A Retirement House of Cards

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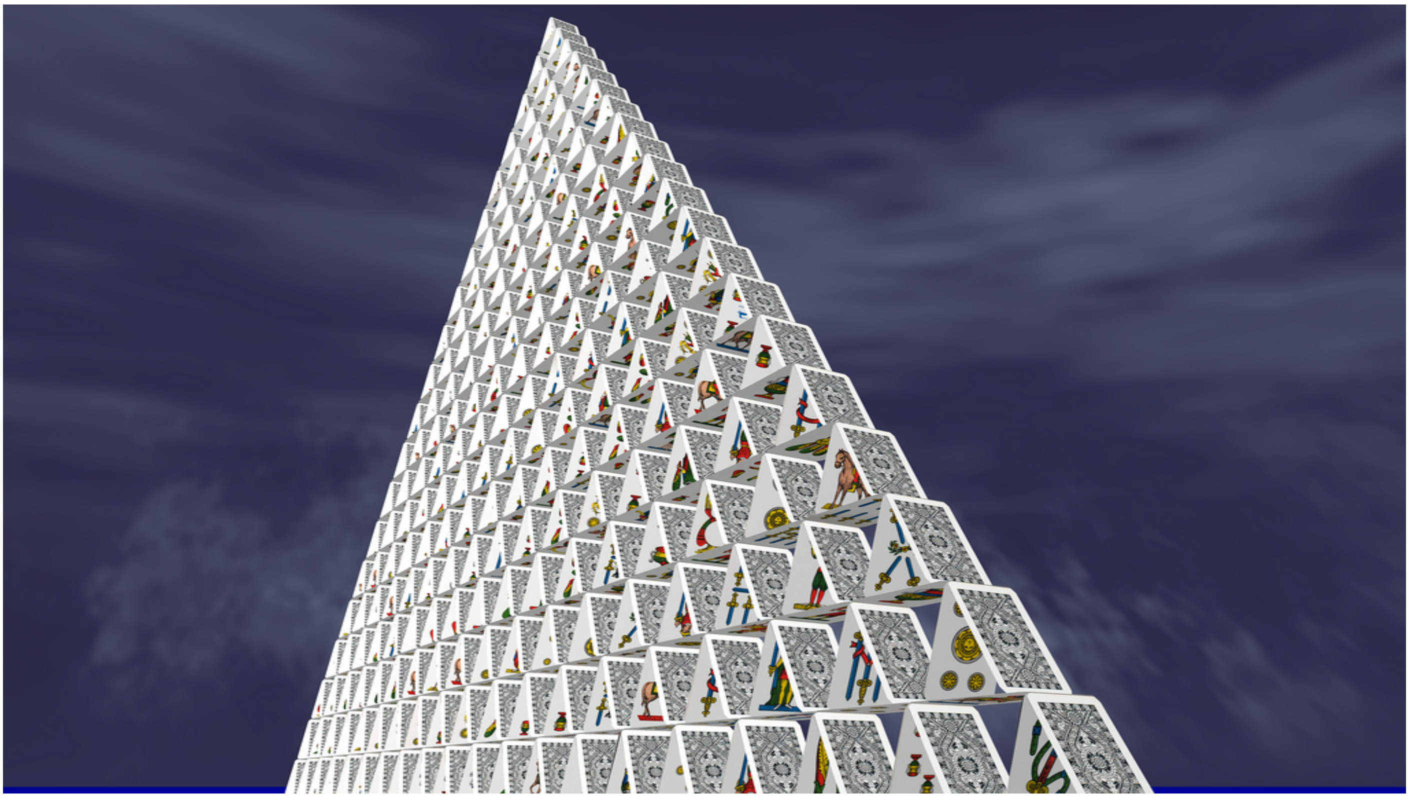

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By: Susan Pendergrass

In a recent blog post about the state of affairs in a couple of Missouri state pension funds, we pointed out that they're getting costlier and less sustainable with each passing year. Sadly, the systems serving the teachers in our two major cities are even worse. According to a 2017 asset/liability analysis commissioned by the Kansas City Public School Retirement System (KCPSRS), that system is currently only 64 percent funded, partly because the school district has failed to make the required contributions since 2012. At the current contribution rate of 19 percent (9.5 percent from the teachers/9.5 percent employers—either the Kansas City Public School District or a charter school), assuming the fund will earn a 7.75 percent return every year for the next 20 years, the system will be 53 percent funded in 10 years and just 39 percent funded in 20 years. (If the fund earns just 4.75 percent per year, the funding ratio in 2037 will be . . . 0 percent. That's right—no money left in the fund.) Not surprisingly, the KCPSRS has requested that the state legislature increase the school contribution to 10.5 percent next year and 12 percent in the following year. In the best case, a total of nearly 22 percent of payroll will be contributed to the KCPSRS and the fund will earn a consistent return of 7.75 percent every year for 20 years, which would get it to 80 percent funded.

The St. Louis Public School Retirement System (STLPSRS) has its own problems—it was just 64 percent funded in 2016, with 5,000 current teachers supporting 4,600 retirees. Teachers have been contributing 5 percent of payroll, with St. Louis Public Schools (SLPS) and charter schools making up the rest of what the annual actuarial analysis determines is necessary to keep it funded at least 70 percent. As a result, the bill for SLPS and the charter schools has climbed to over 15 percent and, in 2018, the actuarial analysis determined it needed to be 19 percent. However, difficulty keeping up with increasing costs led SLPS to request that the Missouri state legislature cap their contribution rate at 16 percent. In addition, teacher contributions would climb by one-half percent each year until they reach 9 percent (new teachers in fall 2018 will immediately begin paying 9 percent). According to STLPSRS, that would leave them with a $192 million shortfall within 15 years, so they're suing SPLS and the St. Louis charter schools.

Economic conditions, unaffordable benefit promises, and an unwillingness to use realistic investment return assumptions have resulted in precarious fund positions, lawsuits, and attempts to balance the books on the back of the youngest workers. Does it have to be this way? *No.* Many states are moving away from defined-benefit plans (pensions) and toward defined-contribution plans [like 401(k), cash-balance, or hybrid plans]. In some cases, all new employees are placed in the new plans; in others, they can choose between the state defined-benefit plan or the new options.

We're also seeing teacher retirement benefit innovation from within public education. In 19 states, charter schools may choose whether or not to participate in their states' pension plans. A recent analysis of charter school participation in five states that make participation optional found that the schools most likely to opt out of the state plan are urban, elementary schools, and those that are managed by charter networks. Most of the opt-out charter schools offer their teachers 401(k) or 403(b) plans, and the teachers are vested in less than one year. The reasons given for choosing this path were mostly that the schools wanted to lower their estimated costs, give teachers a wider range of investment options, and make their teacher benefits more portable. For today's youngest teachers, this is an important point. Most of them will not meet a vesting period of ten years in one state and, when that happens, they lose the amount that their employer contributed for them.

The good news for teachers and taxpayers is that there is time to protect current and future retirees before the system is bankrupt. The building isn't on fire yet. However, those of us who pay close attention to this complicated topic are starting to see smoke under the door. It's time to start talking about how to stabilize Missouri's teacher pension systems.

About the Author

Susan Pendergrass
Director of Research and Education Policy

Susan Pendergrass was Vice President of Research and Evaluation for the National Alliance for Public Charter Schools before joining the Show-Me Institute. Prior to coming to the National Alliance, Susan was a senior policy advisor at the U.S. Department of Education during the Bush administration and a senior research scientist at the National Center for Education Statistics during *the Obama administration. She earned a Ph.D. in Public Policy from George Mason University.*

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Show-Me Institute

5297 Washington Place
Saint Louis, MO 63108
Phone: (314) 454-0647
Fax: (314) 454-0667

3645 Troost Avenue
Kansas City, MO 64109
Phone: (816) 287-0370

Email: info@showmeinstitute.org

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