Laura and John Arnold Foundation
Principles for Pension Reform

By their own estimates, state governments have accrued more than three-quarters of a trillion dollars in pension debt. When combined with municipal pension debt, conservative estimates of the total state and local unfunded liability top $1 trillion.

Our public employees deserve more than false promises. They deserve to be part of a system that is fiscally sound, responsibly managed, and that ensures that their retirement benefits will be paid when due. For the past three years, the Laura and John Arnold Foundation has encouraged governments to face the true magnitude of their pension problems and to develop structural reforms that are comprehensive, sustainable, and fair. For some systems, relatively minor changes are sufficient to address the problem. Others require more comprehensive reform. What is invariably true is that addressing the issue today will prevent a crisis tomorrow. Below are the reform principles that we use to guide this work.

1. Employers should fully fund employee benefits.
    a. Employers should have a funding target of at least 100 percent.
    b. Employers should fund benefits as they are earned and not engage in practices that threaten the plan's financial well-being.
        i. Employers should always pay the full cost of benefits earned in any given year.
        ii. Employers should pay off any pension debt over a closed interval not to exceed 30 years.
        iii. Employers should strive to avoid pension debt payment schedules with negative amortization.
    c. Plans should adequately inform policymakers of the plan's downside risk, and policymakers must have a workable plan to manage that risk.
        i. Plans should report at least 30-year projections for employer cost, assets, liabilities, and benefit payments.
        ii. Plans should report at least three sets of projections under differing investment return scenarios (low, middle, expected).
        iii. Policymakers should have a plan in place for actions that will be taken in case the plan accumulates future pension debt.
2. A public retirement plan should place all employees on a path to a secure retirement.
    a. The plan should have required contribution rates that are sufficient to reach a secure retirement.
    b. Employers should strive to offer short or gradual vesting schedules, and in no case should the vesting periods exceed 5 years.
    c. The retirement plan should place employees on a path to a secure retirement regardless of tenure.
3. Employees should have access to professionally managed, low-fee, pooled investments.
4. Employees should have access to lifetime income options (annuities).