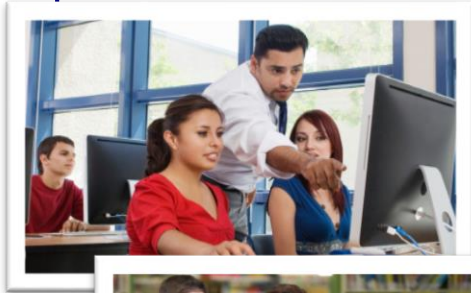# Legislative Commission on Pensions and Retirement

February 7, 2017

TRA's membership and mission

Serving teachers for over 100 years – five generations of educators

TRA membership – nearly 190,000

- 80,530 active teachers
- 63,503 retired public school educators, state college faculty
- 13,680 deferred, vested members
- 31,850 deferred, non-vested members

TRA assets and benefits
- $20 billion in assets
- $1.7 billion in annual payments which benefit local economies and generate tax revenue

TRA's mission:
- ➤ *Retirement security for Minnesota teachers*
- ➤ *Support state's education system by attracting and retaining teachers*

Pensions help recruit and retain teachers

Teacher shortages increasing – studies show pensions help attract and retain experienced teachers

- **Recruitment**: Among workers under age 40, 63% say offer of defined benefit (DB) pension is important in accepting the job, up from 28% just two years before. (Towers Watson, 2012)

- **Retention**: Three-fourths of new hires say DB pension is compelling reason to stay on the job. Teacher effectiveness and productivity improve with experience. (Towers Watson, 2012 and National Bureau of Economic Research, 2006; Milanowski and Odden, 2007)

- Teacher **turnover costs high** – recruitment, hiring, orientation, productivity loss. (Alliance for Excellent Education, 2005 and National Institute on Retirement Security, 2011)

- **Teacher pay gap** partly filled by pensions. 2016 study shows teacher salaries lag those of comparably educated by 17%. (Allegretto and Mishel, 2016)

TRA revenue sources: Investment returns provide most pension funding

The TRA Pension Buck
Pensions are a shared responsibility.
86¢ of every $1 paid to TRA pensioners comes from investment earnings and member contributions.

73¢ Investment Earnings
14¢ Employers
13¢ Employees

TRA Comprehensive Annual Financial Reports, 1990-2016

Pensions are a shared responsibility.
Every dollar paid to retirees comes from three sources:

62¢ Investment Earnings
26¢ Employers
12¢ Employees

National public pension average:
(Source: National Association of State Retirement Administrators, Oct. 2016)

Effects of experience study

2015 experience study evaluated all actuarial assumptions and recommended:

- Lower investment assumption from 8.5% to 8%, adds to costs, lowers funded ratio.

- Updated mortality table – members and retirees are living longer – on average an extra **two years**, adds significantly to costs.

TRA board 2016 proposal addressed experience study:

- TRA board built support among stakeholders (actives, retirees, employers) and recommended a balanced package of benefit cuts and contribution increases to address experience study results, but they were not enacted.

- Delay in enacting changes is costly:

  - Adds **$1.12 million per month or $13.4 million** per year to benefit costs because COLA remains at 2%.

  - Decreases contribution revenue by at least **$22.5 million** per year, not including potential investment earnings on that revenue.

TRA 2017 legislative proposal

Retirees

○ Reduce COLA from 2% to 1% for 5 years, 1.5% thereafter, eliminate 2.5% COLA trigger

Active teachers

○ Reduce future COLA from 2% to 1.5%, eliminate 2.5% COLA trigger

→ **COLA savings equal 2.66% of pay which is equivalent to $124 million annually or $1.5 billion over TRA's projection period**

Employers

○ Increase contribution rate from 7.5% to 9.5%, phased over 4 years (0.5% per year)
○ Offset by state pension aid through pension adjustment mechanism in school aid formula

Portion of proposal borne by each group*

Actives 27%

Employers 46%

Retirees 27%

Members 54%
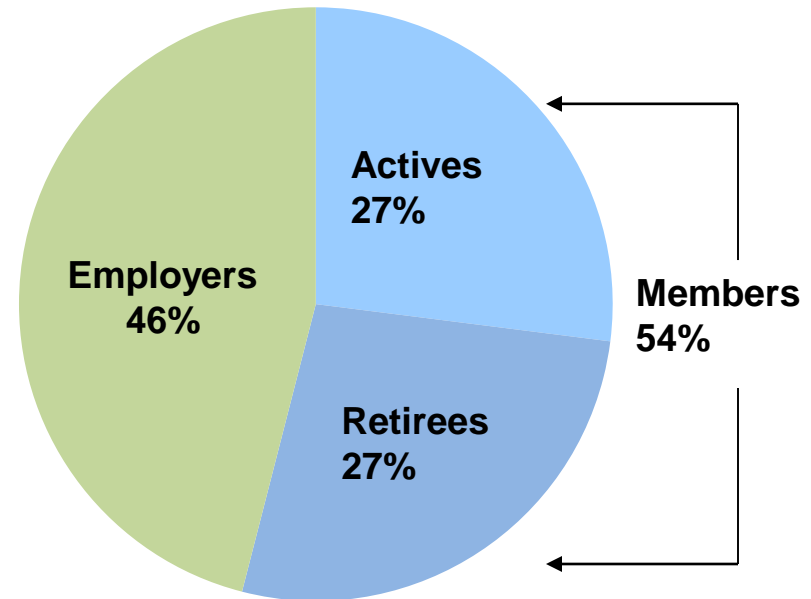
*Based on present value of contributions and benefit cuts over 30 years.
Source: TRA Actuary

TRA 2017 legislative proposal – state pension aid

	TRA rate	Costs for school districts/charters (assuming 0%/ yr payroll growth)	Costs for school districts/charters (assuming 2.5%/ yr payroll growth)	Aid in Governor's budget	Annual shortage
FY18	8.0%	$21.6 million	$22.7 million	$21.6 million	$0 – 1.1 million
FY19	8.5%	$43.2 million	$46.5 million	$43.1 million	$0.1 – 3.4 million
FY20	9.0%	$64.8 million	$71.5 million	$43.1 million	$21.7 – 28.4 million
FY21	9.5%	$86.4 million	$97.6 million	$43.1 million	$43.3 – 54.5 million

Other TRA package elements:

➢ Extend amortization period to 30 years

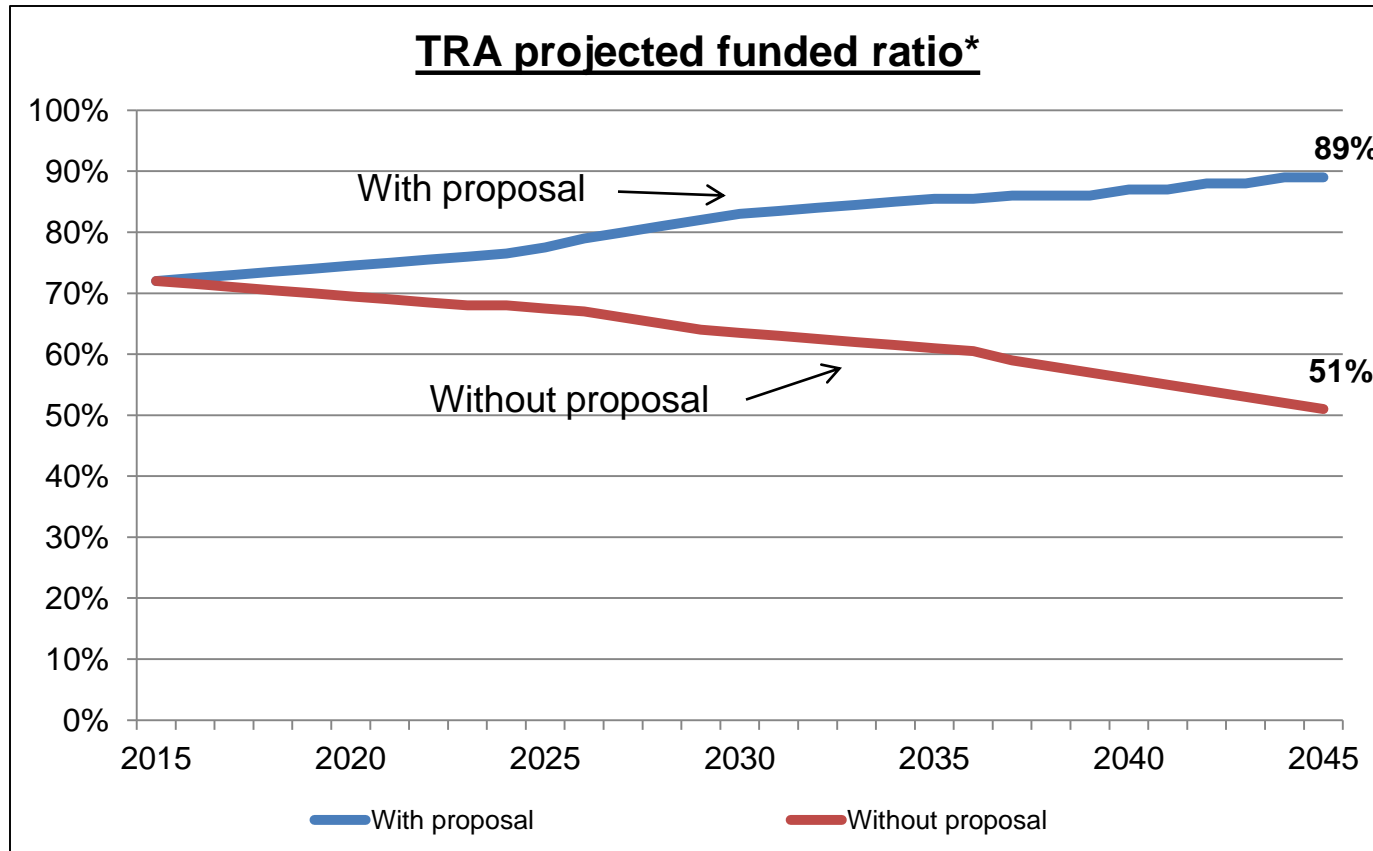➢ Require employer contributions on salaries of re-employed retirees

TRA 2017 proposal --
component savings

Proposal element	Savings/revenue (as % of pay)	Savings/revenue* (in $/year)
COLA Cuts	2.66%	$120 million
Contribution Increase	2.00%	$90 million (in 4th year)
30 year amortization	1.08%	$49 million
Total savings/revenue	5.74%	$259 million
Remaining deficiency after proposal (actuarial value)	(0.42%)	$19 million

* Assumes annual payroll base of $4.52 million with 0% growth assumption.

TRA financial status – positive impact of TRA 2017 proposal

TRA projected funded ratio*

With proposal — 89%

Without proposal — 51%

With proposal

Without proposal

* Assumes investment assumption of 7.5% for five years, 8% thereafter.

TRA's 2017 proposal – investment assumption

Investment assumption – thorough study needed before long-term assumption changed

- TRA board supports a thorough, data-driven study of <u>all</u> economic assumptions before the long-term investment assumption is changed. The next experience study, due in 2 years, will look at all assumptions (investment return, inflation, wage and payroll growth) in a comprehensive, holistic manner.

- As an interim step, TRA supports lowering the investment return assumption to 7.5% for temporary 5-year period with the long-term rate remaining at 8% until study is completed.

- Investment assumption is long-term and used to project liabilities for 50 to 60 years into the future. It should not be overly influenced by short-term volatility nor frequently changed without careful study.

- Moving from 8.5% to 7.5% investment assumption is costly, immediately adding **$3.2 billion** to TRA liabilities and raising its deficiency by **5.8% of pay**.

- Even with TRA's proposed package of reforms, TRA would be deficient by over 2% of pay ($103 million annually) if a 7.5% assumption is immediately implemented. Moving to 7.5% assumption without a plan to pay for it would increase risks for TRA and jeopardize it financially.

TRA financial status –
impact of 7.5% investment assumption change

	FY16 valuation Return assumption: 7.5% for 5 yrs, then 8% ------------- with TRA proposal	FY16 valuation Return assumption: 7.5% all years ------------- with TRA proposal	Difference – added cost of using 7.5% assumption
Actuarial Accrued Liability	$27.2 billion	$28.3 billion	+ $1.1 billion
Current Funded Ratio (actuarial value)	74.3%	71.4%	- 2.9%
Projected Funded Ratio (in 30 years)	89%	70%	- 19%
Contribution Deficiency (actuarial value)	(0.42%)	(2.69%)	**Increases deficiency by 2.27% of pay $103 million per year**
(market value)	(1.36%)	(3.60%)	**Increases deficiency by 2.24% of pay $101 million per year**

TRA financial status – Impact of 7.5% investment assumption

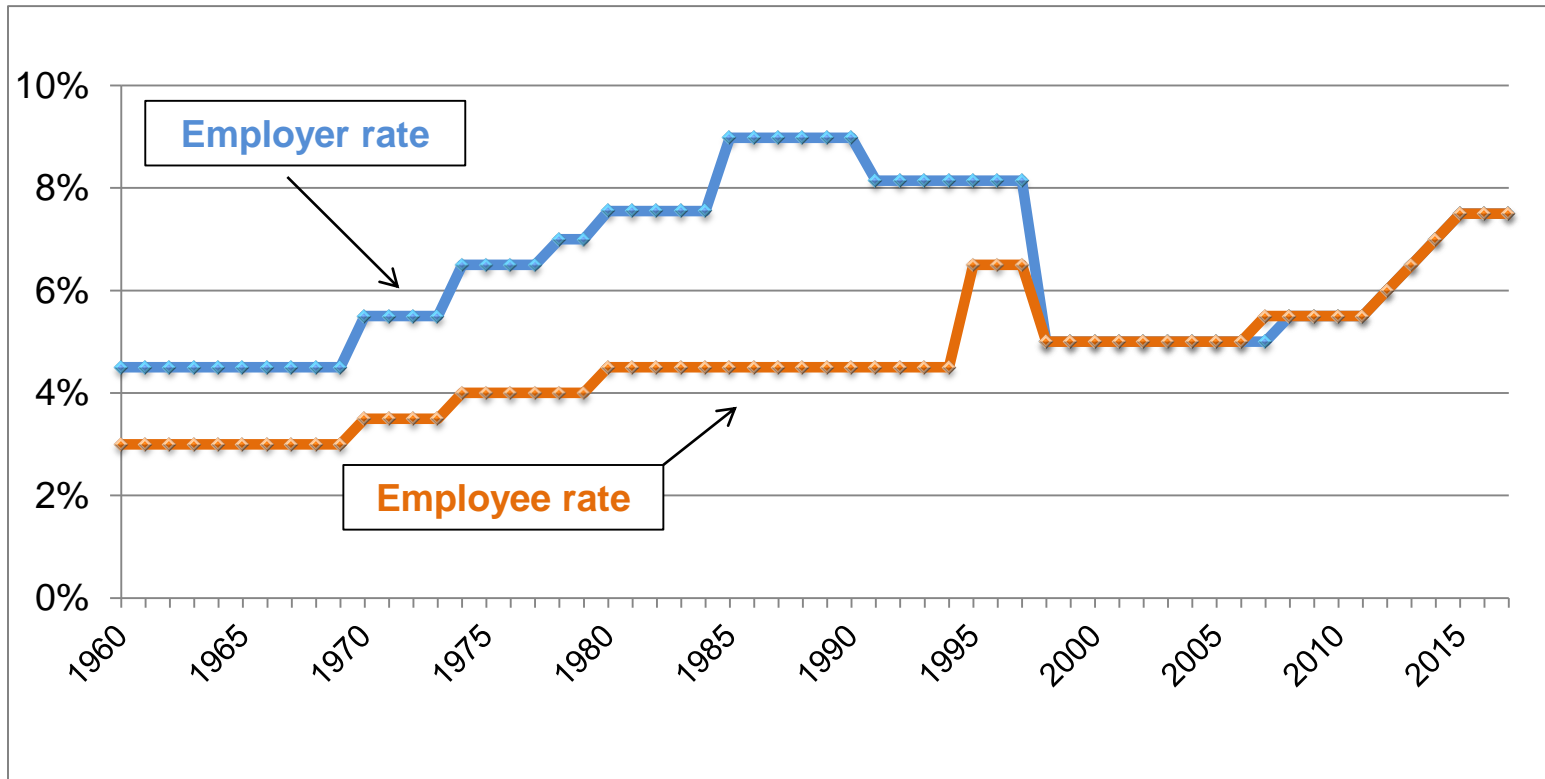**TRA projected funded ratio***
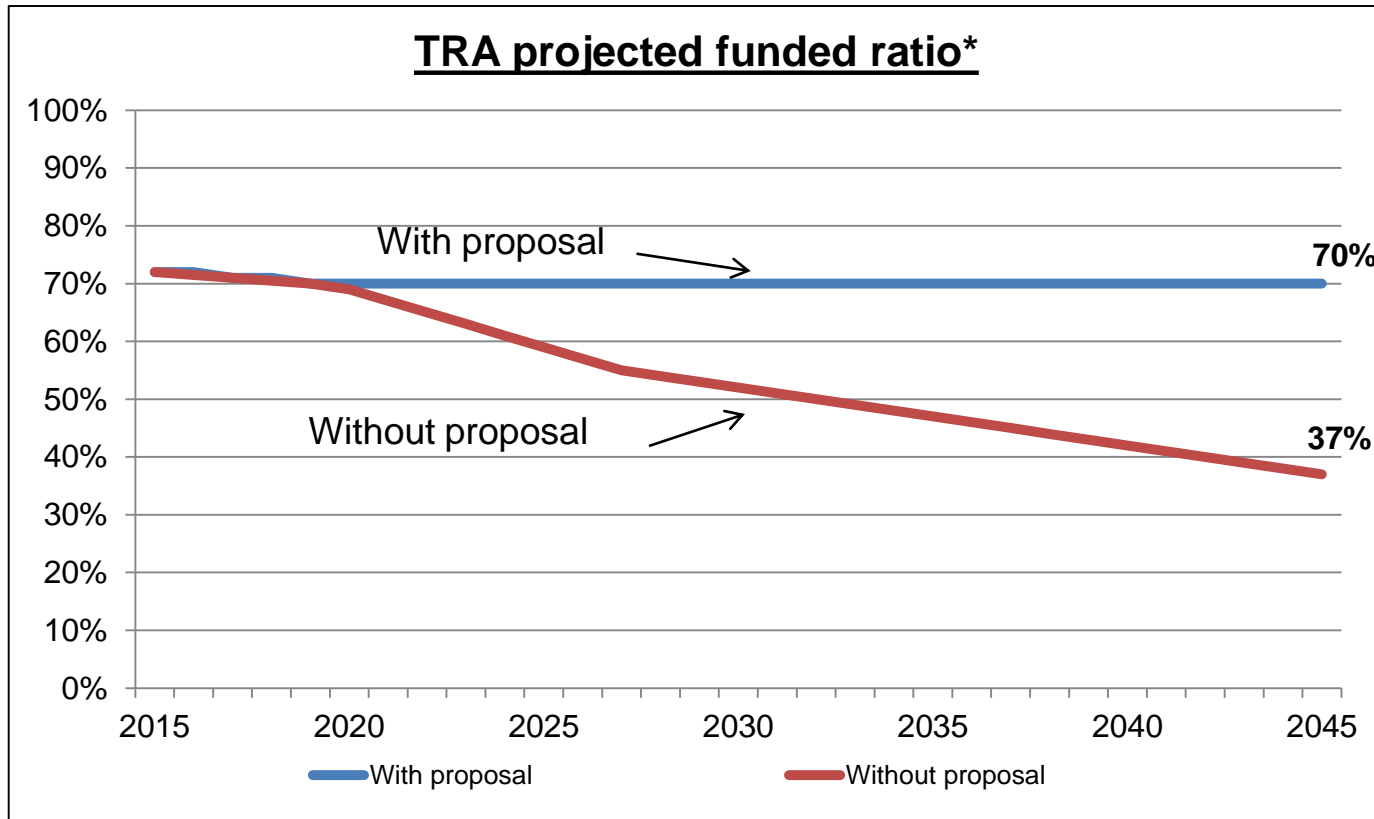
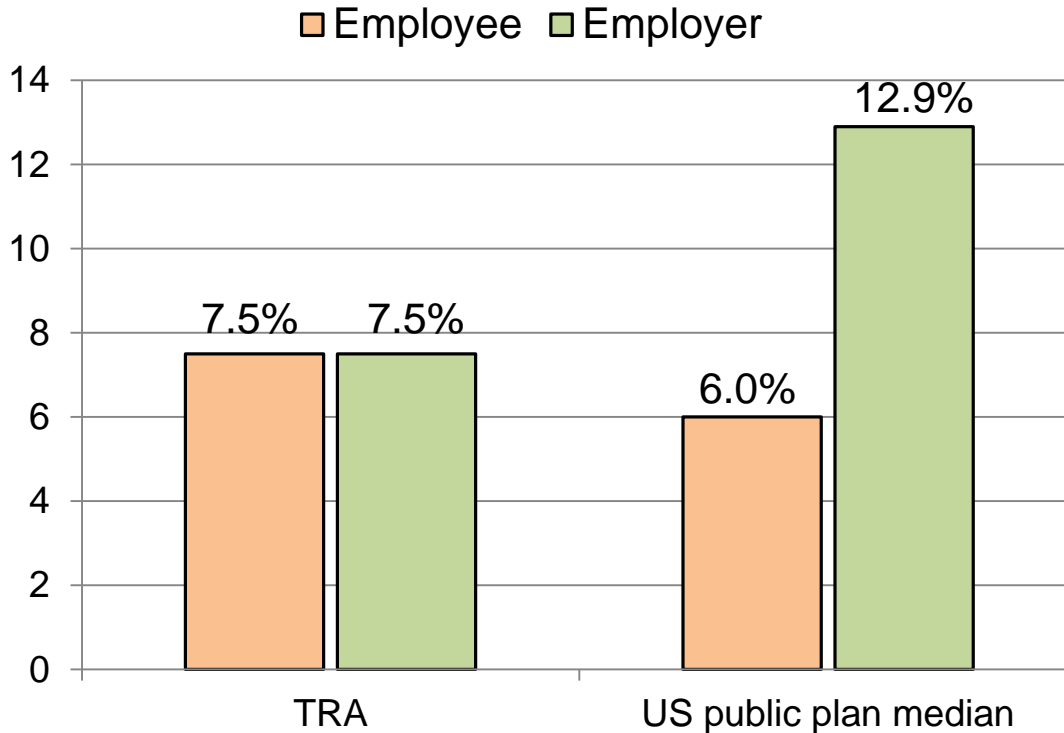*Assumes investment assumption of 7.5% for all years.

TRA contribution rate history

For most of TRA history employer rate has been higher than employee rate.

Employee contribution rates in MN higher, employer rates in MN lower

Source: NASRA FY2016 for Social Security-covered plans

Contribution rates in adjacent states

	Employee	Employer
North Dakota	3% *	12.26% **
North Dakota Teachers	11.75%	12.75%
South Dakota	6%	6%
Wisconsin	6.8%	6.8%
Iowa	5.95%	8.93%
MN TRA	7.5%	7.5%

*ND employee contribution rate is 7% in statute, but employer picks up 4% of that rate.
**ND employer rate includes 1.14% contribution to employee health care savings accounts and 4% employer pickup of employee rate.

Tradition of careful stewardship to ensure plan stability

- **Disciplined and proactive management**. TRA continuously monitors and proposes adjustments to the fund as conditions warrant.

- **Proactive pension reforms.** Board-proposed 2010 legislation was critical, cost savings: $1.75 billion (TRA).

- **Periodic experience studies** (every 4 years). Changes proposed based on data in a careful, thoughtful manner with involvement of stakeholders.

- **Modest benefits.** The average monthly pension for retired Minnesota teachers eligible for social security is $1,855.

- **Relatively low cost**. In Minnesota, government pension contributions are only 2.1% of total state and local government spending, compared to an average 4.1% in all other states. (Census Bureau)