

RHODE ISLAND PENSION ADVISORY WORKING GROUP

BRIEF PREPARED BY THE OFFICE OF
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INTRODUCTION

In 2011, the General Assembly passed the Rhode Island Retirement Security Act (“RIRSA”) to address the public pension fund’s large, unfunded liability. As of 2010 the underfunded liability for the Employees’ Retirement System of Rhode Island (“ERSRI”) was approximately \$7 billion, with just a 48.4% combined funded ratio (representing the percent of the retirement system’s actuarial liability that is covered by assets). The RIRSA sought to foster long-term fiscal stability and retirement security in Rhode Island through sweeping changes to the State’s benefits structure.

Among other reforms, RIRSA:

- (1) Froze pensioner cost-of-living adjustments (“COLAs”) until the collective funded status of ERSRI, State Police Retirement Benefits Trust (“SPRBT”), and Rhode Island Judicial Retirement Fund Trust (“RIJRF”) reaches 80%; and
- (2) Replaced participants’ traditional defined-benefit (“DB”) pension plan with a new hybrid system, comprised of a more limited DB plan and a new defined-contribution (“DC”) plan.

After 11 years, the combined funded ratio has risen to 60.4% and actuarial projections anticipate the fund will reach 80% by 2031.

Article 12 of the Fiscal Year 2024 budget, enacted as R.I. Gen. Laws § 36-10.2-11, requires the General Treasurer convene an “advisory working group” to assess the impact of the RIRSA reforms, and proffer “options for consideration” by the General Assembly to “improve the pension programs or address any unintended consequences of the [RIRSA].” R.I. Gen. Laws § 36-10.2-11.

This brief intends to provide members of the Rhode Island Pension Advisory Working Group with a base understanding of the system and the 2011 Reforms, and provides a basic outline for the Working Group’s efforts.

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STATUTORY AUTHORITY

Rhode Island General Laws § 36-10.2-11

- (a) The general treasurer shall establish and convene an advisory working group to assist in the review and analysis of the impacts of the Rhode Island Retirement Security Act of 2011 on the state’s public retirement systems and their current and retired members. The working group shall develop options for consideration by the general assembly that may be needed to improve the pension programs or address any unintended consequences of the Act. Options, to the extent possible, shall include a clear cost-benefit analysis.
- (b) The advisory working group may include, but not be limited to, designees from the following: the office of the general treasurer, actuarial professionals, private sector unions, state and/or national organizations interested in pension reform and sustainability, pension advocacy groups and financial and investment professionals.
- (c) On or before March 1, 2024, the general treasurer shall forward a report containing the findings, recommendations and proposed options for consideration to the governor, speaker of the house and president of the senate.

OPEN MEETINGS ACT

The Rhode Island Open Meetings Act is a state law that requires “public business be performed in an open and public manner.” R.I. Gen. Laws § 42-46-1. By its own language, the Act applies to “public bodie[s],” defined as “any department, agency, commission, committee, board, council, bureau, or authority, or any subdivision thereof.” R.I. Gen. Laws §§ 42-46-2 (5); 42-46-3. Meetings of any public body are subject to the Act’s mandates whenever they convene “to discuss and/or act upon a matter over which the public body has supervision, control, jurisdiction, or advisory power.” R.I. Gen. Laws § 42-46-1. While the statute refers to the body as an “advisory working group,” the body is created by the legislature and quite clearly has “advisory power” that is derived from statute and is therefore subject to the Act.

Working Group Members must take caution to not inadvertently create a quorum through informal discussion. For purposes of the Act, a quorum is “a simple majority of the membership of a public body.” *See* R.I. Gen. Laws § 42-46-2 (6). Casual conversation among Working Group members may create a “walking” or “rolling” quorum in certain circumstances. A rolling quorum “may be created where members of a public body attain a quorum by a series of one-on-one conversations or interactions, whether in person or by electronic means.” Open Meetings Act Checklist, Office of Attorney General Peter F. Neronha (July 2020). For example, Member A speaks with Member B on matters pending before the Working Group. Member A – in turn – speaks with Member C and Member C speaks with Members D and E. While no more than three members spoke at any given time (an insufficient number for a quorum in a body of ten) a total of five members discussed the same subject through a series of discussions.

MEETING STRUCTURE

Collectively, the Advisory Working Group is scheduled to meet six times. Meetings will commence in early November and continue through the start of the legislative session to terminate in mid-February. Meetings will be held at the State House. Three of the six meetings are scheduled to be held in House hearing rooms, and three of the six meetings are likely to be held in Senate hearing rooms. The tentative schedule will be as follows:

- The first meeting, on or around **November 2, 2023**, will be in the State House, House Lounge. The General Treasurer will begin the meeting with a brief overview of the Office’s efforts in convening the Working Group. The Treasurer will then discuss the charge of the Working Group, define its purpose, name the co-chairs, and lay the foundation for subsequent sessions.
 - After, each member will introduce themselves and provide a brief summary of their professional experience and expertise.
 - During this meeting, the Working Group will hear an actuarial assessment of the Rhode Island Pension fund from Joseph Newton of Gabriel, Roeder, Smith (“GRS”), a review of State pension investments and performance by William Forde of NEPC, and a presentation concerning the State’s finances and bonding capacity relative to the Rhode Island Pension fund from Thomas Huestis of PRAG.
 - Throughout the presentations, the Working Group will have the opportunity for questions, comments, and to propose areas of further study.
- The second meeting, on or around **November 30, 2023**, will be in the State House, House Lounge, during which the Working Group will solicit testimony from stakeholders in organized labor. Time permitting, there will be public comment at this meeting.
- The third meeting, on or around **December 14, 2023**, will be in the State House, House Lounge, during which the Working Group will hear testimony from other community stakeholders, including active and retired members of ERSRI. There will be public comment at this meeting.
- The fourth meeting, on or around **January 17, 2024**, during which the Working Group will hear an overview of public pension trends from subject matter experts, will have public discussion and debate concerning the materials presented thereto, and will begin to finalize options for consideration by the actuary and ultimately by the General Assembly. The actuary will prepare assessments at the direction of the Working Group. If there are any outstanding presentations necessary, or if the Working Group would like to hear more concerning earlier presentations, that will occur during this meeting.
- The fifth meeting, on or around **January 31, 2024**, during which the Working Group will finalize its preliminary findings. The state actuary will present any actuarial assessments requested during the fourth meeting. The Working Group will discuss and debate the options presented, narrowing the options based on plausibility.
- The sixth and final meeting, on or around **February 21, 2024**, during which the Working Group will summarize its efforts, its findings, and options for consideration contained in the final report.

MEMBERSHIP

- (1) **Ernie Almonte, CPA** – President of the Rhode Island League of Cities and Towns.
- (2) **Eric Atwater, FSA** – Partner, Aon PLC.
- (3) **Patrick Crowley** – Secretary Treasurer of the AFL-CIO.
- (4) **Michael DiBiase** – President and CEO of the Rhode Island Public Expenditure Council.
- (5) **Thomas Huestis** – Senior Managing Director of Public Resources Advisory Group (“PRAG”).
- (6) **John P. Maguire** – Active Teacher Representative, Employees’ Retirement System of Rhode Island Board and retired member of ERSRI.
- (7) **Alicia Munnell** – Director of the Center for Retirement Research at Boston College. Director Munnell has selected **Laura Quinby** to serve as her designee. Ms. Quinby is a senior research economist at the Center for Retirement Research.
- (8) **George Nee** – President of the AFL-CIO.
- (9) **Edinaldo Tebaldi** – Professor of Mathematics and Economics and Director of Strategic Planning & Institutional Effectiveness at Bryant University.
- (10) **Jonathan Womer** – Director of the Rhode Island Department of Administration.

TRUTH IN NUMBERS REPORT

A forerunner to pension reform, the Office of General Treasurer Gina Raimondo issued a report in June 2011 called “Truth in Numbers: The Security and Sustainability of Rhode Island’s Retirement System.” Gina M. Raimondo, *Truth in Numbers: The Security and Sustainability of Rhode Island’s Retirement System*, June 2011 (hereinafter the “Report”). Intended to justify a comprehensive “re-design” to “financially secure” Rhode Island’s pension system, the report addressed four core facets of the pension system, each summarized in turn:

- (1) Estimating the price tag for past service;
- (2) Diagnosing the key drivers of the structural pension deficit;
- (3) Understanding the implications of further inaction; and
- (4) Providing a framework for solutions.

See id. at *1.

(1) Estimating the Price Tag for Past Service

To establish a baseline, the Report first assessed the financial scope of Rhode Island’s pension problem. *See id.* at *2. In doing so, it considered the unfunded liability, applying both public and private pension accounting principles. *See id.* When applying public accounting rules, the Report determined Rhode Island had a \$6.8 billion unfunded liability. *See id.* When applying private pension rules – which are generally more conservative given the relative impermanence of private pensions¹ – the Report estimated the State’s unfunded liability to be \$9 million. *See id.*

(2) Diagnosing the Key Drivers of the Structural Pension Deficit

In effect, the Report traced Rhode Island’s pension deficit to “[d]ecades of ignoring actuarial assumptions [which] led to lower taxpayer [and] employee contributions being made into the system.” *See id.* at *3.

The Report credited this failure to “[f]ive primary factors”:

- (a) **The State’s repeated failure to “utilize sound actuarial practices,”** by ignoring actuarial recommendations in the late 1980s and throughout the 1990s. *Id.* Specifically, the State only made 52% of the annual required contributions and 0% of the state contribution for teachers (1992), relied on unrealistic investment return assumptions (1997), and artificially inflated the asset value by shifting the valuation method during turbulent economic times (1996-1997). *Id.*
- (b) **The State increased employee benefits without a corresponding increase in the employee and/or employer contribution rates** throughout the 1970s and 1990s. *See id.* at *4.
- (c) **The pension structure** that emerged from the 2005-2010 reforms failed to address COLAs, resulting in retirement benefits that exceeded 100 percent of an employee’s final average

¹ “Public and private pensions are governed by different accounting rules with varying approaches to two key calculations, the discount rate and asset valuation, which have a significant impact on determining the unfunded liability for any fund.” Raimondo, *Truth in Numbers, supra*, at *2.

earnings *before* retirement in some instances. *See id.* at *5. Compounding the issue, “the true normal cost for nearly all employees and retirees had never been fully contributed to the system,” further increasing the unfunded liability. *Id.*

- (d) **Retirees were living longer**, increasing long-term pension cost from benefits and COLAs without corresponding funding changes. *See id.*
- (e) The **assumed investment performance** was artificially inflated. *See id.* at *6. The resulting annual required contribution (“ARC”) payments, which rely on the assumed investment performance, were lower than the true investment performance would dictate. This necessitated additional withdrawals from the fund itself (to close the nexus), thereby increasing the unfunded liability. Illustrative of this point, the state pension fund’s investment performance “averaged only 2.28 percent over the [preceding] decade . . . which is significantly below its assumed 8.25 percent rate of return.” *Id.*

(3) Understanding the Implications of Further Inaction

Absent systemic reform, the Report concluded that large, unsustainable annual expenditures – consuming an ever-greater share of the State budget – would be required to continue meeting the ARC payment given the existing benefit structure. *See id.* Based on analyses performed by actuaries, the Report found that “taxpayer contributions to the state retirement expenses [had] doubled” in the preceding seven years, from \$139 million in 2003 to \$303 million in 2010. *Id.* “Under projections provided by [the actuary], these contributions [would] double again to approximately \$615 million in 2013 and [would] soon exceed \$1 billion.” *See id.* at *7. And since employee contribution rates are fixed by statute, “taxpayers shoulder the burden for all required contribution increases.” *See id.* If taxpayer dollars must be increasingly allocated to meeting pension obligations, state aid to fund vital public services must necessarily decrease by the same amount. *See id.* at *8-9. Exasperating the problem, the Report argued the State’s credit rating would decline as the pension system’s unfunded liability grows, thereby increasing the cost of borrowing. *See id.* at *9.

(4) Providing a Framework for Solutions

Through reform, Treasurer Raimondo sought to achieve one fundamental goal: “a secure, sustainable retirement system.” *See id.* at *11. To achieve that, Treasurer Raimondo recommend the package of changes that would become the Rhode Island Retirement Security Act of 2011, discussed *infra*.

RHODE ISLAND RETIREMENT SECURITY ACT OF 2011

I. Findings

To justify pension reform, to both the public and members of the General Assembly, the architects of the RIRSA included a robust “legislative intent and findings” section. As drafted and enacted, the legislature found that Rhode Island had “one of the lowest funded and most vulnerable statewide pension systems in the country,” necessitating “comprehensive reform” “to ensure the sustainability of the state’s public retirement system.” 2011-S 1111a, at *1. The retirement system’s “\$7 billion” unfunded liability was found to “threaten[] the base pensions of current and future public workers, hamper[] the ability of the state to provide its citizens with vital services necessary for the public’s health, safety and welfare, and place[] an unsustainable financial burden on all Rhode Island citizens and taxpayers.” *See id.*

Echoing findings made in Treasurer Raimondo’s Truth in Numbers Report, the impetus for reform was underscored by the rapid rise in “government contributions to ERSRI,” which “more than doubled between fiscal years 2005 and 2011” and were “estimated to double again in fiscal year 2013 to exceed over \$600 million.” *Id.* at *2. Without immediate reform, the legislature predicted the State’s contribution would continue to increase and soon “exceed \$1 billion dollars” annually, impacting the State’s credit rating, and impeding the “[S]tate’s ability to address critical infrastructure needs for education, transportation and other crucial public projects.” *Id.* at *2-3.

The Act likewise calls attention to the “myriad of pension program designs” in Rhode Island’s municipalities, and the “critical and immediate public importance that these public pension programs be restructured.” *Id.* at *3.

In passing the Act, and by its express language, the legislature found Rhode Island’s pension system had reached an “emergency stage” which “must be addressed without delay.” *Id.* at *4. The RIRSA, it concluded, was both “reasonable and necessary to achieve that end.” *Id.*

II. Summary of Statutory Changes

As introduced in October 2011, the RIRSA proposed five major reforms to chart a path forward for Rhode Island’s pension system. The RIRSA:

- (1) Suspended COLAs until the collective funded ratio of the state pension system reached 80%, and instead replaced the annual COLA with an adjustment once every four years;²
- (2) Created a new defined-contribution pension plan to work in tandem with the State’s traditional defined-benefit pension plan;³
- (3) Increased the retirement age for current employees to Social Security age thresholds;⁴

² *See* R.I. Gen. Laws § 36-10-35(g)(1) (concerning state employees but replicated in Titles 16 and 45)

³ *See* R.I. Gen. Laws § 36-10.3-1, *et seq.*

⁴ *See* R.I. Gen. Laws § 36-10-9(c)(ii) (concerning state employees but replicated in Titles 16 and 45); 2011-S 1111a, at *17-18 (RIRSA)

- (4) Extended the amortization period from 19 to 25 years to make payments toward the unfunded liability more palatable to taxpayers and more sustainable for the state budget;⁵ and
- (5) Crafted a framework to help municipalities reign in unfunded pension liabilities. *See, infra.*⁶

1. Suspension of Annual COLAs

RIRSA suspended COLA payments until the aggregate funded ratio for ERSRI, SPRBT, and RIJRFRT reaches an 80% funded ratio. Under the new law, pensioners received an adjustment every five years – subsequently amended to four every year – based on a statutory formula that directly corresponds with investment performance. *See* R.I. Gen. Laws §§ 16-16-40 (f); 36-10-35 (h); 45-21-52 (i).⁷ Before pension reform, “[r]etirees received a [COLA] tied to inflation and capped at 3 percent of the first \$35,000 of their pensions; in other words, up to \$1,050 per year.” Robert Hiltonsmith, *Rhode Island’s New Hybrid Pension Plan Will Cost the State More While Reducing Retiree Benefits*, Economic Policy Institute Issue Brief #366 (June 20, 2013), at 2; 2011-S 1111a.

2. Hybrid Defined-Benefit, Defined-Contribution Plan

Perhaps the most significant and enduring of RIRSA’s reforms replaced pensioners’ traditional DB pension plan with a new hybrid system, comprised of a more limited DB plan and a new DC plan. This reform aimed “to reduce defined-benefit liabilities with a DC fund while also maintaining support from union groups who desire the security of a DB system.” Randazzo, *Pension Reform Case Study: Rhode Island*, *supra*, at *18.

Following reform, employees are automatically enrolled in a DC account administered by TIAA-CREF and are given a number of investment options. Employees must contribute 5% of their base salary and employers (i.e., the State) must contribute 1%. *See* Gabriel Roeder Smith & Company, *Rhode Island Retirement Security Act of 2011: Plan Details*, at *2 (October 2011).

Previously, state employees and teachers contributed 8.75% and 9.5% of their respective salaries to the DB fund. *See* Gabriel Roeder Smith & Company, *Rhode Island Retirement Security Act of 2011: Plan Details*, at *2 (October 2011).

3. Retirement Age

The RIRSA raised the normal retirement age for receiving a full pension to match the Social Security normal retirement age (then 66 years of age). *See* Hiltonsmith, *supra*, at 3. The ‘Rule of

⁵ *See* R.I. Gen. Laws § 36-10-2.1 (decreasing the amortization period from 30 years to 20 years); 2011-S 1111a, at *14 (RIRSA)

⁶ This framework created the Advisory Council to Locally Administered Pension Plans and the Locally Administered Pension Plan Study Commission. *See* R.I. Gen. Laws § 36-10.2-1, *et seq.*

⁷ Legislation passed during the 2023 legislative session repealed the four-year COLA, instead creating a ‘quarter COLA.’ This statute provides pensioners one-fourth of a COLA each year based on the same statutory formula. *See* R.I. Gen. Laws § 16-16-40 (g); 36-10-35 (i); 45-21-52 (j). Both the new quarter COLA and the four-year COLA are calculated based partially on the consumer price index and partially on a 5-year average investment return, with a maximum of 3.5% and a minimum of 0%. Outcomes have been varied over the past decade. Since the five-year interment performance average used to calculate COLA size is heavily influenced by investment performance in the final months of the 5-year lookback period. Consequently, there was no COLA in 2016 and a relatively small adjustment in 2020.

95' is an "alternative full benefit retirement eligibility date," which allows members to retire earlier than their schedule-based eligibility date.⁸ *Id.* "Under the Rule of 95, members can retire when their age plus their years of service equal 95 provided that they are at least 62 years old." *Id.* Prior to RIRSA, teachers and state employees could retire with full benefits at the age of 65 with 10 years of service, or at the age of 62 with 29 years of service. *See* Gabriel Roeder Smith & Company, Rhode Island Retirement Security Act of 2011: Plan Details, at *2 (October 2011).

4. Amortization Period

The RIRSA extended the amortization period from 19 to 25 years to "smooth out the unfunded liability so that taxpayer payments needed to ensure solvency would be easier for the state budget to handle." Randazzo, *Pension Reform Case Study: Rhode Island, supra*, at 19.

5. Municipal Pension Reform

As part of the RIRSA reforms, the General Assembly passed the "Pathway to Retirement Security for Locally Administered Pension Funds Act" to "promote the sustainability and longevity of pension plans established and administered by municipalities." R.I. Gen. Laws § 45-65-2. By its express language, the statute aims to:

- (1) Preserve a reasonable and affordable level of pension benefits;
- (2) "Avoid significant and unanticipated retirement benefit deductions";
- (3) Avoid diversion of resources to satisfy pension obligations;
- (4) Prevent the financial downgrade of municipal bond ratings;
- (5) Encourage ratings agencies "to take positive credit actions on Rhode Island municipal bonds"; and
- (6) Foster economic growth and financial stability in Rhode Island.

R.I. Gen. Laws § 45-65-3 (3). To accomplish that goal, the statute authorized the creation of a 14-member study commission and a five member "advisory council." *See* R.I. Gen. Laws §§ 45-65-8, 45-65-10 (a). The Commission was created to "review existing legislation and pension plan administrative practices and to make recommendations for the improved security and funding of locally administered plans and other post-retirement benefit obligations of cities and towns." R.I. Gen. Laws § 45-65-8. The Commission issued a comprehensive report on January 9, 2015.

State law requires the Advisory Council furnish an annual report by April 30 of each year that includes an assessment of the fund performance, funded status, administrative costs, assumed rate of return, and budgetary capacity for each locally administered pension plan. *See* R.I. Gen. Laws § 45-65-10 (b). As Chairperson, the Treasurer is further obligated to include "an opinion . . . regarding the sustainability of each plan and any potential areas of concern." R.I. Gen. Laws § 45-65-10 (d). The Advisory Council completed its most recent study in late April of 2023.

⁸ Employees' Retirement System of Rhode Island, *Retirement Eligibility Rules, Eligibility based on the Rule of 95*, accessed Aug. 25, 2023, at [Retirement Eligibility | ERSRI](#).

2015 PENSION LAWSUIT SETTLEMENT

After the General Assembly passed the RIRSA in 2011, “a number of lawsuits were filed by various state and municipal unions on behalf of their affected members,” claiming that the RIRSA reforms were unconstitutional and thus invalid. *Clifford v. Raimondo*, 184 A.3d 673, 678 (R.I. 2018).

Following protracted litigation and a neutral mediation process, the parties agreed to a settlement, softening some of the benefit cuts occasioned by the 2011 Reform. Thereafter, the legislature “enacted the 2015 amendments to RIRSA,” consistent with the terms of the settlement. *Id.* at 684. In so doing, the legislature implemented the following changes, *inter alia*, to the RIRSA, effective July 1, 2015:

- Retirees or beneficiaries of retirees that retired on or before June 30, 2012, received a 2% COLA payment on the first \$25,000 of their pension benefit immediately.
- Retirees or beneficiaries of retirees that retired on or before July 1, 2015, received two \$500.00 stipends: one within 60 days of enactment, one the following year.
- The statutory formula used to calculate a COLA was amended and the maximum annual COLA was increased to 3.5%.
- Rather than receive a COLA once every five years, retirees or beneficiaries of retirees will receive a COLA once every four years until the plan reaches 80% funded status.
- For retirees and beneficiaries of retirees that retired on or before July 1, 2015, the \$25,000 COLA cap was increased to \$30,000 (indexed) for any COLA payment made under the four-year COLA provision.
- State employees, teachers, and active municipal employees in the MERS system with 20 years of service as of June 30, 2012, were no longer required to participate in the defined contribution plan and the future accrual rate (post July 1, 2015) increased to 2%, subject to a corresponding increase in the member contribution rate.⁹
- State employees, teachers, and active municipal employees in the MERS system with between 10 and 20 years of service as of June 30, 2012, received an additional employer contribution.¹⁰
- The retirement eligibility age was decreased for all current and future state employees, teachers, and municipal employees in the MERS system.¹¹
- For members impacted by the RIRSA part-time anti-spiking rule, if a member’s highest 5-year average calculation is less than the \$35,000 indexed, that member’s pension will be based on the greater of the following: (1) the highest 10-year average earnings, or (2) the highest 5-year earnings with an indexed \$35,000 cap.

⁹ For state employees and teachers, the member contribution rate increased to 11% of pay. For municipal employees in the MERS system, the member contribution increased to either 8.25% or 9.25% depending on whether the unit has a COLA provision.

¹⁰ The additional employer contribution was 0.25% for members with 10 to 15 years of service, and 0.50% for members with 15 to 20 years of service.

¹¹ Following enactment, current and former members were eligible to retire with full benefits upon reaching age 65 with 30 years of service, age 64, with 31 years of service, age 63 with 31 years of service, or age 62 with 33 years of service or under the then-existing RIRSA retirement date, whichever was earlier.

- The early retirement penalty for ERSRI and MERS members that chose to retire before eligible for full unreduced benefits was changed to the following schedule: 9% for year one, 8% for year two; and 7% for each year thereafter.
- The retirement age for current and former members of MERS Police and Fire units was reduced to age 50 with at least 25 years of service, or any age with at least 27 years of service, subject to a 2% increase in the member contribution rate. The multiplier was also increased for active and future MERS Police and Fire members who retire after July 1, 2015, after reaching age 57 with at least 30 years of service.

Approximately 400 class members objected to the settlement agreement. *See Clifford*, 184 A.3d at 682. After a five day “fairness hearing,” the Rhode Island Superior Court concluded the terms of the settlement were “both procedurally and substantively fair.” *Id.* at 684. Several plaintiff classes appealed the Superior Courts decision. In 2018, the Rhode Island Supreme Court found the Superior Court gave due consideration to the “concerns raised by various objectors to the settlement,” and did not “abuse her discretion in concluding that the settlement was fair, reasonable, and adequate.” *Id.* at 695. The Supreme Court thereby affirmed the settlement. *See id.*

BOND RATINGS

The relative health and changes to the State's pension fund impact the State's bond rating. At present, Rhode Island maintains a 'AA' general obligation rating from both Fitch Ratings and Standard & Poor. *See* Fitch Ratings, Fitch Rates Rhode Island's \$147MM GOs 'AA'; Revises Outlook to Positive, at 1 (Oct. 13, 2023) (hereinafter "Fitch Ratings"); Standard and Poor, Rhode Island; Appropriations; General Obligation; Moral Obligation, at 2 (Oct. 12, 2023) (hereinafter "S&P"). This year, Fitch Ratings revised its Rating Outlook to "Positive from Stable." *Id.* at 1. The State maintains a Aa2 issuer rating and a stable outlook from Moody's Investors Services. *See* Moody's Investor Services, Rating Action: Moody's assigns Aa2 to Rhode Island's GO bonds; outlook stable, at 1 (Oct. 12, 2023) (hereinafter "Moody's").

The State's long-term liabilities, which include the pension fund, are a key driver underlying those ratings. *See* Fitch Ratings, at 1-2. Fitch Ratings cautioned that the State's outstanding pension liabilities continue to dominate its long-term liabilities. Despite Rhode Island's pension obligations, Fitch concluded that "[p]ensions stabilized following statutory benefit and assumption changes a decade ago that were validated in court." *See, id.* Indeed, "growing financial relief from pension changes enacted more than a decade ago" have had a marked influence in Fitch's decision to upgrade the State's outlook. *Id.* at 1-2.

S&P likewise finds confidence in past "reforms to reduce the state's unfunded postretirement liabilities and sustain pension funding progress." *See* S&P, at 3. But S&P tempers this optimism with reference to historically weak pension funding discipline and low funding levels. *See id.* at 4. While noting the "improved overall pension funded ratio" at the conclusion of fiscal year 2021, S&P considers the funded status "as relatively low, but improving." *See id.*, at 3-4. To improve Rhode Island's core economic metrics, S&P counseled continued fiscal discipline in pension administration, which would likely occasion positive rating action. *See id.*, at 4-5

THE 2005 REFORM AND ITS IMPACT ON EMPLOYEE RETENTION

In 2005, the Rhode Island General Assembly passed a partial pension reform package that significantly reduced retirement benefits for certain public employees. *See* 2005-H 5270 Art. 7 Sub. A-aa (the “2005 reform”). The 2005 reform “raised the normal retirement age¹² [], reduced the multiplier that determines benefit levels and capped future cost-of-living adjustments” without a corresponding raise in salary.¹³ Laura D. Quinby and Gal Wettstein, *Do Benefit Cuts Encourage Public Employees to Leave?*, Center for Retirement Research at Boston College, State and Local Pension Plans Number 65, at *2 (May 2019). Many teachers also lost access to subsidized retiree health insurance (“RHI”) before age 65. *See* Laura D. Quinby and Gal Wettstein, *Do Benefit Cuts Encourage Public Employees to Leave?*, Executive Summary, Center for Retirement Research at Boston College.

Significantly, the 2005 reform *only* impacted ERSRI members who were not vested (i.e., attained 10 years of service) by June 30, 2005. *See* 2005-H 5270 Art. 7 Sub. A-aa. Vested ERSRI members and municipal employees participating in MERS were both spared and retained pre-reform benefits. *See id.*

The unique structure of this reform allowed the Center for Retirement Research at Boston College (“the Center”) to perform a comparative assessment of the number of employers staying in state service or in the classroom before and after the 2005 Reform. Specifically, the Center compared “non-vested members of ERSRI, before and after the reform, to vested members and to all members of MERS.” Quinby, Executive Summary, *supra*.

Through their study, the Center found that the 2005 Reform “caused an immediate 2.4-percentage-point increase in the rate of job exit (‘separation’), corresponding to a 12-percent increase in the baseline separation rate.” *Id.* “To put this response into context given the size of the benefit cut, [the Center’s analysis] scale[d] these effects by the expected present value of benefits lost, finding that a one-percent decrease in lifetime benefits caused a 0.28-percent increase in the rate of separation, on average.” *Id.* The study notes, however, that teachers were less likely to separate compared with state employees, given the nature of their profession. *See id.*

From a fiscal perspective, the Center’s study estimates that separations occasioned by the 2005 Reform “caused a one-time increase in direct costs of between \$1.8 million and \$8.1 million,” a comparatively small cost “relative to the pension savings.” *Id.* The study tempered this conclusion, however, noting that cost associated with “the loss of skilled workers” is difficult to quantify. *Id.*

¹² The 2005 Reforms established the retirement age of 59 with 29 years of service or age 65 with 10 years of service, created the Plan B benefit accrual structure, and change the COLA to the percentage increase in the CPI-U or 3%, whichever is less, effective on the third anniversary of one’s retirement. *See* Senate Fiscal Office Issue Brief, Recent Pension Reforms, at 2 (October 12, 2010).

¹³ Prior to the 2005 reform, employees could retire at age 60 with 10 years of service, or at any age with 28 years of service, and received a fixed 3% compounding COLA annually. After the reform, employees not vested by the reform implementation date could retire at age 65 with 10 years of service, or at age 59 with 29 years of service, and receive a CPI-linked COLA capped at 3% beginning on the third anniversary of their retirement. *See* 2005-H 5270 Art. 7 Sub. A-aa.

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Amortization Period and Amortization Cost – To spread the cost of the unfunded liability over a period of time, a plan chooses an amortization period during which it will pay off its unfunded liability. The unfunded actuarial accrued liability from the 2011 pension reform is being amortized over a closed 25-year period from June 30, 2010. *See* ERSRI Actuarial Experience Investigation for the Period Ending June 30, 2022, at 32. The remaining amortization period is 12 years. *See id.* The amortization cost is then calculated as the amount that will be sufficient to pay off the unfunded liability over the amortization period. *See* ERSRI Actuarial Experience Investigation for the Period Ending June 30, 2022, at 37.

Contribution Rate – The fiscal year 2023 employer contribution rates are based on annual actuarial valuations. *See* ERSRI Audit Fiscal Year Ended June 30, 2022, at 11. The employer contribution rates for the DB plan for fiscal year 2023 are 28.01% for State employees, 26.16% for Teachers, 24.16% for Judges, and 20.87% for State Police. *See id.* Employers contribute 1% to the DC plan by statute (3% for teachers or MERS non-police or fire employees not covered by Social Security). *See* RI 401(a) Adoption Agreement, executed Jun. 29, 2012. By statute, employees contribute 5% of their annual salary. *See* ERSRI Audit Fiscal Year Ended June 30, 2022, at 11; RI 401(a) Adoption Agreement, executed Jun. 29, 2012. Teachers who are not covered by Social Security must contribute 7% of their compensation. *See* ERSRI Audit Fiscal Year Ended June 30, 2022, at 27; RI 401(a) Adoption Agreement, executed Jun. 29, 2012.¹⁴

Cost of Living Adjustment (“COLA”) – The RIRSA suspended full annual COLAs until the ERSRI, SPRBT, and JRBT plans collectively reach a funded status of 80%. Once returned, the COLA calculation is represented by the following formula: 50% of the COLA is calculated by taking the previous 5-year average investment return, less 5% (5-year return minus – 5.0% with a max of 4%) and 50% calculated using the increase in the Consumer Price Index for All Urban Consumers (“CPI-U”) from the prior September 30 (max of 3%) for a total maximum COLA of 3.5%. *See* R.I. Gen. Laws §§ 16-16-4 (g)(1)(B); 36-10-35 (h)(1)(B); 45-21-52 (d)(1)(B). Under legislation passed during the 2023 session, retired members of ERSRI and MERS units that have not reached an 80% funded ratio¹⁵ will receive .25% of the annual COLA until the system reaches 80% funded. *See* R.I. Gen. Laws §§ 16-16-4 (g)(2); 36-10-35 (h)(2); 45-21-52 (d)(2).

For members (and their beneficiaries) that retired after June 30, 2015, the annual benefit adjustment provided in any calendar year is equal to the lesser of either the member’s retirement allowance or a base amount of \$28,855 (indexed annually) amount (as set by the pertinent statute, depending on type of service) multiplied by the percent resulting from the COLA calculation.

For member (and their beneficiaries) that retired before June 30, 2015, the annual benefit adjustment provided in any calendar year is equal to the lesser of either the member’s retirement allowance or a base amount of \$31,026 (indexed annually) amount (as set by the pertinent statute, depending on type of service) multiplied by the percent resulting from the COLA calculation.

¹⁴ Note, these are *pre-tax* dollars. *See* RI 401(a) Adoption Agreement, executed Jun. 29, 2012.

¹⁵ As of June 30, 2022, 64 of the 122 MERS Units were receiving COLAs. *See* ERSRI Audit Fiscal Year Ended June 30, 2022, at 19, 21.