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Arizona's Deepening Public-Pension Quagmire.

Reform efforts and an ongoing court case show what happens when the bills come in for overly generous retirement programs.

Illinois' and New Jersey's public pensions may be in worse shape, but Arizona takes a backseat to no one when it comes to pension intrigue. A case before the state's Supreme Court is highlighting that intrigue as well as some of the basic decisions state and local governments face as they grapple with the sustainability of their retirement systems.

In 2011, Arizona enacted reforms to its Public Safety Personnel Retirement System (PSPRS), which at the time also included the Elected Officials Retirement Plan (EORP). The changes required active employees to contribute more toward retirement, suspended retirees' cost-of-living adjustments (COLAs) and conditioned future benefit increases on the fund's financial health. As a result, police and firefighter contributions increased from 7.65 percent of salary to 11.65 percent and about 200 judges saw their retirement contributions jump from 7 percent of salary to 13 percent.

A 2014 state Supreme Court ruling restored retiree COLAs, which added \$1.5 billion to the system's unfunded liability. Now a case brought by two active judges challenging the increased employee contributions has made its way to Arizona's Supreme Court after a lower court ruled that the state must refund the increased contributions. The refunds would cost about \$175 million.

Here's where things start to get particularly interesting. While the judges' case is before the Supreme Court, that's not exactly who will be hearing it. Four out of the five justices recused themselves because they would benefit from any refund. The fifth, Justice Clint Bolick, was appointed after the EORP was closed to new members in 2014, so he will be part of a special five-judge panel that will hear the case. And since the EORP was part of the Public Safety Personnel Retirement System, the panel's ruling will also affect police and firefighters.

The Arizona pension quagmire is further complicated by a voter-approved 1998 state constitutional amendment saying that "public retirement benefits shall not be diminished or impaired." That provision is unusual but not unique among the states, and it's the basis of the lower court's ruling that the increased contributions must be refunded.

The EORP was shut down because it was so expensive. That's what happens with a system that allows members to retire after 20 years with full benefits. Fifteen percent of its retirees receive six-figure annual pensions, and the average annual benefit is north of \$50,000.

But two larger policy issues are at play in the Arizona pension case. One is that while it's certainly tempting to push liabilities off into the future, taxpayers would be better served by a system that pays higher salaries when necessary rather than promising generous pension benefits that subsequent generations can't afford.

The second lesson is just as simple. If state and local governments are going to continue offering rich defined-benefit pensions, both employees and taxpayers had better be prepared to pay for them.

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