New Mexico's Amazingly-Generous Government Employee Pension Deal: A Case Study

By Paul J. Gessing

Introduction

Lobbyists for government workers regularly claim that government employment is no more generous than equivalent work in the private sector.[1] While this may be true if we only compare salaries, there is no comparison between the benefits packages provided to public workers and those available in the private sector.

Unlike the "defined contribution" retirement plans available in the private sector, government workers in New Mexico are given "defined benefit" plans that place the risk on taxpayers and guarantee workers a 3 percent annual cost of living increase regardless of market or cost of living realities.

The following information and spreadsheet shows an example of the PERA payouts for an actual case. We believe that the case represents an abuse of taxpayers and illustrates the unsustainable nature of New Mexico's public employee pension system.

This situation is perfectly legal and we do not assert any wrongdoing. In fact, a professional financial planner would be professionally obligated to explain to their client – the recipient – that these generous benefits are indeed available to them. It is up to policymakers to change the law to make sure that reasonable benefits are available for government workers and that the system can be sustained in the future.

It should be noted that we at the Rio Grande Foundation do indeed appreciate the efforts of fire fighters and police and the fact that they put themselves in danger for our benefit. This sacrifice does merit shorter service terms and somewhat more generous retirement benefits than their desk-bound brethren (in both the public and private sectors). However, the fact remains that taxpayers have a limited ability to pay these benefits and it should be noted that fire fighters and police choose their work in a free marketplace knowing the dangers they might experience on the job.

Finally, by way of background, it is worth noting that fire fighters and police *do not* have the most dangerous jobs in America (at least in terms of fatalities per 100,000). According to a report from *BusinessInsider.com* that relies on data from the Bureau of Labor Statistics, the most dangerous job in America is fisherman, followed by logger, aircraft pilot, and farmer (to name

[1] Carter Bundy, "Apples to Apples, Public Workers Make Less," *NMPolitics.net*, January 27, 2011, http://www.nmpolitics.net/index/2011/01/apples-to-apples-public-workers-make-less/.

just a few of the most dangerous jobs). Police officer is tied for 10th in the report and fire fighter ranks 13th.[2]

Background on New Mexico's Pension Problems

All states have significant pension liability issues. Part of this has been driven by the political considerations of politicians who would rather offer more generous pensions (to be paid by their successors and future generations of taxpayers) and part of this has been driven by generous GASB standards that allow states to assume an 8 percent rate of return on pension fund investments. Other factors certainly come into play, but these are two of the big ones.[3]

According to Rio Grande Foundation pension analyst Scott Moody, "New Mexico's defined benefit retirement system is massively underfunded. The pension system reports an unfunded liability of $4.6 billion; however, new analysis finds that the pension system is underfunded by at least $7.5 billion and may be as high as $22.9 billion—or three times greater than the state's general obligation bond debt.[4]"

The varying calculations are based on varying discount rate assumptions with the 8 percent rate of return seen as massively unrealistic. Thus, over time, New Mexico taxpayers will be forced to pay an additional $4.6 billion at minimum and as much as $22.9 billion to make good on the obligations of New Mexico's government pensions. Given the nation's grim economic outlook and elevated unemployment rate, it seems likely the situation will only worsen.

In addition to the general problems with government pensions as mentioned above, the policymakers who have created these pension systems have often created glaring loopholes that make the pensions incredibly generous. One such example is the basis for our pension case study below. We believe that the case shows that government worker pensions are far out of line with anything in the private sector, but more importantly, that unique features of government pensions make them completely unsustainable in the future.

Hopefully, policymakers will consider eliminating this and other similar loopholes, but we reiterate that the generous and guaranteed natures of government pensions are unsustainable.

Pension Case Study

A municipal firefighter born in 1949 was 60 yrs old when he retired last year. We don't know how long he worked there (probably 20 years), but it was his second career because he had another pension coming in from another government employer. He also will receive some kind of retirement payment from Social Security although the specific numbers and details are not known in this case.

---

[2] *BusinessInsider.com*, "The Most Dangerous Jobs in America 2010," http://www.businessinsider.com/the-15-most-dangerous-jobs-in-america-2010-3#.

[3] Dunstan McNichol, "States Face Pension Stress as GASB Rules Widen Gap," July 9, 2010, http://www.businessweek.com/news/2010-07-09/states-face-pension-stress-as-gasb-rules-widen-gap.html.

[4] J. Scott Moody and Wendy P. Warcholik, Ph.D, "Understanding New Mexico's Unfunded Pension Liabilities," January, 2010, http://www.riograndefoundation.org/downloads/rgf_ual_2.pdf.

His *annual* pension payout starting this year would be $73,200 as a single pension beneficiary. This kind of guaranteed annual income in retirement is nearly unheard of outside of government.

Given PERA's 3 percent annual Cost of Living Adjustment (COLA), his annual pension will rise by at least 3 percent as long as he lives. That is a pretty good deal, right? The New Mexico House attempted to reduce this generous, guaranteed COLA for non-public safety workers in HB 644, but the measure was not taken up in the Senate and thus remains in place for both types of workers under PERA.[5]

But, under New Mexico's pension rules (he chose to do this because he was divorced), he was able to make his granddaughter (born in 2003) his Joint with 100% payout beneficiary. Because of this shift, he would *only* receive $55,200 per year from his pension. After 2 years, this amount will increase by 3% annually and will be paid to his granddaughter *until she dies*.

The Pension is determined by the following formula: **number of years' service x a pension factor x your average monthly pay during your highest 3 year pay period**. This amount is then adjusted up by 3% per year after 2 full years of retirement.

The header "Single Pension" on Chart 1 shows the retiree's "single pension" if he were to hang onto the pension himself. Were he to live to 80 years old, his annual pension payout will be more than $132,000 annually when he dies. From now until his 80th birthday, he'll rake in an astonishing $1,729,723! Good luck finding that deal in the private sector.

Even more astonishing is the ability to pass this benefit along to his four year old granddaughter by naming her a "Joint Beneficiary." This is perfectly legal under current law. And, while the immediate payout is reduced somewhat, the total burden to taxpayers escalates dramatically.

This scenario is outlined in the "Joint Life Pension" column of Chart 1. By her 21st birthday, assuming that her grandpa has died and that she is the beneficiary, she'll be receiving an annual "pension" exceeding $88,000 annually. By the time she hits her 40s, she'll be receiving $150,000 annually, and by the time she is ready for retirement, her grandfather's very generous pension – assuming the taxpayers can still foot the bill – will be paying her an astonishing $300,000 annually.

Assuming that her grandpa dies at 75 and she lives to the age of 80, taxpayers will shell out a positively mind-boggling **$14.5 million** in payments over her lifetime. To say that this is unsustainable is a dramatic understatement.

Chart 1.

		Retiree's Age	Granddaughter Age	Year	Joint Life Pension	Single Pension
COLA	**3.00%**	60	4	1	$55,200.00	$73,200.00
monthly payment	***$4,600.00***	61	5	2	$55,200.00	$73,200.00
annual	**$55,200.00**	62	6	3	$56,856.00	$75,396.00

[5] Rep. Bill O'Neill, "Pension Reform Right Thing to Do," *NMPolitics.net*, March 25, 2011, http://www.nmpolitics.net/index/2011/03/pension-reform-is-the-right-thing-to-do/.

payment						
		63	7	4	$58,561.68	$77,657.88
monthly payment	***$6,100.00***	64	8	5	$60,318.53	$79,987.62
annual payment	**$73,200.00**	65	9	6	$62,128.09	$82,387.24
		66	10	7	$63,991.93	$84,858.86
monthly dif.	**$1,500.00**	67	11	8	$65,911.69	$87,404.63
		68	12	9	$67,889.04	$90,026.77
Insurance DB	**$1,252,000.00**	69	13	10	$69,925.71	$92,727.57
		70	14	11	$72,023.48	$95,509.40
Investment ROR	***5.00%***	71	15	12	$74,184.18	$98,374.68
		72	16	13	$76,409.71	$101,325.92
Final Salary:	**$92,000**	73	17	14	$78,702.00	$104,365.70
80% pension		74	18	15	$81,063.06	$107,496.67
		75	19	16	$83,494.95	$110,721.57
		76	20	17	$85,999.80	$114,043.21
		77	21	18	$88,579.80	$117,464.51
		78	22	19	$91,237.19	$120,988.45
		79	23	20	$93,974.30	$124,618.10
		80	24	21	$96,793.53	$128,356.64
			25	22	$99,697.34	$132,207.34
			26	23	$102,688.26	$136,173.56
			27	24	$105,768.91	$140,258.77
			28	25	$108,941.98	$144,466.53
			29	26	$112,210.23	$148,800.53
			30	27	$115,576.54	$153,264.54
			31	28	$119,043.84	$157,862.48
			32	29	$122,615.15	$162,598.36
			33	30	$126,293.61	$167,476.31
			34	31	$130,082.42	$172,500.60
			35	32	$133,984.89	$177,675.61
			36	33	$138,004.44	$183,005.88
			37	34	$142,144.57	$188,496.06
			38	35	$146,408.91	$194,150.94
			39	36	$150,801.17	$199,975.47
			40	37	$155,325.21	$205,974.73
			41	38	$159,984.96	$212,153.97
			42	39	$164,784.51	$218,518.59
			43	40	$169,728.05	$225,074.15
			44	41	$174,819.89	$231,826.38
			45	42	$180,064.49	$238,781.17
			46	43	$185,466.42	$245,944.60
			47	44	$191,030.41	$253,322.94
			48	45	$196,761.33	$260,922.63
			49	46	$202,664.17	$268,750.31
			50	47	$208,744.09	$276,812.82
			51	48	$215,006.41	$285,117.20
			52	49	$221,456.61	$293,670.72
			53	50	$228,100.30	$302,480.84
			54	51	$234,943.31	$311,555.26
			55	52	$241,991.61	$320,901.92
			56	53	$249,251.36	$330,528.98
			57	54	$256,728.90	$340,444.85
			58	55	$264,430.77	$350,658.19
			59	56	$272,363.69	$361,177.94
			60	57	$280,534.60	$372,013.28
			61	58	$288,950.64	$383,173.68
			62	59	$297,619.16	$394,668.89

	63	60	$306,547.73	$406,508.95
	64	61	$315,744.17	$418,704.22
	65	62	$325,216.49	$431,265.35
	66	63	$334,972.99	$444,203.31
	67	64	$345,022.18	$457,529.41
	68	65	$355,372.84	$471,255.29
	69	66	$366,034.03	$485,392.95
	70	67	$377,015.05	$499,954.74
	71	68	$388,325.50	$514,953.38
	72	69	$399,975.26	$530,401.98
	73	70	$411,974.52	$546,314.04
	74	71	$424,333.76	$562,703.46
	75	72	$437,063.77	$579,584.56
	76	73	$450,175.68	$596,972.10
	77	74	$463,680.95	$614,881.26
	78	75	$477,591.38	$633,327.70
	79	76	$491,919.12	$652,327.53
	80	77	$506,676.70	$671,897.36
	81	78	$521,877.00	$692,054.28
	82	79	$537,533.31	$712,815.91
	83	80	$553,659.31	$734,200.39
	84	81	$570,269.09	$756,226.40
	85	82	$587,377.16	$778,913.19
	86	83	$604,998.47	$802,280.58
	87	84	$623,148.43	$826,349.00
	88	85	$641,842.88	$851,139.47
	89	86	$661,098.17	$876,673.66
	90	87	$680,931.11	$902,973.87
	91	88	$701,359.05	$930,063.08
	92	89	$722,399.82	$957,964.97
	93	90	$744,071.81	$986,703.92

The aforementioned chart and astonishing pension payment generosity should be troubling enough to taxpayers and policymakers. But, the Legislature has continued to open the government pension plan to ever-greater numbers of potential beneficiaries.

For starters, the granddaughter in this example could – if she felt the need to work given this massive, unearned pension benefit – become the ultimate double-dipper if she works for the government. This would lead to her having a generous government pension (on top of the pension provided by her grandfather) someday.

In addition, according to a PERA handbook: "State General members can retire at **ANY** age with 75 percent of their Final Average Salary after 25 years of service or 80 percent of their final annual salary as after working 26 years and 8 months.[6] Some municipal police and fire plans offer retirement after 20 years of credit." This does not prevent people from retiring with less years of service and receiving '*reduced'* benefits based on the formula above.[7]

After 5 years of service, many employees can actually 'purchase' service credit to artificially increase their years' service factor! Anyone with 5 years of government service can receive a

[6] Public Employees Retirement Association of New Mexico, "PERA Member Handbook," September 2010.
[7] *Ibid.*

pension after age 65. Generally, the more years of service you have, the earlier you can start receiving your pension.

Conclusion

New Mexico taxpayers face a looming public pension crisis. First and foremost, policymakers need to close gaping loopholes like those that allow a pension to be passed on to a recipient's grandchild.

Ultimately, however, New Mexico will have to join Michigan, Alaska, and the District of Columbia in offering public workers defined contribution rather than defined benefit retirement plans.[8] Taxpayers simply cannot be placed on the hook as guarantors of ever-increasing annual pension payouts that rise regardless of investment performance.

[8] Scott Moody, "New Mexico's Public Sector Work Force is Unsustainable," http://www.riograndefoundation.org/downloads/rgf_nm_public_sector.pdf.