



Testimony Before the Joint Committee on Public Service Regarding the MBTA Retirement Fund

by Iliya Atanasov

February 25, 2014

Thank you, Chairman Brownsberger, Chairman Michlewitz and members of the Joint Committee on Public Service for engaging so relentlessly with an issue of tremendous significance to the welfare of the commonwealth.

My name is Iliya Atanasov. I am senior fellow on finance at Pioneer Institute.

The subject of this hearing is a matter of critical public interest because of the role of the MBTA in our economy and in the everyday lives of millions of Massachusetts residents.

Pioneer had warned about the potential impact of the festering governance issues at the MBTA Retirement Fund weeks before the \$25 million loss at Fletcher Asset Management was made public by the press:

The MBTA has been in the grips of a structural crisis for years, remaining in the top ranks for largest debt burden and highest cost of services rendered among similar agencies across the country. One of the root causes of this untenable situation is a poor level of transparency regarding its retirement plans, which had accumulated unfunded [liabilities] of about \$2.74 billion as of their last valuations.¹

The survival of the T is inexorably dependent on sales tax revenues, local assessments and direct assistance from the commonwealth. In fiscal 2013, it received well over \$1.1 billion in taxpayer support through these channels. This amount was almost double the MBTA's operating revenue of \$630 million, most of which also came out of taxpayers' pockets in the form of fees for tickets and passes.

In fiscal 2013, the MBTA recorded some \$830 million in total expenses on employee compensation and benefits. In other words, operating revenue

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alone would not have been enough to cover all employment costs, let alone operate the network or leave anything for long-overdue capital investments.

A complete breakdown of labor expenses is presented in Exhibit 1 of your handouts. Of the \$830 million in employee expenses in fiscal 2013, \$451 million were paid out in direct compensation. Pension costs arising from obligations to Social Security and the MBTA's retirement plans amounted to some \$141 million.

Last November, Pioneer's research alerted the public to the skyrocketing costs of the T's pension plans. In Exhibit 2, you can see that pension expenses have doubled in the past six fiscal years, surpassing one fifth of total payroll. Note that this amount does not include the Social Security payments and retiree healthcare benefit obligations.

Exhibit 3 puts these alarming trends into perspective. Since 2001, total wage costs have increased by about 50%. Meanwhile, total pension cost has jumped by a whopping 250%, to well over \$100 million. In other words, pension costs have been growing at five times the rate of wages. Such aberrant tendencies are unsustainable, especially in view of the fact that retiree health care is not being advance-funded at all.

One is then compelled to ask about what happened with the truth – the truth about who is responsible for the pension obligations and who has been misrepresenting this fact for many, many years, spinning a web of deceit and dishonesty.

The MBTA Retirement Fund is an offshoot of the pension agreement between the T and its unions. According to this agreement, three quarters of the increases in annual required contributions after fiscal 2007 must come from the MBTA – i.e., from the taxpayer money that keeps it running.

Exhibit 4 presents some data derived from the last valuation of the fund, which – you have guessed correctly – Pioneer did not obtain from the retirement board. As of that valuation, which was recorded at yearend 2011 but only finalized in June 2013, the

annual required contribution was determined to be close to \$77 million. That contribution was projected to increase by 4% annually through 2041.

Some 56% of the required contribution were slated towards retiring the unfunded liability of the MBTA retirement fund; only about 42% of the contribution arose from the newly earned benefits.

As of yearend 2011, the MBTA Retirement Fund had an unfunded liability of \$726 million. The T's share of that unfunded liability would amount to no less than \$545 million. Given the 30-year open funding schedule, the MBTA would have to contribute at least \$1.6 billion to see the unfunded liability extinguished through 2041. A breakdown of these payments by decade is presented in Exhibit 5.

There is much at stake here, but ultimately this is a matter of what is fair and just, of doing the right thing. Can our commonwealth, its residents and its elected leaders trust the MBTA Retirement Fund to know and do the right thing?

The fund's board consists of seven members, three of whom are formally appointed by the MBTA's employees to represent their interests. None of the employee representatives bring to the table prior experience in investment management. Moreover, their voting to keep the fund's records sealed casts serious doubt on whether they are truly looking out for the plan's members. I urge the T's employees to call their union leadership and ask them why James O'Brien, James Evers and James O'Connell are hiding information about the retirement fund's operations from the public, thereby also galvanizing public opinion against the union.

Even more befuddling is the behavior of the three so-called representatives of the MBTA and, supposedly, of the taxpayers who keep the transit authority solvent. Janice Loux, the retirement board chair, is an executive of Unite Here and a lifetime union organizer. Jonathan Davis is a longtime employee of the T, who most likely stands to collect a generous pension from the fund, and rose in the senior ranks

of the MBTA when the executive director of the fund, Michael Mulhern, led the authority. Darnell Williams, the third MBTA representative on the board, is a community organizer. None of them are known for substantial expertise in the field of investment management.

Katherine Hesse, the “honorary” member of the board who also stymied disclosure, is a partner at a law firm specializing in employee benefits and representing over 30 employee benefit trusts. She rounds out a board of seven on which four members, including the chairwoman, are lifetime union functionaries and another one is an employee of the T.

In light of these facts, one cannot help asking: Who at the MBTA retirement fund is to stand for the interests of the T’s riders and the commonwealth’s taxpayers?

It seems to have fallen upon the members of this panel to take that role.

If the MBTA Retirement Board members appointed from the quota of the T know right from wrong and are determined to discharge their duties, they should resign their posts immediately – in protest of the board’s recent decisions, if for no other reason. To reiterate, the appointments of Janice Loux and Jonathan Davis are in clear conflict with the interests of taxpayers. Together with Darnell Williams, they have long been complicit in the conspiracy of silence that has shrouded the fund from public scrutiny for well over a decade. None of them blew the whistle on the Fletcher affair. Even as the last vote on disclosure was lost for the cause of accountability, they chose not to engage the issue publicly, opting instead to stay in tune with the rest of the board. That makes clear where their allegiances lie.

Therefore, effective reform can hardly take place unless the board members from the state’s quota are relieved immediately from their appointments on the retirement board and from any other positions they may hold with the state and any of its constituent units.

The time is at hand to send a clear message that mocking the laws and the elected government of this commonwealth and abusing the public trust is not acceptable and will not be tolerated. Now is the time to set an example of what accountability means. Now is the time to blaze a path of transparency by demanding that the fund’s financial statements, investment contracts, board deliberations, budgets, investment reports and other relevant information be opened to public scrutiny.

Thank you.

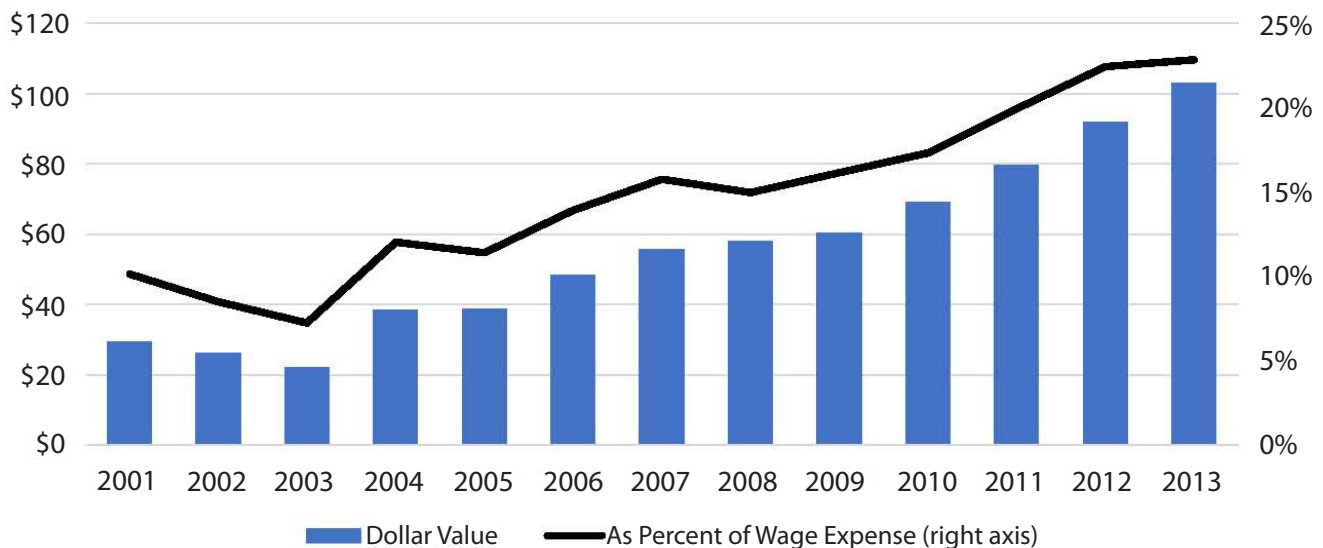
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Exhibit 1. MBTA Labor Costs

| FY Ended June | Wages | Medical & Dental Insurance | OPEB ²⁷ | Pensions | Social Security Taxes | Workers' Comp | Other | Capitalized | Total |
|---------------|-----------|----------------------------|--------------------|-----------|-----------------------|---------------|---------|-------------|-----------|
| 2013 | \$450,898 | \$65,104 | \$185,595 | \$102,941 | \$38,654 | \$8,778 | \$1,131 | -\$22,548 | \$830,553 |
| 2012 | \$410,156 | \$77,350 | \$183,676 | \$91,988 | \$36,760 | \$7,989 | \$1,346 | -\$22,353 | \$786,912 |
| 2011 | \$399,292 | \$67,227 | \$141,035 | \$79,568 | \$34,990 | \$11,125 | \$1,987 | -\$19,351 | \$715,873 |
| 2010 | \$399,573 | \$66,746 | \$142,547 | \$69,186 | \$34,634 | \$10,897 | \$2,769 | -\$17,717 | \$708,635 |
| 2009 | \$374,876 | \$66,486 | \$151,350 | \$60,518 | \$34,106 | \$8,675 | \$2,057 | -\$25,835 | \$672,233 |
| 2008 | \$387,958 | \$61,152 | \$158,856 | \$58,054 | \$34,331 | \$10,871 | \$2,076 | -\$28,096 | \$685,202 |
| 2007 | \$353,900 | \$51,978 | \$57,618 | \$55,747 | \$31,446 | \$11,965 | \$1,968 | -\$26,240 | \$538,382 |
| 2006 | \$347,846 | \$112,790 | \$50,182 | \$48,387 | \$31,264 | \$16,238 | \$1,963 | -\$23,806 | \$584,864 |
| 2005 | \$339,760 | \$94,035 | \$47,880 | \$38,743 | \$30,335 | \$20,971 | \$2,112 | -\$19,453 | \$554,383 |
| 2004 | \$321,386 | \$89,363 | \$41,153 | \$38,645 | \$28,076 | \$19,305 | \$2,877 | -\$18,017 | \$522,788 |
| 2003 | \$304,854 | \$78,983 | \$36,361 | \$22,091 | \$26,820 | \$5,912 | \$403 | -\$17,777 | \$457,647 |
| 2002 | \$307,843 | \$80,805 | \$33,175 | \$26,199 | \$26,883 | \$10,085 | \$1,259 | -\$17,048 | \$469,201 |
| 2001 | \$291,093 | \$68,766 | \$32,157 | \$29,515 | \$25,347 | \$14,394 | \$2,575 | -\$16,790 | \$447,057 |

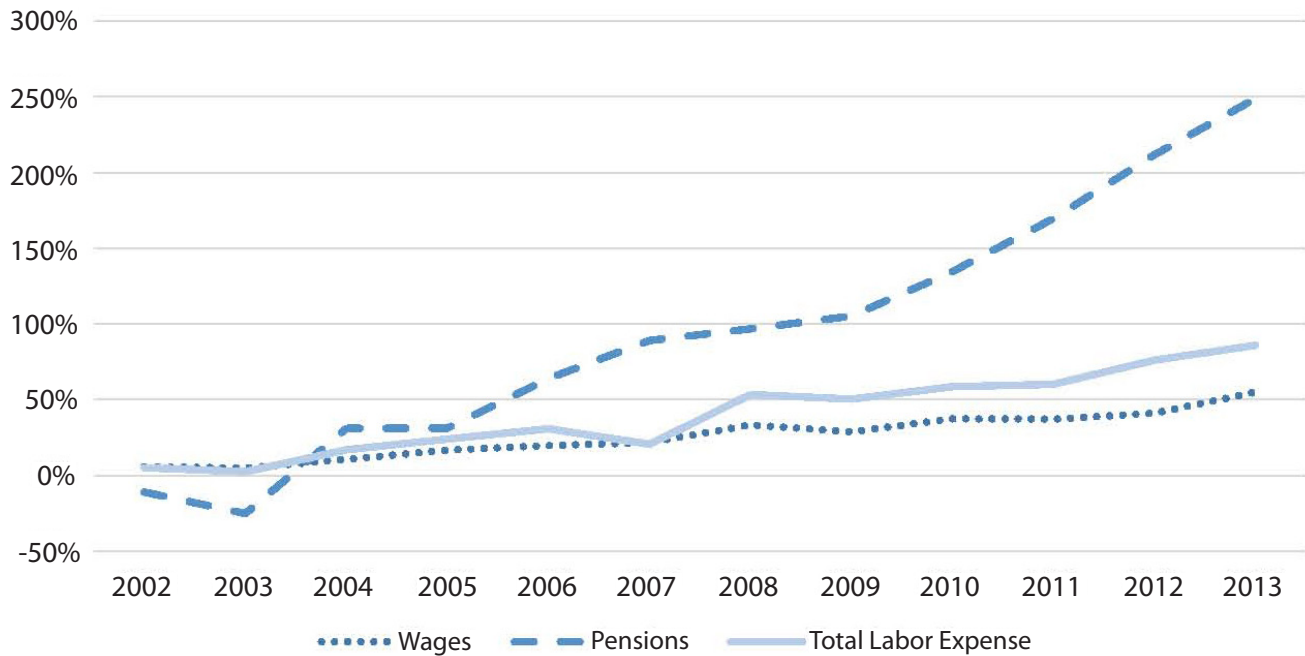
Source: Iliya Atanasov, "Have the MBTA Retirement Plans Gone Off the Rails?" Pioneer Institute White Paper 108 (November 2013), <http://pioneerinstitute.org/download/have-the-mbtas-retirement-plans-gone-off-the-rails/>

Exhibit 2. MBTA pension expense dollar value and as percent wage expense



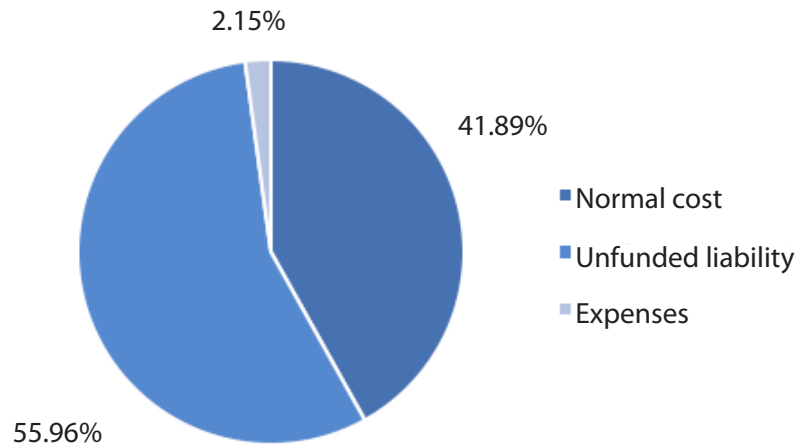
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Exhibit 3. Cumulative growth of select MBTA expenses (FY 2002-2013)



Source: Iliya Atanasov, "Have the MBTA Retirement Plans Gone Off the Rails?" Pioneer Institute White Paper 108 (November 2013), <http://pioneerinstitute.org/download/have-the-mbtas-retirement-plans-gone-off-the-rails/>

Exhibit 4. Structure of required contributions as of 2011 valuation (submitted in June 2013)

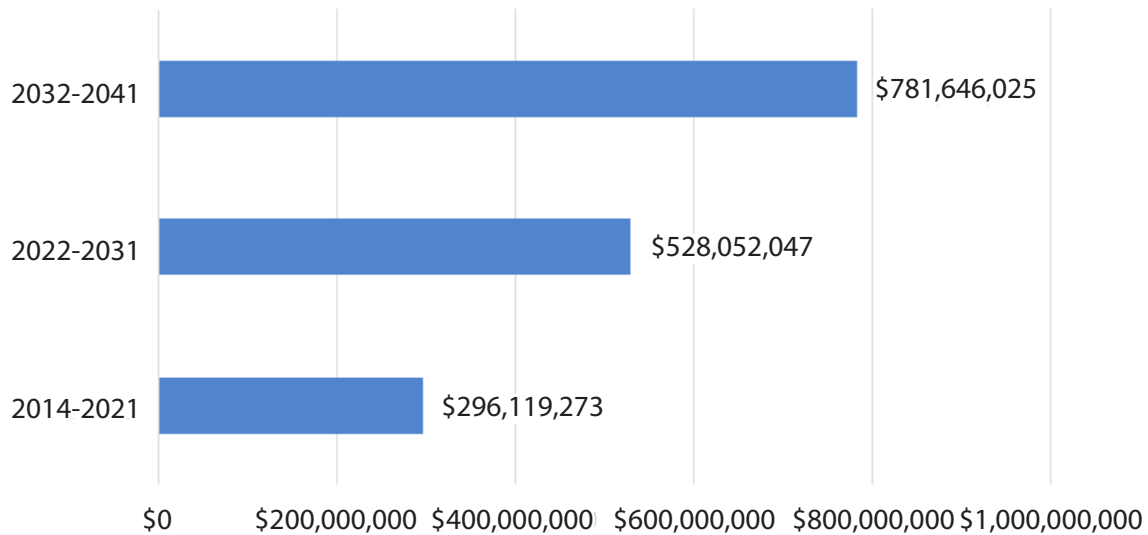


| Component | Percent covered payroll | Percent of total ARC | Dollar value | MBTA share ¹⁴ |
|---------------------------|-------------------------|----------------------|--------------|--------------------------|
| Normal cost | 8.75% | 41.89% | \$32,084,451 | \$24,063,338 |
| Unfunded liability | 11.69% | 55.96% | \$42,849,577 | \$32,137,183 |
| Expenses | 0.45% | 2.15% | \$1,649,470 | \$1,237,103 |
| Total | 20.89% | 100.00% | \$76,583,498 | \$57,437,624 |

Source: Iliya Atanasov, Solvency and Insolvency of the MBTA Retirement Fund (Pioneer Institute, February 20, 2014), http://pioneerinstitute.org/better_government/the-end-of-the-line-for-the-mbta-retirement-fund/.

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Exhibit 5. Projected MBTA payments toward the 2011 unfunded pension liability



Source: Iliya Atanasov, Solvency and Insolvency of the MBTA Retirement Fund (Pioneer Institute, February 20, 2014), http://pioneerinstitute.org/better_government/the-end-of-the-line-for-the-mbta-retirement-fund/.

Endnotes

1. Iliya Atanasov, “Have the MBTA Retirement Plans Gone Off the Rails?” Pioneer Institute White Paper 108 (November 2013), <http://pioneerinstitute.org/download/have-the-mbtas-retirement-plans-gone-off-the-rails/>, p. 16.



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