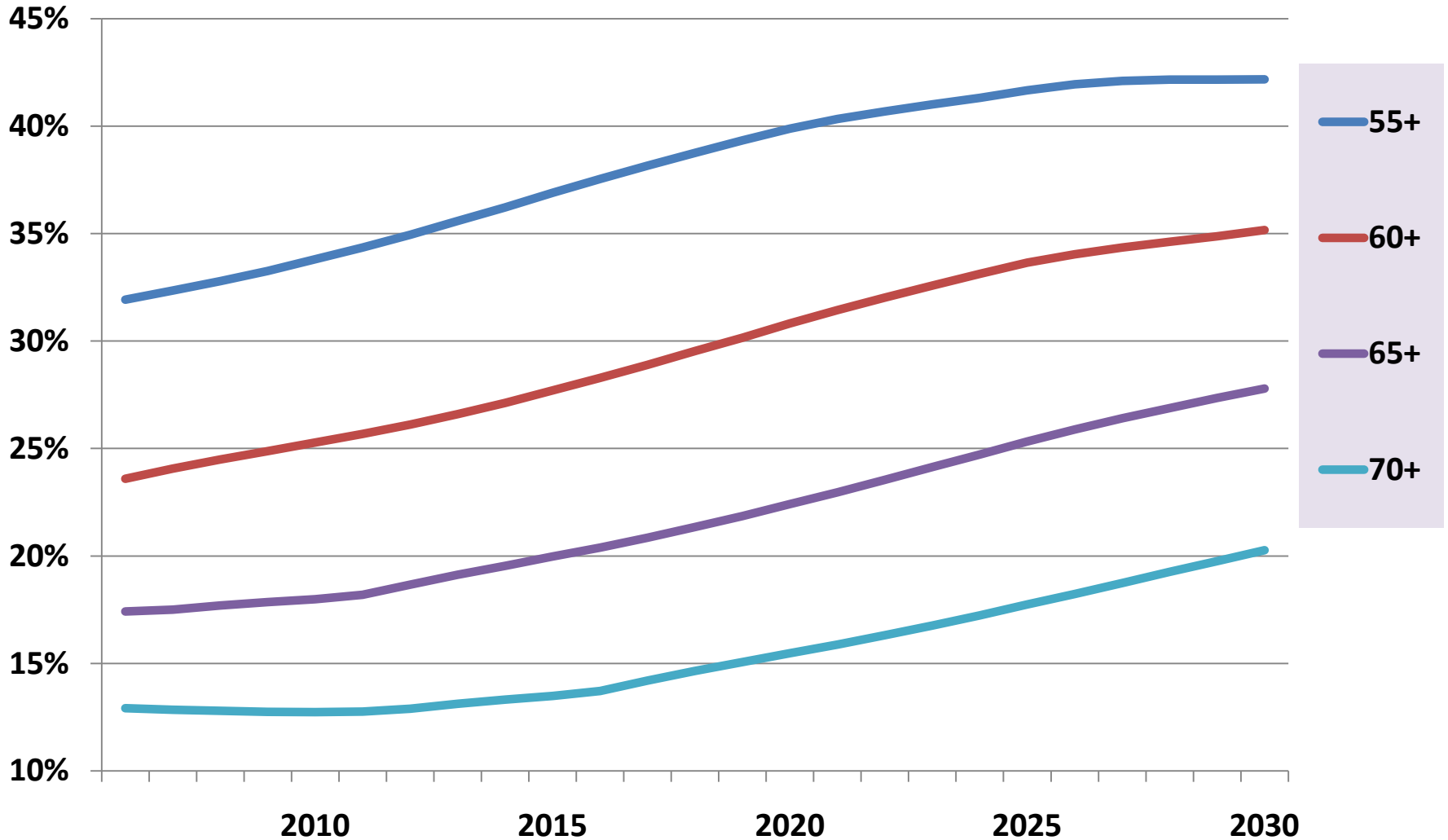
# Outline of Study

- Demographic trends
- Defined-benefit pension plans
- Comparing pensions in New England states
- Labor market incentives
- Pension reform

# Caveats

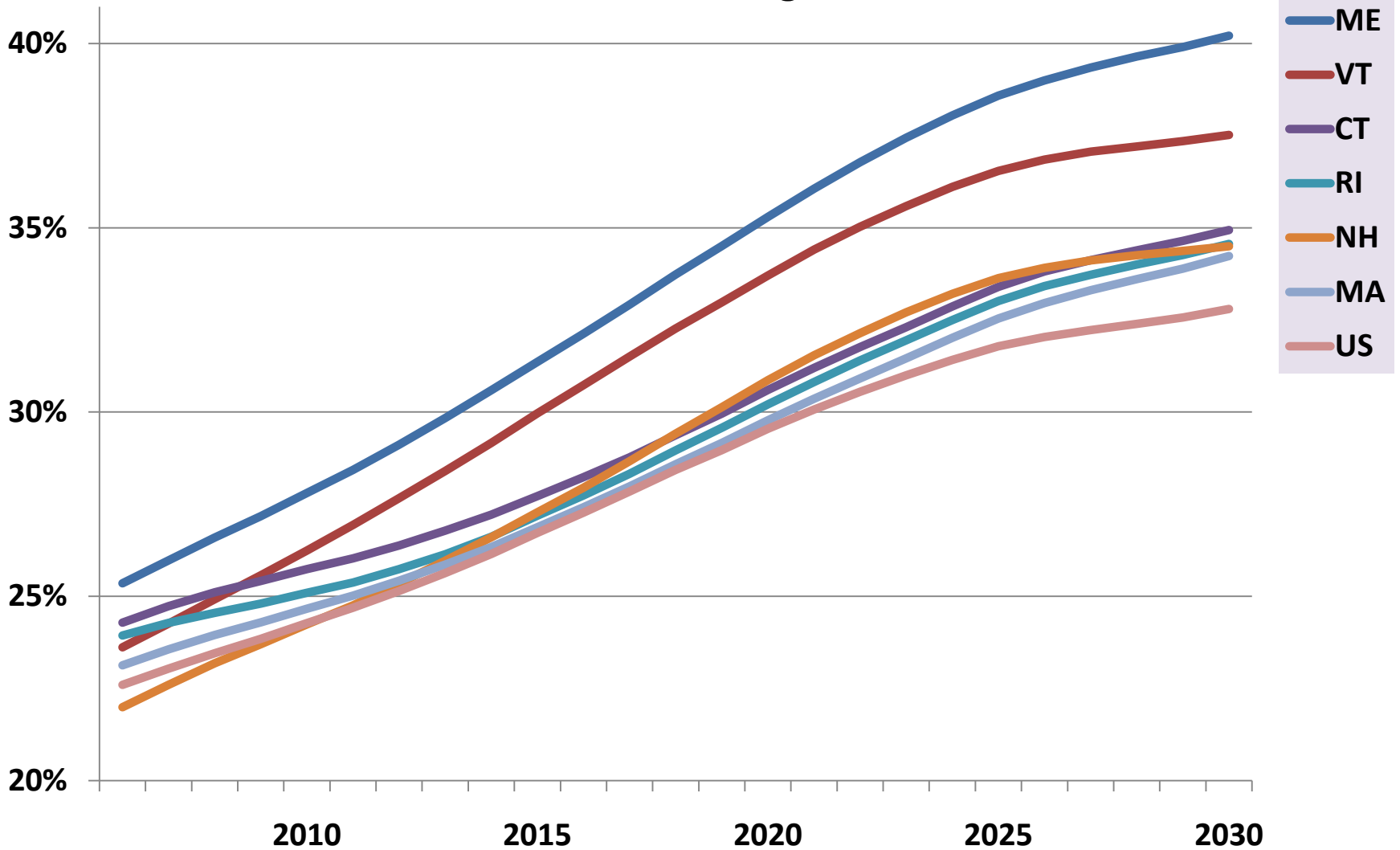
- My focus is the age structure of the pension plans, not their funding status.
- My focus is general plan for new employees, not grandfathered plans or job-specific plans.
- Includes reforms through the 2009 legislative sessions only.

**Figure 1**  
**Projected Percent of Adult Population at Older Ages**  
**All New England States**



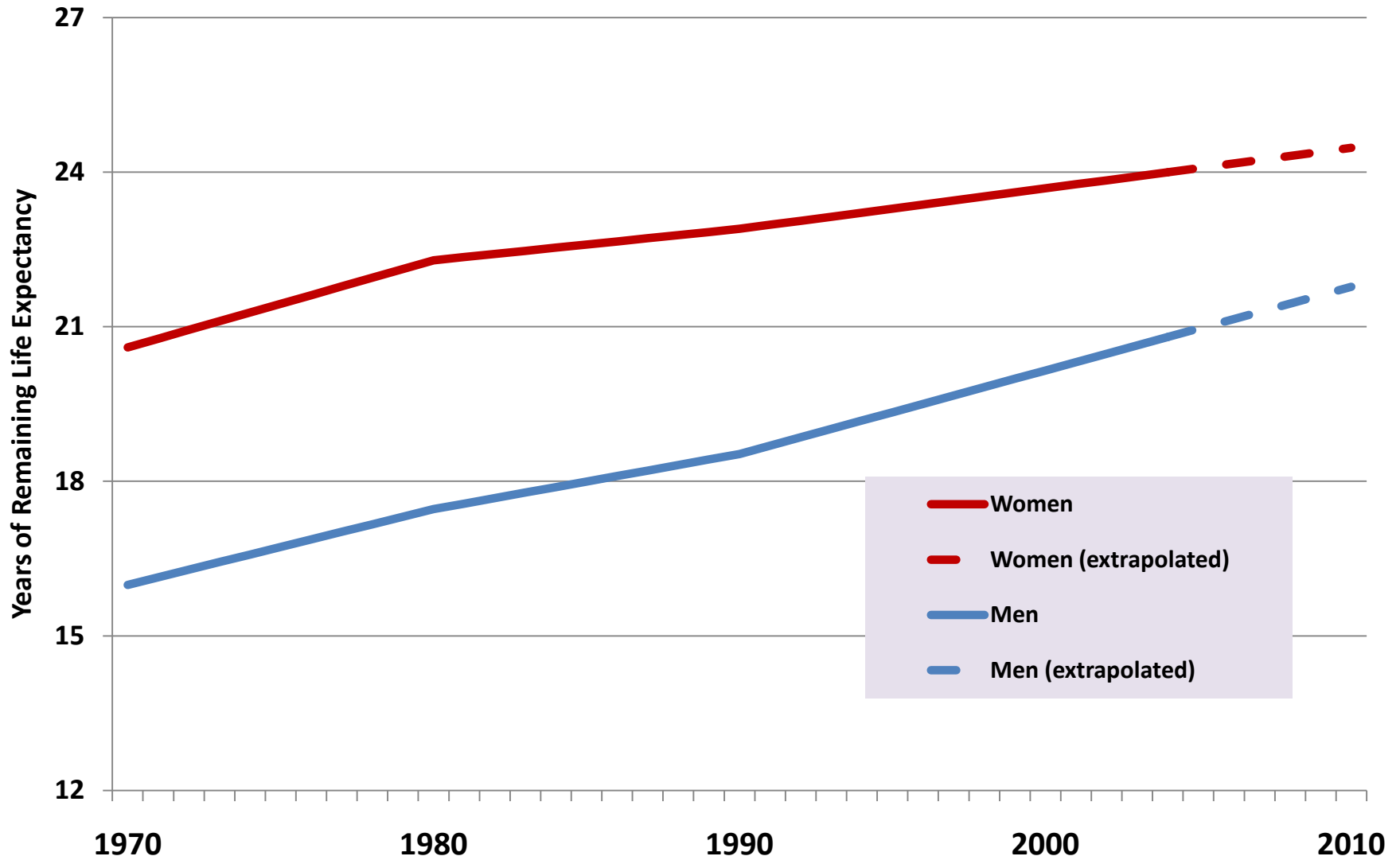
Source: Author's calculations based on U.S. Census Bureau data

**Figure 2**  
**Projected Percent of Adult Population Over Age 60**  
**Individual New England States**



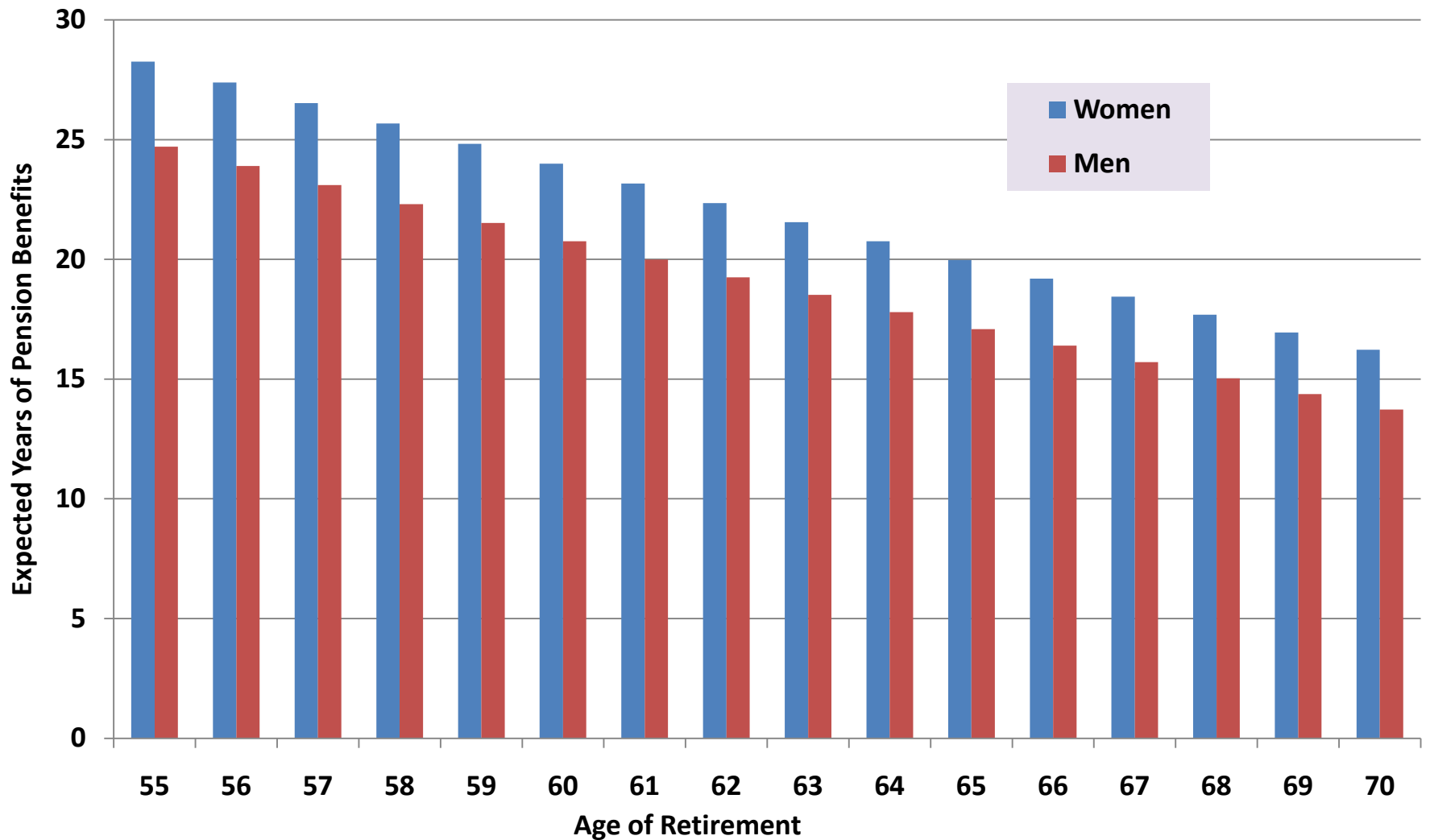
Source: Author's calculations based on U.S. Census Bureau data.

**Figure 3**  
**Years of Remaining Life Expectancy at Age 60 in the United States**



Source: National Center for Health Statistics (2007, table 11), extrapolations by author.

**Figure 4**  
**Expected Number of Years of Pension Benefits**  
**Based on Retirement Age (2004)**



Source: National Center for Health Statistics (2007, tables 2 and 3), Life expectancy by age.



# Defined-Benefit Pension Plans

- DB versus DC plans
- Example of DB plan
  - Maine’s retirement pension is 2% of “final average salary” per year of service, inflation-adjusted annually, beginning at age 62.
  - Early retirement allowed after 25 years of service with pension reduced 6% for each year before age 62.

# Variation in Details

- Social Security opt-out
- Vesting
- “Full” benefit formula
- Normal retirement
- Early retirement
- Age-related benefit adjustments
- Benefit limits
- Employee contribution
- Inflation adjustment

# Variation in Details (other)

- Definition of final salary base
- Limits to final salary base
- Opportunities for supplementary service credits
- Treatment of part-time or overtime work
- Survivorship options
- Minimum guarantees

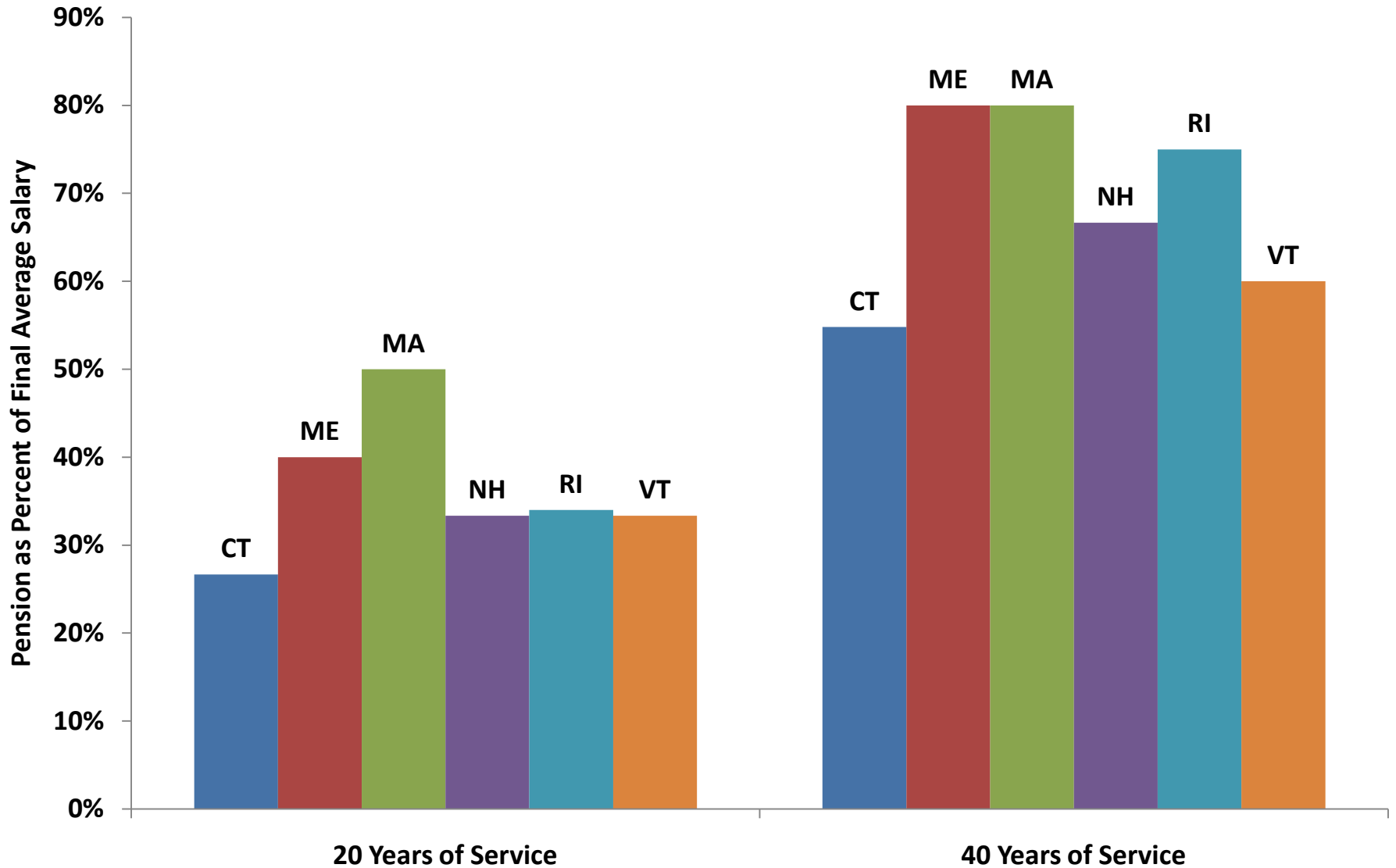
# Social Security Opt-Out

- Employees in Connecticut, New Hampshire, Rhode Island and Vermont participate in both Social Security and the state pension plan.
- Employees in Maine and Massachusetts participate in the state pension system only.

# Full Benefit Amount Per Year of Service

CT	1.333 percent of salary up to “breakpoint” level (\$51,700 in 2009), 1.833 percent of salary above “breakpoint” level, 1.625 percent of salary for years of service above 35	
ME	2 percent of salary	
MA	2.5 percent of salary (max 80%)	
NH	1.667 percent of salary before age 65, 1.515 percent of salary at age 65 and older	
RI	1.6 percent for years 1–10 1.8 percent for years 11–20 2.0 percent for years 21–25	2.25 percent for years 26-30 2.5 percent for years 31-37 2.25% for year 38 (max 75%)
VT	1.667 percent of salary (max 60%)	

**Figure 5**  
**Full Pension Benefit as Percent of Final Average Salary**



Source: Author's calculations based on descriptions of benefit plans in state publications.

# Eligibility for Full Pension

CT	Age 60 with 25+ years of service, age 62 with fewer than 25 years of service
ME	Age 62
MA	Age 65
NH	Age 60
RI	Age 62 with 29+ years of service, age 65 with fewer than 29 years of service
VT	When sum of age and years of service is 87, or age 65

# Eligibility for Reduced Pension

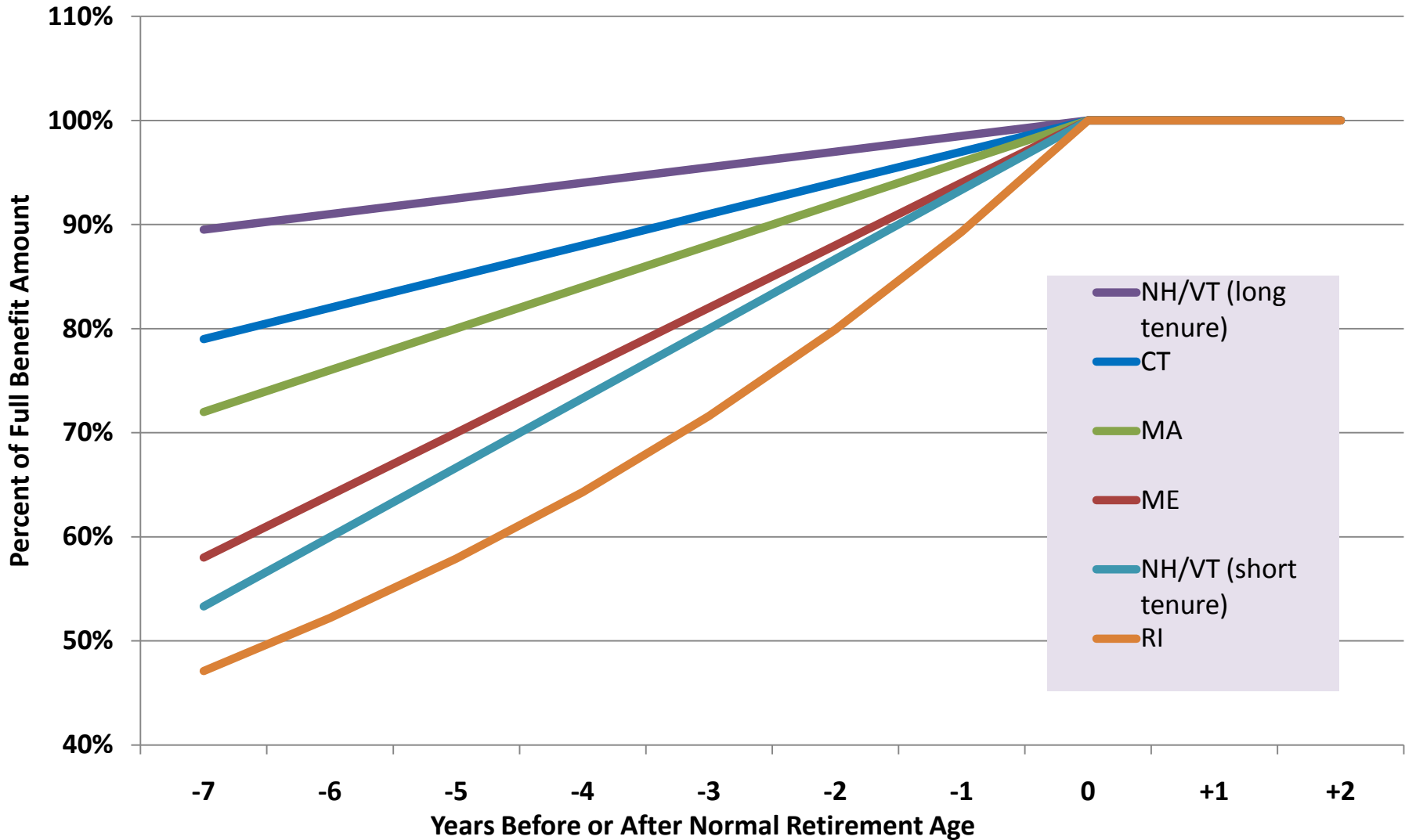
CT	Age 55 with 10 years of service
ME	25 years of service
MA	20 years of service, or age 55 with 10 years of service
NH	Age 50 with 10 years of service; or any age with 20 years of service, and if sum of age and years of service is at least 70
RI	Age 55 with 20 years of service
VT	Age 55 with 5 years of service



# Benefit Reduction for Early Retirement

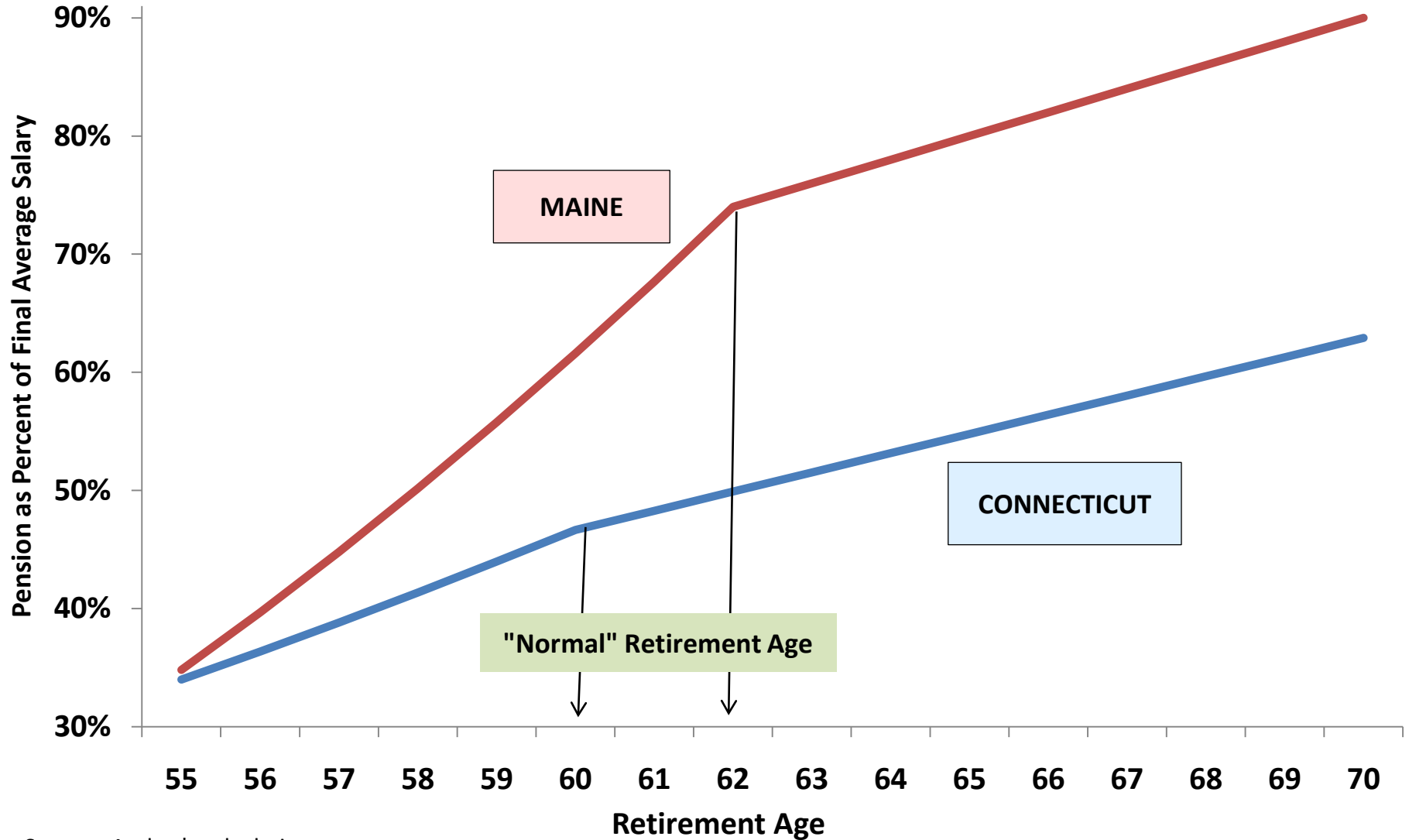
CT	If 25+ years of service, 3 percent per year before age 60 If <25 years of service, 3 percent per year before age 62
ME	6 percent per year before age 62
MA	4 percent per year before age 65 (see footnote 8)
NH (VT)	1.5 percent per year before age 60 (65) if 35+ years of service 6.67 percent per year before age 60 (65) if less than 20 years (VT: No reduction if age plus years of service is 87+)
RI	No reduction if age 62 with 29+ years of service, Otherwise actuarial reduction (eg. age 64 – 89%, age 62 – 72%, age 60 – 58%, age 55 – 35%)

**Figure 6**  
**Benefit Adjustments for Retiring Before/After "Normal" Age**



Source: Author's calculations based on descriptions of benefit plans in state publications.

**Figure 7**  
**Pension as Percent of Final Average Salary, by Retirement Age**  
**for Employee Hired at Age 25 in Maine, Connecticut**

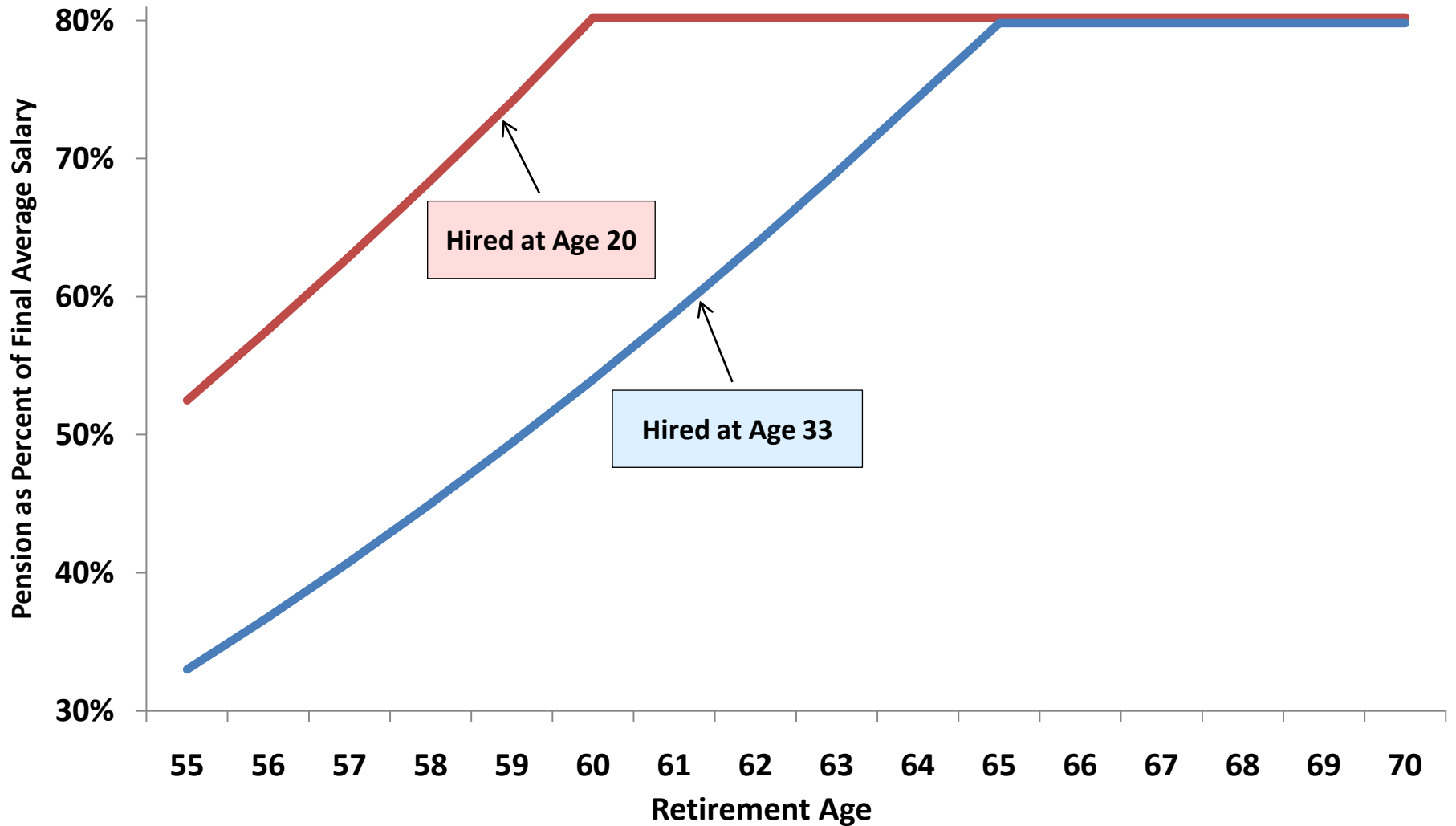


Source: Author's calculations

# Maximum Benefit

- 60% of salary in Vermont
- 75% of salary in Rhode Island
- 80% of salary in Massachusetts
- No limit in Connecticut, Maine or New Hampshire

**Figure 8**  
**Pension as Percent of Final Average Salary, by Retirement Age**  
**for Massachusetts Employee Hired at Age 20, 33**

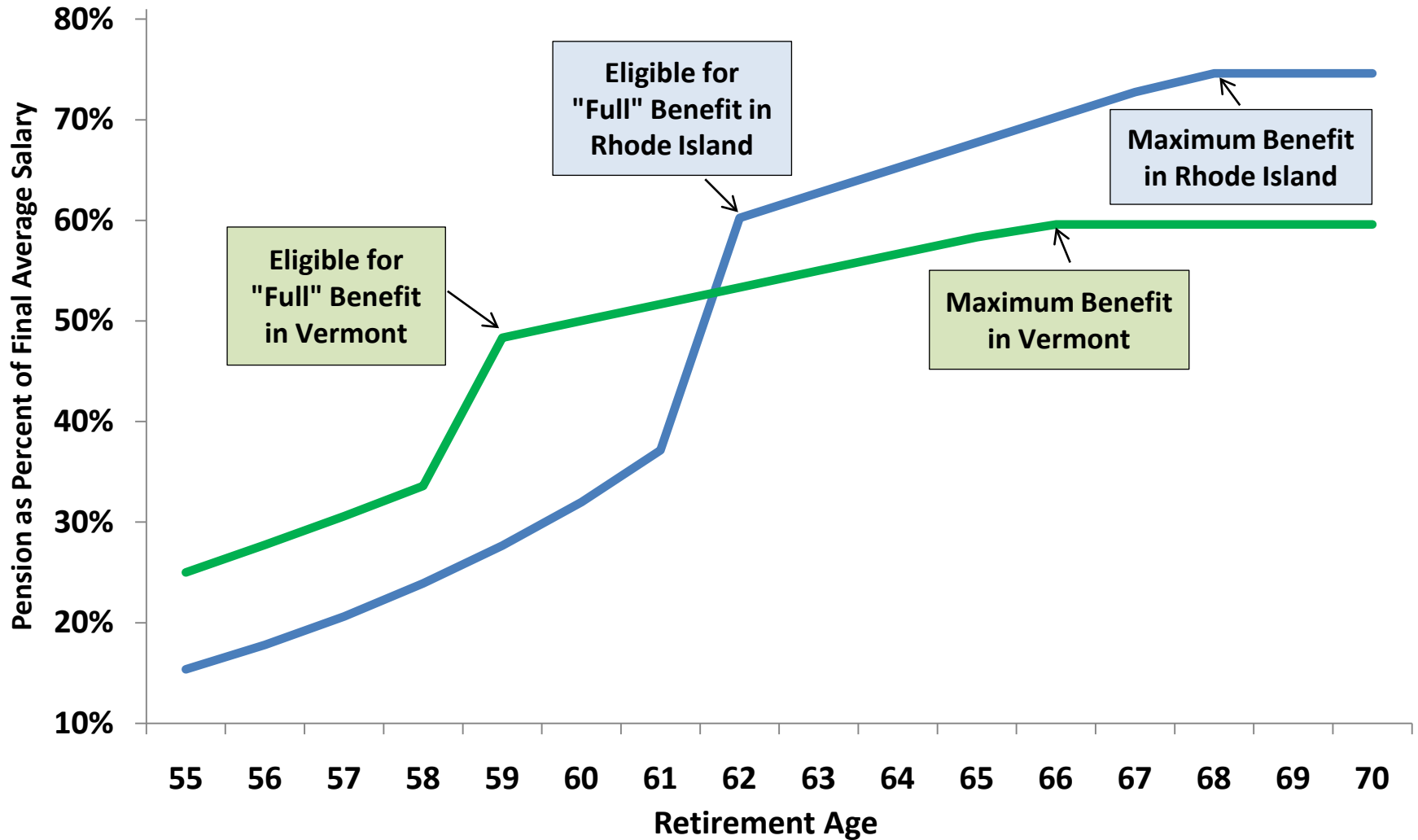


Source: Author's calculations

# Special Rules for Full Benefits

- Connecticut: Full benefits at age 60 with 25 years of service, otherwise age 62.
- Rhode Island: Full benefits at age 62 with 29 years of service, otherwise age 65.
- Vermont: Full benefits when sum of age and service tenure is 87, otherwise age 65.

**Figure 9**  
**Pension as Percent of Final Average Salary, by Retirement Age**  
**for Employee Hired at Age 30 in Rhode Island, Vermont**



Source: Author's calculations

# Pension Reform: Issues & Options

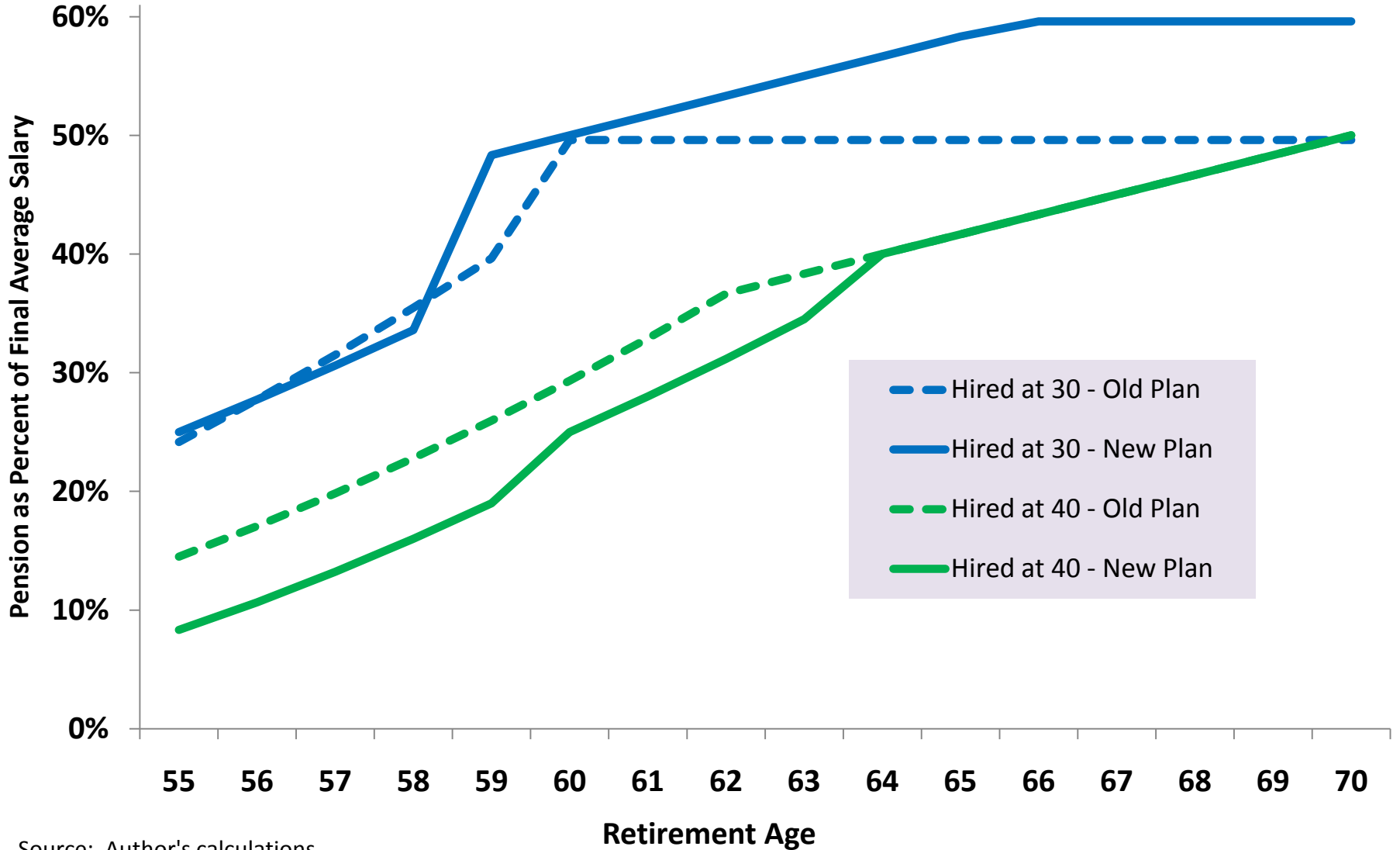
- Vested employees versus new employees.
- Raising statutory retirement ages to reflect increased longevity.
  - Social Security phasing back to age 67.
  - Indexing retirement age to life expectancy.
- Age neutrality for early retirement.
- Age neutrality for later retirement.
- DB plan versus Social Security and DC plan.
  - Many private sector employers have phased out traditional DB pension benefits.



# 2008 Vermont Reforms

- Normal retirement age changed from age 62 or 30 years of service to age 65, or when the sum of age and years of service reaches 87.
- Maximum benefit increased from 50 to 60 percent of salary.
- Early retirement more attractive for long-service employee; less attractive for short-service employees.

**Figure 10**  
**Effect of 2008 Reform on Benefit Structure in Vermont**

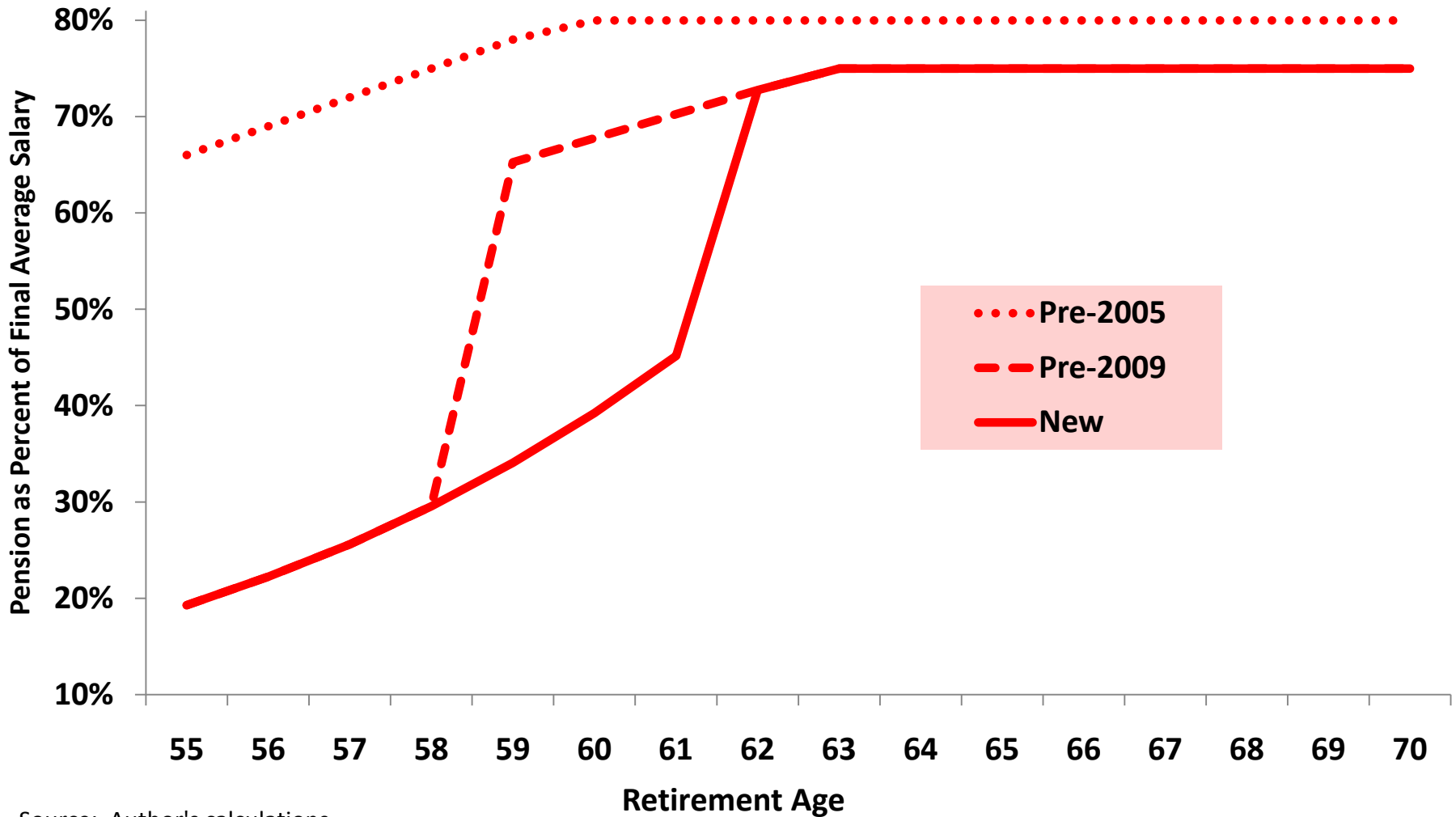


Source: Author's calculations

# 2005/2009 Pension Reform in Rhode Island

- Pre-2005: Full benefit eligibility after 28 years of service, otherwise age 60.
- 2005 Reform: Full benefit eligibility at age 59 with 29 years of service, otherwise age 65.
- 2009 Reform: Full benefit eligibility at age 62 with 29 years of service, otherwise age 65.

**Figure 11**  
**Effect of 2005/2009 Reforms on Benefits in Rhode Island**  
**for Employee Hired at Age 25**



Source: Author's calculations

# 2009 Pension Reform in Massachusetts

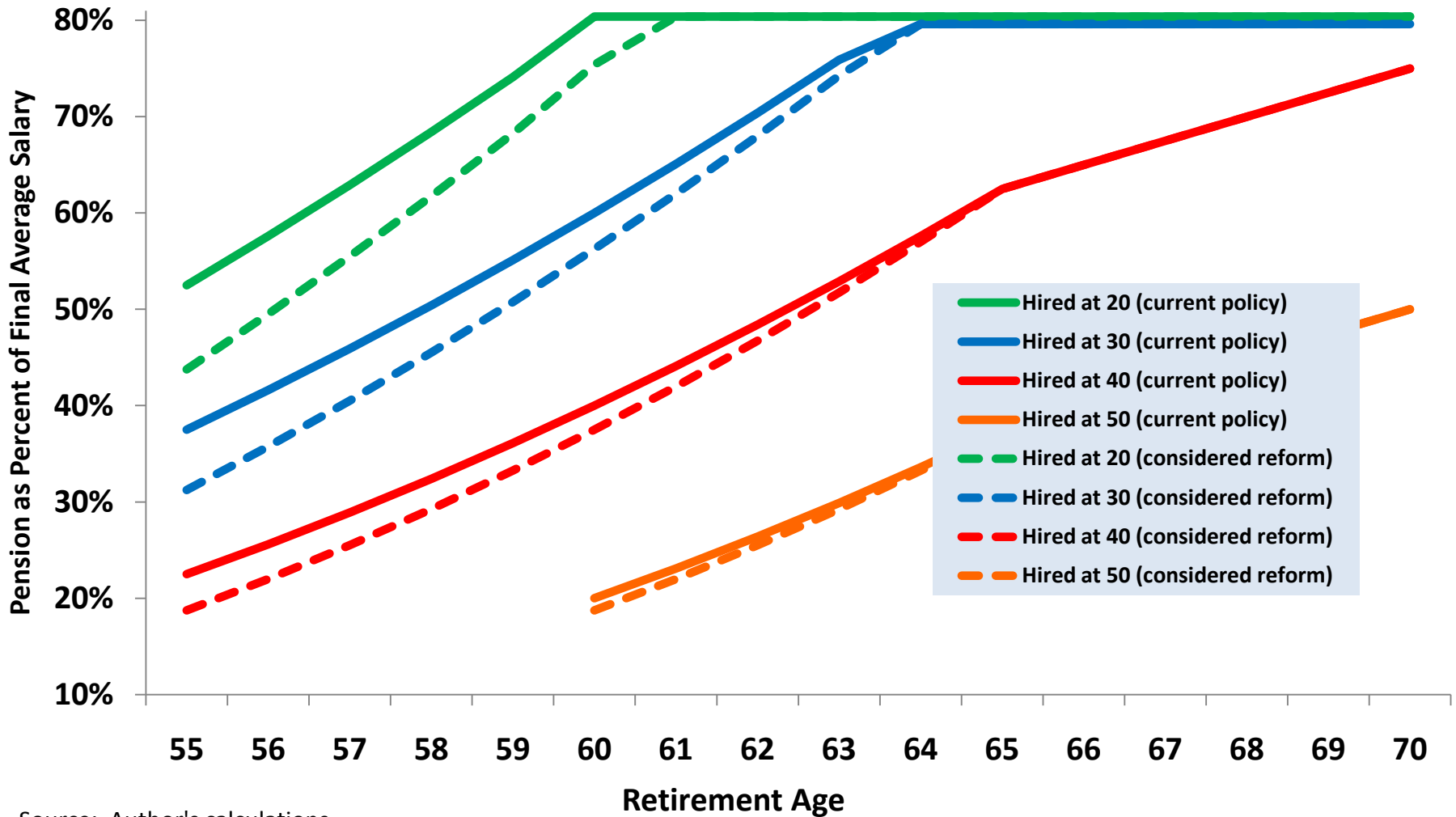
## Focused on Perceived Abuses

- Prevents getting full year of service credit for as little as one day of work.
- Limits special early retirement arrangements.
- Limits the compensation base to wages and salary (excluding housing, travel and car allowances).
- Eliminates service credit for unpaid positions.

# 2009 Study Commission in Massachusetts

- Final report noted early retirement incentive in current formula, and described option for eliminating it:
  - “Encourage later retirement and lower system cost by reducing the age factors by 0.125 percent rather than the current 0.10 percent.”

**Figure 12**  
**Pension as Percent of Final Average Salary, by Retirement Age,**  
**under Reform Considered by Massachusetts Commission**



Source: Author's calculations

# For Discussion

- How many years of post-retirement support should a pension system be structured to support?
- Should a pension system have a “normal” retirement age at all, or should it be neutral with respect to retirement?



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