Just how efficient is the Governor's "Efficiency Task Force" on FRS?

On July 9, 2012, in Florida Retirement System - Pension Plan, Uncategorized, by FRS Options News

It is no secret Florida Governor Rick Scott is putting FRS benefits back in his sights for the 2013 legislature. Every day the papers and internet post more stories about FRS being scarily underfunded and the taxpayers are being unfairly burdened by "overly generous" pensions to public workers. We can only guess that, this being an election year, the legislators made an effort to appease FRS members (and their votes) with few and minor changes in the 2011 legislative session. It does not appear that will be the case next year. Scott recently went on the record saying that pension plan reform is one of his key financial challenges for the state.

The Governor's "Government Efficiency Task Force" stacked with his supportive favorites, Senate President Haridopolis and House Speaker Cannon brought back recommendations that coincide with the Governor's mandates for "pension reform". No surprise there! We can't help but wonder if the Task Force really studied the issue or just had a little guidance from the Governor as to what "efficiencies" they should look for? They identified the FRS Pension Plan as one of their key areas for legislative change. Again, there is no surprise to those who have been watching how politics really work. The task force commentary creates more questions for us than it answers.

"Scott has identified funding for the pension plan as one of the two key financial challenges facing the state".

Why? The pension is one of the best funded pension plans in the country, and at 87% funded. If the Governor's concern is truly proper funding, why did he just sign a bill that reduced contributions in to the plan by some 30%? It makes absolutely no sense to cut contributions to a plan Scott is constantly disparaging as underfunded. If anything, the legislature should have increased contributions in order to bolster the plan funding. His actions contradict his words, and as we all know *Actions Speak Louder Than Words*.

As taxpayers, we all desire financial efficiency and cost consciousness from our government. If the intent of the Governor and Legislature is simply to cut the financial burden to taxpayers brought about by the pension plans for government employees, then why don't they just say that. Instead, it appears (to us at least) the politicos are creating false perceptions and engaging in fear as their rationale for cutting benefits.

"Scott repeated his assertion that the pension plan is not fully funded"

We can't argue with that point. The FRS pension plan is not *fully* funded. At 87% funding level, it is one of the better funded plans in the nation (the average is 77%), and up until the financial chaos of 2008-9, it was overfunded. Currently the FRS Pension Plan has enough assets (in the fund) to meet 100% of its obligations for the next 26.37 years. Would it make sense to allow the investment process to catch up over those 26.37 years (as it has historically done a good job of)? Our question is, is it prudent to make significant long term changes based on a short term anomaly in the financial markets. In the two fiscal years reported since June 30 of 2009, FRS has turned in performances of 14% and 21%.

"Scott said the deficit may actually be worse — a point reinforced by the new government efficiency report — since it is based on a very optimistic annual rate of return of 7.75 percent, which the state has not achieved in recent years".

Who has determined that a target investment return of 7.75% is "very optimistic"? The Standard and Poor's 500, which is a commonly accepted barometer of stock market returns, has returned 11.8% annually over the last 30 years. Longer term the S&P has consistently returned between 9 and 10% historically. Since 70% of the assets in FRS are invested in the stock market, simple math would allow us to believe 7.75% is very realistic. Again, we would ask why the Governor (and his task force) are convinced that the future will deviate significantly from historical long term averages? Some of our readers have accused us of "cherry picking" statistics for FRS returns. The following chart shows ALL returns that are available to FRS members from the Florida SBI website:

1975 - 9.9% - - - 1985 - 29.6% - - - 1995 - 18.5% - - - 2005 - 10.2%

1976 - 14.0% - - - 1986 - 27.8% - - - 1996 - 17.2% - - - 2006 - 10.6%

1977 - 13.5% - - - 1987 - 10.1% - - - 1997 - 21.3% - - - 2007 - 18.1%

1978 - -0.3% - - - **1988 - -0.3%** - - - 1998 - 22.0% - - - **2008 - -4.4%**

1979 - 6.9% - - - 1989 - 14.9% - - - 1999 - 14.0% - - - **2009 - -19.0%**

1980 - 0.0% - - - 1990 - 10.5% - - - 2000 - 10.8% - - - 2010 - 14.0%

1981 - -3.8% - - - 1991 - 9.1% - - - **2001 - -6.9%** - - - 2011 - 22.9%

1982 - 3.7% - - - 1992 - 14.4% - - - 2002 - 8.1%

1983 - 43.5% - - - 1993 - 15.0% - - - 2003 - 2.8%

1984 - -2.8% - - - 1994 - 6.0% - - - 2004 - 16.7%

A little analysis will show some interesting FACTS. Up until the Financial Chaos of 2008, all annual returns were in excess of the target of 8% (now 7.75%) The 10 year average thru 2007 was around 10.33%, and the 20 year return average was closer to 15.5%. Well above the target rate. Since the turmoil of 2008, the short term numbers are now (as logic says they must be) down. The current 5 year and 10 year average return are just over 5%, and the 15 year will be closer to 8% now. All longer period averages are still above the target 7.75%. Even the shorter 3 year rate is already back to a more normal average of around 8.5%. **The simple average return achieved by FRS for ALL year's from 1975 until 2011 is right around 11%.** FRS returns mirror the averages of the stock market, and there is absolutely no reason to believe that will change going forward. One does not need to be a mathematician or Statistician to realize that one really bad year such as we had in 2008 will very obviously skew short term averages, but one bad day does not an average make! FRS is guided by long term interests, not short term!

"Former State Senator Pat Neal of Manataee County headed a subcommittee that looked at other more realistic rates of return, such as basing it on a 30-year average for U.S. Treasury bonds"

This may well be the most ridiculous assumption presented. Why would any investment plan consider using the average return for 30 year US Treasury Bonds, when 70% of the assets are invested in stocks; the same stocks that represent, and are a proxy for the prosperity of the United States? Why would a task force determine that the rates of returns that have been successfully used for the long term are no longer realistic? It is interesting to note that the rate of return over the last 30 years for Treasury bonds is actually 11.8%, .5% higher than the rate on stocks. Rather than use the actual return of treasuries (11.8%), the committee would recommend we only use the interest rate paid out (5.3%). We would argue their presumptions are arbitrary, and defy the real numbers.

If the long term return on stocks is 10%, and 70% of FRS assets are in stocks, then would it not be "realistic" to expect the stock investments to return at least 7%? Would it not also be "realistic" to conclude that if the long term return on bonds is at least 5.8%, then the 30% of the assets invested in bonds would return at least .75% (5.8%/.3) doesn't logic dictate that 7.75% is not "overly optimistic" or "arbitrary". Is this simply another political tactic to make us believe the plan is in trouble so that the legislature can cut benefits?

A lower rate of return would expand the size of the pension plan deficit. For instance, a 5.22 percent return would mean the fund could meet only 61 percent of its obligations.

Why would a "task force on efficiency" suggest a plan whereby they reduce a plan that is well funded at 87%, and reduce it to a grossly underfunded plan at 61% of required funding? Lowering the target rate to such a ludicrous target simply mandates that employers would have to make significantly higher contributions than would be necessary. Such a move would do absolutely nothing positive for FRS; it would simply create an underfunded plan as a political tool to force the conversion to a "401k" type of employee paid plan? Do the Governor and his "efficiency task force" desire to bolster the plan, or do they merely want to create an underfunded plan, in order to force the conversion to a "401-k" type plan?

Other states, facing similar pension challenges, have adopted hybrid plans, including Rhode Island, which adopted a plan last year that is projected to reduce its pension deficit by 41 percent, the efficiency report showed.

Why would the task force choose Rhode Island as an example? According to the Pew Center on the States study, Rhode Island's State Workers and Teachers' Pension Plan is one of the worst funded plans in the nation. It was less than 60% funded when this legislation was passed. The Rhode Island plan calls for changes to be administered *UNTIL* the plan gets to the 80% funding level that is considered appropriate. FRS is currently 87%. Wouldn't it be more logical to compare apples with apples? Once again, the example used, especially without any supporting information as to what the situation was in Rhode Island, is a political slight-of-hand. While the Governor is focusing on rhetoric, the plan is plundered by the legislature.

"State lawmakers and the governor need to stay focused on state pensions and some of the lavish perks that some state employees were allowed to accrue — at great cost to taxpayers".

The average pension paid out to FRS members is slightly over $17,000 per year, to an employee who spent 30 years working for the public. Again, the Governor chooses to use the smallest fraction of pensioners, those who receive high benefits, as the norm. We find that to be so disingenuous, so unrealistic, and so deceptive as to be simply wrong for a Governor that was elected to represent the people of our state to do.

If one repeats fiction often enough, it becomes fact. FRS members really need to educate the public, so the rhetoric does not become the truth!

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