Executive Summary

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Lifting the Pension Fog

What teachers and taxpayers need to know about the teacher pension crisis

National Council on Teacher Quality

EducationCounsel

Authors

Kathryn M. Doherty, Sandi Jacobs and Martin F. Lueken

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Each state received a draft of its analysis in September 2016 to review and provide comments and corrections; systems also received a final draft of the analysis for their state a month prior to release. Not all of the systems responded to our inquiries, but the cooperation and assistance of those that did has helped to ensure the factual accuracy of the final product. The authors are also grateful to Michael J. Podgursky for his feedback and counsel in producing this report.

About NCTQ

The National Council on Teacher Quality is a non-partisan research and policy organization working to ensure that every child has an effective teacher. NCTQ is available to work with individual states to improve teacher policies. nctq.org

About EducationCounsel

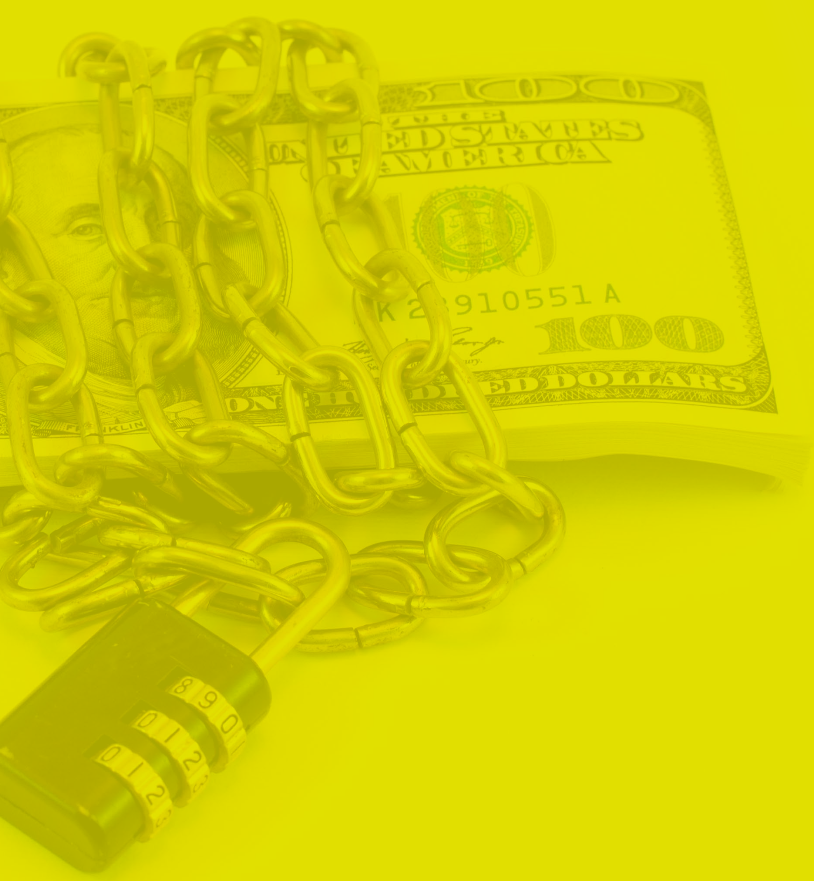
EducationCounsel is a mission-based education consulting firm that combines experience in policy, strategy, law, and advocacy to drive significant improvements in the U.S. education system. educationcounsel.com

The fog is an illusion –

A master of disguise,
Which hides the tangible
Before our very eyes.

But when the fog has lifted
Everything's still there,
And the tangible
Only seemed to've
disappeared.

– Walterrean Salley



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The pension fog — a mix of optimistic projections, willful ignorance, and deferral of consequences — hangs heavily over the policy landscape. In 2016, teacher pension debt nationwide stands at $516 billion dollars. While this is a crisis situation by any definition, little has changed on the teacher pension policy landscape over the last decade.

This year, the National Council on Teacher Quality has partnered with EducationCounsel to present a comprehensive analysis on the health of teacher pension systems in each of the 50 states and the District of Columbia.

In assessing the quality of state teacher pension policy, we've benchmarked the states against a forward looking and sustainable approach to teacher retirement benefits in four key goal areas: pension flexibility, sustainability, neutrality, and, new for 2016, transparency. Our goals are to help make the not-so-obvious aspects of teacher pensions more visible and understandable, and to explore policy options for teacher retirement that could better support the security and interests of teachers and taxpayers alike.

Figure A. Summary of State Teacher Pension Policy

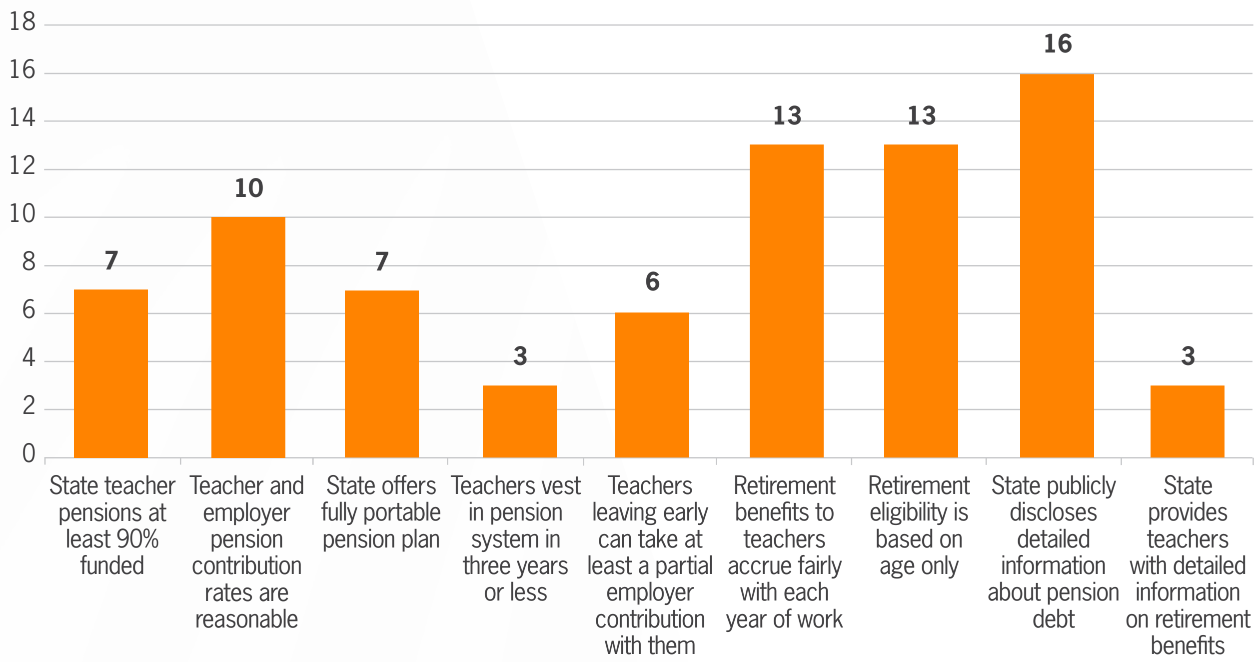
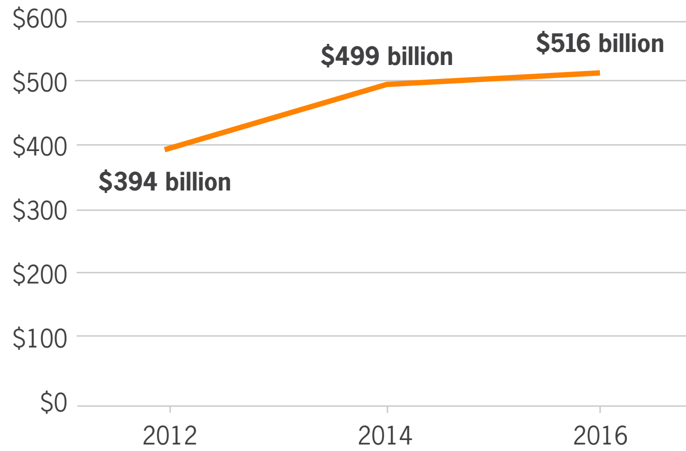


Figure B. State teacher pension system debt nationwide



Key Findings

In most states, current teacher pension systems are untenable and can't be fixed without comprehensive policy reform.

Nationwide just 11 states — **Alaska**, **Illinois**, **Maine**, **Minnesota**, **New Hampshire**, **New Jersey**, **Rhode Island**, **South Dakota**, **Utah**, **Washington** and **Wisconsin** — meet any of the four goals (flexibility, sustainability, neutrality or transparency) for teacher pension health, and no state meets them all.

The number of states with well-funded pension systems is in the single digits and has steadily declined over the past decade.

In 2016, just seven states had teacher pension systems that are funded at 90 percent or higher. **South Dakota** and **Wisconsin** are the only two states in the nation with fully-funded teacher pension systems. At 42 percent, **Illinois** continues to have the lowest funded pension system in the nation.

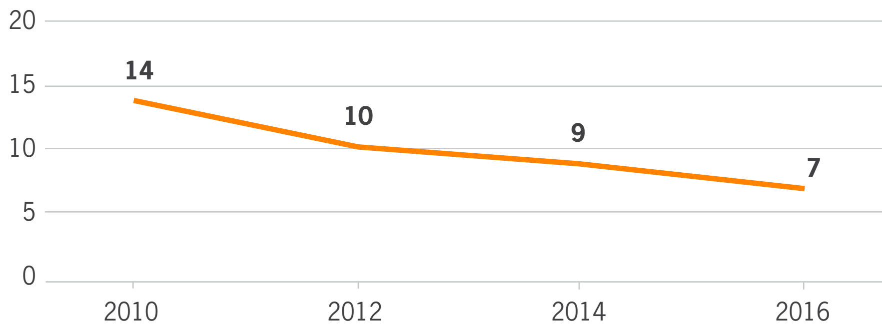
Most current pension contributions go to debt service.

In 38 states, the majority of employer contributions to teacher pensions go toward funding the system's unfunded liabilities, not paying now for the benefits due to working teachers when it is their turn to retire. Nationwide, more than two-thirds of every dollar contributed by employers to teacher retirement systems goes toward servicing the enormous pension debts that have accrued across the states.

Despite serious financial consequences for public coffers, as well as for teachers' and taxpayers' pockets, most states steadfastly cling to traditional defined benefit retirement programs.

In 38 states teachers have only one primary option. They are enrolled in defined benefit pension plans. Only **Alaska** provides teachers with a flexible and fair defined contribution plan. Six other states — **Florida**, **Michigan**, **Ohio**, **South Carolina**, **Utah** and **Washington** — offer teachers a choice. **South Dakota** stands out for being a state that demonstrates how a defined benefit system can be structured in a way that is financially sustainable and provides flexibility to teachers.

Figure C. Number of states with well-funded teacher pension systems (2010-2016)



The typical defined benefit plan is increasingly costly and harder to collect.

The last decade has seen a steady rise in pension contribution rates for teachers and employers. Since 2008, when NCTQ started collecting data on teacher pensions, 32 states have increased teacher contributions to pension systems. Just since 2012, 37 states have increased the contribution rates required of employers.

But even as they contribute more, teachers are less likely than ever to collect on their promised benefits. Every state except **Arizona**, **Minnesota** and **South Dakota** now delays teacher vesting in pension systems for longer than three years. Twenty states make teachers wait seven to 10 years to vest. Just six states allow teachers to take their contributions and at least a portion of employer contributions when they leave the pension system.

Few states with traditional defined benefit pensions provide adequate information to stakeholders on pension system health or to teachers on their personal retirement benefits.

Some states are ahead of their peers on public disclosures related to pension health. **South Dakota** come closest, and nearly meets this goal, because of its overall teacher pension system transparency and because it provides teachers with an annual benefits statement that includes some of the important data we think teachers should have about their own nest eggs. **Alaska**, **Delaware**, **Maine**, **Minnesota** and **North Dakota** report projections for future contributions required to fully amortize the systems' total unfunded liabilities, and they also report these projections under a range of assumptions about the rate of return on investments, not just under the systems' own assumptions. However, nationwide only 15 states publicly report projections for the future contributions that would be required to pay off pension debt.

When it comes to providing teachers, the key beneficiaries of pensions, with information, states do an even worse on transparency. Only **Vermont** and **South Dakota** break out and reports to individual teachers the amount contributed by them and the amount contributed by the employer. Only **Wyoming** and **South Dakota** provide teachers with some information about the opportunity cost of leaving contributions in the system by reporting what a teacher would need to contribute on his or her own to achieve the same level of benefits at some future date.

The miasma blanketing teacher pension policy suggests that states are, at best, engaged in short-term magical thinking their retirement systems:

- The rates of return assumed by most states have been way too high. In 2016, 41 states made their pension calculations based on a 7.5 percent or higher rate of return on investments, and 13 of those states set their expectations at an 8 percent or higher return.
- In an effort to boost investment returns and make up for lost ground, public pension systems have made increasingly risky investments.
- The fees paid to pension investment managers are astronomical. Like any fund, state teacher pension funds need to be managed. States are not obligated to disclose such fees to the public, and therefore, not surprisingly, most state funds choose less than full disclosure.

Pension Policy Recommendations

Systemic reform of teacher pensions requires states to make tough decisions that are right for the long term. State leaders and pension plan sponsors have the power to change the trajectory of state pension plans for teachers by:

1. Offering teachers the option of a defined contribution pension plan.

All teachers should have the option of a fully portable pension system as their primary pension plan.

2. Shoring up pension funding for existing commitments.

States need to take action to secure the financial health of teacher pensions by adjusting unrealistic assumed rates of return and making scheduled payments to their pension systems.

3. Including all new teachers in Social Security.

Some or all teachers in 16 states do not participate in Social Security. Including teachers in Social Security in all states could help provide a safety net as states undertake pension reform.

4. Instituting safeguards that prevent politically expedient decisions that cost both teachers and taxpayers in the long run.

States need strategies to prevent the raiding of pension funds and to stop policymakers from making politically expedient commitments now that will have to be paid for later.

5. Ensuring some basic principles of fairness.

Teachers should be able to: a) vest no later than the third year of employment; b) have the option of a lump-sum rollover to a personal retirement account upon termination of employment that includes, at minimum, the teacher's contributions and accrued interest at a fair interest rate; c) have options for withdrawal from either defined benefit or defined contribution plans that include funds contributed by the employer; and d) purchase time for unlimited previous teaching experience at the time of employment, as well as all official leaves of absence such as maternity or paternity leave.

6. Requiring that pension systems are neutral, uniformly increasing pension wealth with each additional year of work.

Pension systems that set up teachers to earn vastly different benefits for the same number of years worked are costly and unfair. The formula for determining benefits should preserve incentives for teachers to continue working until conventional retirement ages.

7. Providing taxpayers and teachers with the information they need to make educated decisions about their retirement futures.

In order for taxpayers and teachers to hold public officials accountable, they are entitled to: a) information projecting the future contributions required to fully pay off a system's total pension debt; b) data on who makes employer contributions (e.g., state and/or school districts) and the proportion of total contributions for which each contributor is responsible; and c) information on debt service beyond reported liabilities (e.g., pension obligation bonds) that has been taken on to fund current or future pension obligations.

National Council on Teacher Quality

1120 G Street, NW, Suite 800, Washington, D.C. 20005
Tel: 202-393-0020 Web: nctq.org

EducationCounsel

101 Constitution Avenue, Washington, D.C. 20001
Tel: 202-545-2961 Web: educationcounsel.com