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Analysis

H.C.R. 20 – Rep. Schneider
As Introduced

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ORSC Position

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House Concurrent Resolution 20 urges Congress to reject any legislation that would require Ohio's public employees to participate in Social Security.

<u>Staff Comments</u> - Social Security is projected to become insolvent by the year 2041, at which time it will be able to provide only 74% of the benefits payable. While the various proposed reforms have differed widely, one common thread among various proposals over the years provides for mandatory Social Security coverage for all new state and local government employees currently not covered.

The Social Security Administration estimates that approximately 5 million state and local government employees occupy positions not covered by Social Security. Seven states - California, Colorado, Illinois, Louisiana, Massachusetts, Ohio, and Texas - account for 71% of the noncovered employees. Based on a survey conducted by the Public Pension Coordinating Council, teachers, along with police and firefighters, are more likely than other employees to occupy noncovered positions.

Unlike the Social Security System, Ohio's public retirement systems are not in need of federal reform. These systems are well funded. Congress should follow the example of Ohio's public retirement systems in its consideration of effective Social Security reform.

Ohio's public retirement systems provide comprehensive, secure benefits through effective management and oversight: The Ohio General Assembly has a long and successful track record regarding its five statewide public employee retirement systems. With over $143 billion in combined assets as of January 1, 2005, Ohio's public retirement systems provide comprehensive retirement, disability, survivor and health care coverage to over 1.5 million state and local government employees, teachers, school employees, police and firefighters, and state troopers. Ohio's public retirement systems are actuarially funded to meet their long-term pension obligations, well-managed by their respective boards, and effectively monitored by the legislature through the ORSC - one of the first permanent, bi-partisan and independent pension oversight commissions in the nation.

Ohio's public retirement systems are funded on an actuarially sound basis: Unlike Social Security, which essentially has been financed on a pay-as-you-go basis, Ohio's public retirement systems are funded on an actuarially sound basis. Simply put, the laws governing these systems require public employers and employees to contribute the money to cover the IOU's being earned this year. As a consequence, reserves are accumulated and invested by the systems to pay future benefits that have been promised to members and their families. Investment income constitutes the primary source of revenue for all five systems, funding up to 75% of benefit costs. Under this funding method, contributions are expected to remain relatively stable from generation to generation of Ohio taxpayers; whereas significant increases in Social Security taxes will be required in the future to maintain current benefit levels due to the demographic shift occurring in the United States with fewer people working and paying into Social Security and more people retiring and receiving benefits from Social Security.

Mandatory social security would impose significant tax increases on Ohio's public employers and employees and would likely cause significant reduction or elimination in

benefits, including retiree health care: Ohio's public employees are required to contribute to the retirement systems, ranging from 8.5% to 10.1% of pay. Unlike Social Security taxes, these contributions are generally tax-deferred. Therefore, the after-tax income of Ohio's public employees would be reduced by any shift from pre-tax retirement contributions to after-tax Social Security contributions. Public employers are also required to contribute to the retirement systems, ranging from 13.31% to 25.50% of payroll. Mandatory Social Security coverage would impose an additional 6.2% of pay, up to $90,000 in 2005, on the employee as well as 6.2% on the employer, for a total of 12.4%. A 2005 study on the cost impact of mandating Social Security for state and local governments completed by the Segal Company found that mandatory Social Security coverage would cost Ohio nearly $4.4 billion in employee and employer Social Security taxes during the first five years. Both the Segal report and recent testimony by the Government Accountability Office (GAO) before the House Subcommittee on Social Security point out that pension costs would increase or existing benefits would need to be reduced in order to finance the increased costs associated with mandatory coverage.

Social security provides no comparable benefits for public safety officers: Ohio's public retirement systems are tailored to meet the direct needs of its public employers and employees. This is especially true in the case of Ohio's law enforcement and public safety officers who are provided early retirement and expansive disability and survivor coverage due to the physical demands and hazardous conditions of their employment. Social Security makes no distinction among occupations and, therefore, provides no comparable coverage.

Mandatory social security would create significant costs with little, if any, benefits: Mandating Social Security coverage for state and local government employees is flawed public policy. It would cause great harm to the long-term financial soundness of Ohio's public retirement systems, which predate Social Security, and cause these systems to break promises made to their members with little, if any, material help towards addressing the basic funding problems that have plagued Social Security for decades. A GAO report issued in August 1998 indicates that mandatory Social Security coverage for state and local government employees would add only two years to the solvency of the Social Security System. In 2005, the GAO again acknowledged that mandatory coverage would represent only a small gain for Social Security solvency. In short, mandatory Social Security coverage for state and local government employees is simply another unfunded federal mandate at the expense of well funded state and local retirement systems, such as Ohio's, which provide financial security for millions of public employees and their families.

Social security windfall and offset provisions eliminate unjust enrichment: Contrary to popular belief, Ohio's public employees are not "gaming" the Social Security System. Congress enacted the government pension offset provision in 1977 and the windfall elimination provision in 1983. These provisions eliminated the possibility of state and local government employees collecting windfalls, or in some cases anything at all, from Social Security even though they and/or their spouses had contributed to Social Security. The government pension offset affects spouses of government workers. This provision offsets the amount a spouse or widow(er) receives from Social Security by two-thirds of the amount of the government pension. The windfall elimination provision, on the other hand, reduces a worker's social security benefit if he or she receives a government benefit as well as Social Security.

Voluntary participation should continue for states: Ohio's public retirement systems are well-established and well-respected throughout the nation. The two largest systems, the Public Employees Retirement System (1933) and the State Teachers Retirement System (1920), predate Social Security as do many local police and fire pension funds prior to their consolidation into the statewide Ohio Police and Fire Pension Fund in 1967. Consequently, Ohio's public retirement systems have historically provided substantial retirement, disability, survivor and health care coverage to members and their families.

When the Social Security Act was adopted by Congress in 1935, state and local government employees were excluded from coverage. During the 1950's, Congress enacted several pieces of legislation making state and local government employees eligible for Social Security coverage for the first time, provided the state entered into a voluntary agreement with the Social Security Administration. History has shown that the principal reasons why various states entered into these agreements were that no retirement coverage previously existed, the retirement system was financially unsound, or the retirement benefits were totally inadequate. States had the option to terminate these agreements up until 1983 when Congress, in the face of several states seeking to withdraw from Social Security, unilaterally decided to make these pre-1983 agreements permanent as part of an effort to save Social Security from impending financial insolvency. In 1990 Congress continued its pursuit by mandating Social Security coverage for state and local government employees not covered by a public employee retirement system. Many states, including Ohio, responded by amending their plans to mandate coverage for all part-time and seasonal employees who had previously elected to exempt themselves from coverage.

Proposals that seek mandatory Social Security coverage for state and local government employees simply continue this historic and expedient pattern of generating additional revenues for Social Security in the short-term without recognizing the concurrent creation of additional long-term liabilities to Social Security and without addressing the inherent problems with pay-as-you-go financing of these liabilities. Social Security's history shows that the short-term gains resulting from adding more participants to Social Security have failed to solve the long-term funding problems resulting from pay-as-you-go financing of these future liabilities. Moreover, these proposals ignore the negative impact upon the financial stability of public employee retirement systems and the financial security of public employees and their families.

ORSC Position – At its meeting of October 12, 2005, the Ohio Retirement Study Council voted to recommend that the 126th General Assembly approve H.C.R. 20.