

RETIREMENT SYSTEMS FOR PUBLIC EMPLOYEES IN NEW YORK STATE

BY

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Prior to the year 1917, there was no pension plan of importance for any class of public employees in the State of New York which was on a sound financial basis. Many plans were in operation and not a few had come to the point where it was evident that they would soon have to reorganize or cease to pay retirement benefits. Within a period of four years, four retirement systems were organized, each of which covers larger classes of public employees than had previously been covered and each of which, it is believed, is organized on a sound financial basis.

It is the purpose of this paper to compare similar provisions of these four large retirement systems, to discuss some of the problems which have arisen in the administration of these systems and to present for discussion in the light of the experience of these four systems, the advisability or inadvisability of certain types of provisions in retirement systems for public employees.

The names of the retirement systems in question are listed below together with the date of organization of each and the number of members in 1925. Opposite the name of each system is given a letter by which the system will be designated in the remainder of this paper.

FOUR LEADING RETIREMENT SYSTEMS FOR PUBLIC EMPLOYEES IN NEW YORK STATE

Name	Year Organized	Number of Members in 1925	Letter to designate system
Teachers Retirement System of the City of N. Y.....	1917	25,649	A
N. Y. City Employees Retirement System	1920	29,928	B
N. Y. State Employees Retirement Sys- tem.....	1921	17,402	C
N. Y. State Teachers Retirement System..	1921	29,057	D

A word of explanation is in order regarding the membership of these systems. The membership of system A is properly

described by the name of the system. System B does not include teachers, policemen, firemen and street cleaners of the City of New York; otherwise it includes all but comparatively small classes of public employees of the City. System C originally included state employees only. By amendment it has come to include large groups of employees of cities, counties, towns and villages and provision is made whereby a municipality whose employees are not now members of, or entitled to membership in, a retirement system supported in whole or in part by the State or the municipality, may arrange to make its employees eligible to membership in system C. System D is open to all public school teachers of the State with the exception of those in New York City.

MANAGEMENT

Systems A and D are managed by retirement boards organized for this particular purpose. System B is managed by the Board of Estimate and Apportionment of the City of New York. This board has many duties of an entirely different nature in connection with the administration of the government of the City of New York. The affairs of the retirement system are apt to be only incidental in the voluminous calendar of each meeting of the board. System C is managed by the Comptroller of the State of New York. Here again the management of the system is only incidental among the duties of the responsible head. Each of the four systems is by law given the powers and privileges of a corporation. None of them is a department or division of state or city government.

BENEFITS AND CONTRIBUTIONS

Each of these systems provides a superannuation benefit, sometimes called a service benefit, and a disability benefit. All but system D provide a death benefit. The superannuation benefit is of most importance and will be considered first. Although this benefit differs in different systems, it is such in each that an employee who has from 30 to 35 years of creditable service may expect to be able to retire on something near half pay. Furthermore, all systems require contributions from members and a member who begins his service after the system is established and who serves during a period of from 30 to 35

years, may expect his contributions to furnish about half of his retirement allowance. In each system, deductions from salaries of members are accumulated at 4% interest as savings accounts and the amount in an individual member's account is available in case of his resignation, dismissal or death.

When an employee is retired for superannuation in any one of the four systems, a pension is payable which depends upon the number of years of service as a member, the number of years of creditable service before the system was organized, and upon the salary during the last five or ten years of service. The amount of the pension does not depend explicitly upon the age of the pensioner. In addition to this pension, the service pensioner receives whatever annuity can be purchased with his accumulated salary deductions.

Each of the systems gives credit for service prior to the organization of the system. To state in detail just what prior service is creditable would not be profitable in this paper. With certain important exceptions, creditable service is limited to such service as would entitle an employee to membership in the system if rendered after the system was organized.

With minor exceptions, credit for prior service is dependent upon continuous membership in the system. In other words, if a member with prior service credit discontinues membership in a retirement system, as a result of a change of occupation or otherwise, and later returns to membership, he is classed as a new entrant and has only the credit available to those who entered the service after the system was organized. In this paper, those with full prior service credit will be called present employees and all others will be called new entrants.

It should be apparent from the foregoing paragraphs that the general scheme of the four systems is the same so far as service retirement allowances are concerned. Differences will now be taken up in the conditions for retirement, in the method of determining the pension portion of the retirement allowance and in the amount of the contributions of members. It should be stated at this point that comparatively minor exceptions to general provisions are omitted in this paper and as a result, some of the statements, especially with regard to service requirements and retirement benefits, may not be strictly true in every individual case.

System A provides for service retirement upon attainment of age 65 or upon the completion of 35 years of service. System B has three classes of employees; laborers, mechanics and clerical employees. Members of these classes were originally eligible for retirement at ages 58, 59 and 60 respectively. By amendment each of these retirement ages was reduced by five years. System C provides retirement at age 60 while system D requires 35 years of service or the attainment of age 60 with twenty-five years of service.

Originally systems A, B and C required retirement at age 70 while system D has had no compulsory retirement age. System A has retained this requirement; systems B and C have modified their requirements so as to permit an employee beyond age 70 to continue in service under certain conditions which involve medical examination of the employee and approval of the immediate employer.

In each system, the pension benefit is proportional to the average salary for the last five or ten years of service; this is called in this paper, the final average salary. In systems A and B, the final average salary was originally the average for the last ten years; this has been changed in both systems to the average for the last five years. In systems C and D, the average has always been for the last five years.

In many respects systems B and C are very much alike. As stated above, system B has three classes of employees; the statements which follow regarding system B apply to clerical employees, *i. e.*, to the class whose members may under the amendment retire at age 55. Upon service retirement, systems B and C provide a pension of 1/140 of final average salary for each year of service since last becoming a member and 2/140 for each year of creditable prior service, (*i. e.*, creditable service prior to the organization of the system).

Systems A and D provide a pension of one-quarter of final average salary and, to present employees, an additional pension of 1/140 of final average salary for each year of creditable prior service.

Each system provides a disability benefit in case medical examination discloses that the employee is sufficiently disabled as to be unable to perform his duties. The management of each system has discretionary powers of importance regarding such

retirements. Each system requires a certain number of years service before an ordinary disability benefit is available. Systems A and B require ten years service while systems C and D require fifteen years.

Systems B and C provide special disability benefits for disability caused by accident sustained in the performance of duty. These benefits are quite liberal and are available regardless of the period of service. Systems A, B and C provide explicit death benefits. In system A, this benefit is available only to those eligible for service retirement and is equivalent to the last six months salary preceding death. System B provides the same benefit but it is available to all members. System C, by amendment in 1926, provides one-twelfth of the compensation earnable during the twelve months immediately preceding death for each year of service, but not to exceed half of such compensation. It should be added that accumulated contributions of members are returned in case of death, in addition to the benefits described above.

Systems B and C provide special benefits in case of death due to accident sustained in the performance of duty, the benefits taking the form of payment of accumulated contributions and a pension of half of final average salary to designated beneficiaries.

Options

Under each of the four systems, upon retirement for either service or disability, the pensioner has the option of choosing, instead of the retirement allowance calculated to be paid during his lifetime, a smaller allowance to be paid during his lifetime with the agreement that this is to be followed upon his death by further regular payments or by a lump sum payment to a designated beneficiary. On the basis of mortality tables adopted by the retirement system, the various optional modifications available are, of course, actuarially equivalent to the maximum retirement allowance at the time of retirement. It should be noted, however, that in every case the member has the right to choose an option at the time of retirement. The experience of the retirement systems here discussed, during the few years which have elapsed since their organization, shows clearly that the privilege of choosing options has resulted in selection against the systems. Many cases are on record which show the choice

of an option because the prospective pensioner felt that death was imminent. In fact, it is clearly established that in many cases, those in charge of the retirement systems have advised that options be chosen in cases where the retiring member seemed to have very little chance of living any length of time.

Selection against the systems is most apt to occur in case of retirement for disability. Probably in the majority of cases of service retirement, the member is in normal health and if so, the choice of an option should not, on the average, place extra burdens on the system. In case of disability retirement, on the other hand, the member is not in normal health and being thus on guard against the possibility of early death, it is probable that those who choose options will show heavier mortality than do those who might be termed normal disabled lives.

All four of these systems have had to deal with what have come to be known as death-bed retirements with choice of options. Systems B, C and D have protected themselves to a large extent by provisions of law which enable them to require that, in case an option is chosen, the retiring member must live thirty days after application for retirement in order that the payments under the option shall be made. System A has no such provision and has paid over a million dollars in optional settlements in cases where the retiring members died shortly after retiring.

Discontinuance Benefit

Systems B and C provide retirement benefits for those who meet special service requirements and whose services have been discontinued through no fault of their own. This includes persons who are thrown out of the public service because of changes in political control or because the positions which they occupy have been discontinued. System C has a particularly liberal benefit of this type which may result in pensioning persons at ages as low as forty years merely because they have lost their positions in the public service. There are those who feel that this is a most flagrant perversion of the purposes for which retirement systems are organized and that it shows what dangers are involved when a legislative body can change a retirement system at will.

Accrued Liability

It should be clear from the foregoing paragraphs that the basic unit in calculating the employer's liability is a year of service. In each system, the employer's liability for service prior to membership is thought of as accrued when membership begins. It is recognized in each case, however, that it is neither practicable nor necessary to fund this liability at once and different plans have been adopted in the different systems to spread the burden of building up this fund over a period of years.

System A requires an annual appropriation of one million dollars to support the accrued liability and provides that in case this is insufficient, the remainder needed shall be furnished year by year on the cash disbursement plan. System B requires the annual appropriation of 6% of the accrued liability as of the date when the system began operations. System D collected for the support of the accrued liability, 2.5% of the salaries of members during the first year of operation and 2.5% of the salaries of all eligible teachers whether members or not, for the following four years. The law provides that after the actuarial valuation as of July 31, 1925, a contribution rate shall be determined which will furnish a contribution equal to 4% of the present value of the liability in question at that time. This rate is to be used thereafter and since it applies to the salaries of all members, it will yield an increasing contribution to support the accrued liability. System C uses a method similar to that of system D.

Although the idea of an accrued liability has been useful in impressing upon employers the seriousness of a pension plan, it is submitted that this idea has been misleading in many cases. Incidentally it has led to the charge that until this liability is funded, a retirement system is insolvent. The process of funding, in practically every case introduces elements which are obviously arbitrary and which lead to a lack of continuity in the contribution rates of employers. If, instead of considering any liability as accrued when the system begins, the contribution of the employer were calculated for each member as a level premium to be paid during the remainder of the period of service before eligibility for retirement, we would have the advantages that no liability is hypothecated when the system begins operations and that the employer's contributions change gradually from year to year. Under this method there would never be a time to look

forward to when the employer's contribution rate is to be suddenly decreased. The layman does not thoroughly understand this matter but he thinks he sees clearly that if such a time is going to come, as it will under the plans now in use, the contribution for each year preceding that time can be shaded by extending the period for the heavier contribution or by reducing the contribution rate gradually instead of suddenly.

SOUNDNESS OF FINANCIAL BASIS

There are two fundamentals which distinguish a retirement system which may be said to rest on a sound financial basis:

1. The prospective income of the system is so determined as to be able to support the promised benefits.
2. The sources of income are reliable.

Each of the four systems here discussed provides for revision of contribution rates in case experience demonstrates that the rates in use are too small or too large. Three of the four systems require that contributions on behalf of the employer shall be appropriated by legislative bodies while the fourth takes these contributions from the certain taxes collected for school purposes before distribution to school districts of the state. Each system provides that the employee's contributions shall operate as a savings account so that no complications are here involved. Anyone of these systems can be wrecked by legislation. Three of them can be wrecked by failure of legislative bodies to appropriate funds. The likelihood of such action is a matter of opinion but an important element of safety is the power of the members over legislative bodies through their votes. On the other hand, each of these systems has felt the pressure of efforts to liberalize benefits without regard to cost. Furthermore, liberalizations which have cost millions of dollars to the employers have been made. There is very serious fear on the part of many whose interests are completely centered in the welfare and permanency of this type of retirement system, that excessive liberalizations of benefits may cause the method to fail, through refusal or impossibility to appropriate sufficient funds to maintain the systems.

It should be stated that while this paper was in preparation, a legal decision was handed down which will apparently have

an important effect upon the operations of system B. Supreme Court Justice M. Proskauer handed down a decision to the effect that amendments to the law of system B which had been enacted by the Municipal Assembly of the City of New York are void. The principal amendments in question resulted in lowering the retirement age by five years, in making final average salary the average of the last five years instead of the last ten years salary and in allowing prior service credit regardless of date of joining the retirement system in case the member in question has fifteen years or more of prior service. It will be readily seen that this is a very serious matter to many individuals. A number of retirement allowances will be discontinued as a result of this decision and the status of the corresponding pensioners will be questionable. Retirement allowances have been determined recently on the basis of salaries for the last five years of service and in those cases where a pensioner was eligible to retirement under the law as it read before amendment, the final average salary will apparently have to be changed with a consequent change in the retirement allowances.

The Court's opinion in this case points out that the Municipal Assembly is specifically prohibited by the Home Rule Law from adopting a local law to supersede a state statute if such local law "applies to or affects any provision of law relating to the property, affairs or government of a county or counties." It then points out that some of the members of the Retirement System are County or State employees paid by the City as agent for the County or State. An appeal has been taken from this decision to the Appellate Division of the Supreme Court but as yet no decision has been rendered by that Court. If, after these adjustments are made, the decision above mentioned should be reversed, the procedure will apparently be changed again in accordance with the later decision.

QUESTIONS SUGGESTED BY THE FOREGOING ANALYSIS

It is proposed to discuss to some extent a number of questions regarding retirement systems for public employees in general, the questions being the outgrowth of the experience of the four systems described in the earlier part of this paper. It is hoped that this may lead to expression of opinion which may be helpful in guiding some retirement systems in the future.

Benefits

What benefits should be provided by retirement systems for public employees?

At a time when retirement systems are rapidly becoming more popular, not only for public employees but for industrial employees as well, it would probably be useless to discuss the question of whether or not any retirement system for public employees is justifiable. Assuming that we should have such organizations, however, there is a wide difference of opinion as to what benefits should be provided. There are those who feel that the most that should be included is an annuity benefit to superannuated employees. Others would include besides the superannuation benefit, a benefit for disability not caused by accident in the performance of duty, a more liberal disability benefit in case of accident, a sickness benefit, a death benefit and an unemployment benefit. Furthermore, there is a wide difference of opinion as to how large these benefits should be and as to how they should be supported.

None of the financially sound retirement systems for public employees in New York State provides a sickness benefit as such. However, disability is not sharply defined and considerable discretion is exercised in deciding as to disability retirement. Probably no system would claim to offer an unemployment benefit but the discontinuance benefits of systems B and C might well be described as unemployment benefits.

There has been considerable discussion of the question of whether or not a death benefit is appropriate. Opinion on this question seems to turn on the purpose for which the retirement system is conceived. There is the point of view that the employer has a certain responsibility with respect to the employee which he does not have with respect to the dependents of the employee. In fact, it is held by some that the employer is not interested in the domestic affairs of the employee; that any responsibility which the employee may undertake regarding others is no affair of the employer. This argument is used to support the conclusion that a death benefit has no place in a retirement system.

On the other hand, there is the view that the reason for the existence of a retirement system is the benefit to society which is involved in its operation; that a death benefit will frequently enable a family to avoid abject poverty and that society in

general will thus avoid the loss consequent upon the ill fortunes of some of its members. This is, of course, one of the fundamental arguments for life insurance, and death benefits of a retirement system may well be considered as group life insurance for the employees involved. Possibly the most generally accepted purpose of a retirement system is to improve the service of the employees. From this point of view, it is difficult for some to see that the death benefit is of value.

It is of interest that only two of the four systems discussed in this paper, systems A and B, provided explicit death benefits from the beginning and that system C introduced the death benefit only after five years of operation. Yet all of these systems have offered options at the time of retirement and these options frequently result in death benefits of much larger value than any of the explicit death benefits. It seems queer that the theoretical value of a death benefit should be so solemnly questioned when considered in connection with retirement systems which already allow a broad choice of options upon retirement. It is true that the death benefits are available only before retirement, while optional benefits are available only after retirement so that to some extent they supplement each other.

Assuming that death benefits are desirable, question has been raised as to whether or not they should be, as they are, in the form of lump sum settlements. Only the accidental death benefits of systems B and C are in the form of annuity payments. There is also question as to whether or not optional benefits should be available upon retirement. This is questioned especially in connection with disability retirements. A strong argument for the choice of an option upon retirement is that a member can, at that time, make a choice of benefits more suitable to his circumstances than could be made earlier. If he has no dependents, he will want the maximum annuity for life; if he has a wife, he may want the benefit continued in whole or in part during the life of his wife after his death. From this point of view, permission to choose an option upon retirement is most valuable in obtaining the greatest good from a retirement system. The point which is overlooked entirely is that permission so to choose allows full play to the human tendency to select against the retirement system in case of ill health. This shows up especially in cases of disability retirement.

Probably the most popular optional benefit is the one designated as option number one in each of the four systems. It consists of a lump sum payment to a designated beneficiary or to the estate, upon the death of the pensioner, of that part of the reserve for the retirement allowance at the time of retirement which has not been consumed in payments to the pensioner. There are those who feel that this option should not exist while others would make it compulsory for all members with dependents. It is not clear that the beneficiary is helped as much by a lump sum settlement as she would be by a continuation of the pension payments. It is also held that some of the questionable methods which have been employed to obtain the benefits of option number one would not be used to get the less alluring but possibly more valuable benefits consisting of a continuation of the original pension.

It is futile to theorize regarding benefits desirable for retirement systems without considering the cost. Probably the most fundamental difference between the four systems here discussed and the systems which preceded them is that a more serious effort has been made in case of each of the four systems to anticipate the cost of the benefits promised and to provide income sufficient to support these benefits from sources as nearly unquestionable as it was possible to devise. There are those in pension circles who are anxious regarding the various liberalizations of benefits for fear that the time will come when legislative bodies will fail to appropriate the funds necessary to meet the obligations. On the other hand, there are those who are interested in liberalizing the benefits apparently without regard to the cost, seemingly taking the attitude that the sources of public funds are unlimited.

In this connection, one must not lose sight of the fact that practically all public employees have votes in political elections and that their interests affect the votes of many others. This fact is reflected in the widespread tendency to attempt to broaden the benefits of retirement systems without increasing the contributions of the employees.

Flexibility

Each of the four systems has fixed conditions for retirement. With few exceptions a minimum age, usually 60 years, is set for superannuation retirement. We frequently hear the opinion

expressed that age 60 is too early for retirement. Yet we all recognize that some employees are superannuated at age 55 while others are as valuable as ever if not more valuable than ever at age 65. None of these systems allows a variation of the minimum requirements under any circumstances.

In each system, disability benefits are available in case the applicant has credit for a specific amount of service, either 10 or 15 years. If 15 years is required, no power exists to allow a benefit in case only 14 years credit is available.

System D will retire an employee of age 60 if he has 25 years of service but will not retire an employee of age 69 unless he has 25 years of service; yet there is little question that for the good of the service, many of those between ages 60 and 70 with less than 25 years service should be retired. At the other extreme, 35 years of service entitles one to retirement regardless of age.

System C requires for service retirement that application be made within 15 days after leaving the service; system D requires that the employee shall be a teacher during the year preceding application for retirement. Each system is required to issue prior service certificates and if these have been in effect one year, they can be changed only by discovery by the retirement system of error or fraud.

These facts are stated to show a lack of flexibility in the retirement systems and as a preface to the question as to whether or not any more flexibility would be advisable. Should the management of a retirement system or a medical board have any discretion as to the minimum conditions for either service or disability retirement? Should a person who has fulfilled the service requirements for retirement be in any danger of losing his right to retire by delaying his application a week or a year or should this right be one which he can exercise at any time?

Should a retirement system make superannuation retirement depend upon amount of service as well as age or does this tend to counteract the very purpose of the system? It is suggested for consideration that a retirement system should not have a service requirement for retirement and that the portion of a retirement allowance furnished by the employer to new entrants should be proportional to the amount of service. This is the plan of systems B and C. Where possible, benefits should change

gradually with service rather than to change suddenly from zero to a substantial amount.

These are only a few of the many seemingly arbitrary provisions of the different retirement system laws which cause much trouble in administration. If fifteen years service is necessary for disability retirement, it is only a question of time until the case will turn up where fourteen years service is established and every effort will be made to find another year, often by "interpretation" of the law. If the year cannot be found, the disabled employee will be kept on the payroll, receiving full pay although unable to work, thus practically liberalizing the disability benefit by preceding the legal benefit by an indefinite sick leave at full pay.

Should more than one benefit be available to a member at a given time? For instance if an employee eligible for service retirement is suddenly taken ill and the physician says he can live only a short time, it may at present be advisable for the prospective beneficiary to have computed for comparison the disability benefit with choice of option number one, the service retirement benefit with choice of option, and the death benefit without retirement. Should such a condition exist if it can be avoided?

If application for service or disability retirement must be made within a specified time after having left the service, distressing cases will immediately turn up where, through ignorance, neglect or hope of returning to service, this requirement will not have been fulfilled. If disability retirement with choice of option gives the possibility of a large benefit upon the death of the prospective pensioner, cases will be numerous where questions must be settled as to the authenticity of a signature or of a "mark" or as to whether or not a specified time elapsed between the time of application for disability retirement and the time of death of the applicant.

Apparently many of the difficulties which have developed in the operation of these retirement systems are due to the fact that we have not had much experience along this line. The solutions of many of these difficulties are not easy and it would seem that these are properly problems for the consideration of members of this Society. It should be stated that some of the seemingly arbitrary provisions in the laws of the retirement systems were put there deliberately for particular purposes; not

infrequently, however, they operate otherwise than was apparently intended.

In all insurance work, "close cases" are sure to appear but the companies have long since learned to write their contracts in such a manner as to minimize the possibility of misunderstanding and to eliminate as much as possible in the way of arbitrary conditions. Doubtless, when we have had experience for three-quarters of a century with retirement systems, many of the difficulties which we now experience will be ironed out. It is believed that the members of this Society are by training and occupation qualified to make suggestions from which retirement systems should be able to profit.