STRS OHIO

The STRS Ohio Plan to Strengthen the Financial Condition of the Retirement System

The Issue

Before the 2008 investment market downturn, STRS Ohio had a funding period for its pension fund of 41.2 years, exceeding state statute's 30-year maximum funding period. Economic and demographic factors, such as members living longer, were causing a reduction in available funds to pay off accrued liabilities over time. The unprecedented decline in the global markets and the accompanying recession, along with the projected gradual economic recovery, significantly accelerated the need for STRS Ohio to make changes.

STRS Ohio has the cash flow needed to pay current monthly pensions. In fact, in these challenging times the value of preserving the financial security of the Defined Benefit pension for Ohio's public educators has never been more apparent. However, looking long term, there is a shortfall in the funding of STRS Ohio benefits. If no changes are made, STRS Ohio will eventually be unable to pay pensions.

The Planning Process

In March 2009, the State Teachers Retirement Board took the prudent and proactive step to begin a long-term contingency planning process to address the funding challenge. The board pledged that the process would be detailed, thorough and deliberative, noting that no actions would be taken lightly as all actions impact STRS Ohio members and employers. The board took an important step to strengthen the financial condition of the pension fund by approving a plan at its Jan. 27, 2011, meeting that will help ensure STRS Ohio can continue to pay pensions to future generations of teachers. This plan complies with the Ohio statutory requirement to bring the pension fund to a 30-year funding period.

The Plan

The current expected long-term actuarial rate of return of 8% for STRS Ohio's investment assets cannot be raised; STRS Ohio cannot count on higher investment returns as a solution. In addition, while it is absolutely imperative that STRS Ohio watches every dollar that it spends, reducing operating expenditures cannot solve the long-term issue of funding pensions for future generations of teachers. As a result, the board approved a multifaceted plan to strengthen the financial condition of the retirement system that includes the following components:

Change in Eligibility for Retirement Beginning Aug. 1, 2015

— Increases age and service requirements for retirement.

Age and service requirements for retirement would increase to a minimum age 60 with 35 years of service. (Members may currently retire at any age with 30 years.) This change would be phased in based on the following timeline:

- Age 56 with 31 years beginning Aug. 1. 2015, and retiring by July 1, 2017
- Age 57 with 32 years beginning Aug. 1, 2017, and retiring by July 1, 2019
- Age 58 with 33 years beginning Aug. 1, 2019, and retiring by July 1, 2021
- Age 59 with 34 years beginning Aug. 1, 2021, and retiring by July 1, 2023
- Age 60 with 35 years retiring Aug. 1, 2023, and later

Members may still also retire at age 65 with a minimum of five years of service.

Currently, STRS Ohio members may retire early with a reduced benefit at age 55 with 25 years of service. The service requirement for a now *actuarially reduced* benefit would be increased to 30 years of service. This change would also be phased in based on the following timeline:

- Age 55 with 26 years beginning Aug. 1, 2015, and retiring by July 1, 2017
- Age 55 with 27 years beginning Aug. 1, 2017, and retiring by July 1, 2019
- Age 55 with 28 years beginning Aug. 1, 2019, and retiring by July 1, 2021
- Age 55 with 29 years beginning Aug. 1, 2021, and retiring by July 1, 2023
- Age 55 with 30 years retiring Aug. 1, 2023, and later

Members may also still retire at a minimum age 60 with five years of service, but the benefit would be *actuarially reduced* beginning Aug. 1, 2015.

(continued)

Unreduced Benefit for Retirement Between:	Minimum Age and Years of Service
Now–7/1/2015	Any age and 30 yrs.
8/1/2015–7/1/2017	Age 56 and 31 yrs.
8/1/2017–7/1/2019	Age 57 and 32 yrs.
8/1/2019–7/1/2021	Age 58 and 33 yrs.
8/1/2021–7/1/2023	Age 59 and 34 yrs.
8/1/2023	Age 60 and 35 yrs.
8/1/2015	Age 65 and 5 yrs.

Actuarially Reduced Benefit* for Retirement Between:	Minimum Age and Years of Service
Now–7/1/2015	Age 55 and 25 yrs.
8/1/2015–7/1/2017	Age 55 and 26 yrs.
8/1/2017–7/1/2019	Age 55 and 27 yrs.
8/1/2019–7/1/2021	Age 55 and 28 yrs.
8/1/2021–7/1/2023	Age 55 and 29 yrs.
8/1/2023	Age 55 and 30 yrs.
8/1/2015	Age 60 and 5 yrs.

*An actuarially reduced benefit reflects a reduction of about 8%–9% for each year that a member retires before meeting eligibility for an unreduced benefit.

Change in Benefit Formula Beginning Aug. 1, 2015

— ***New formula would be 2.2% for all years of service.***

Teachers retiring with 35 years of service at age 60 or older would receive 77% of their final average salary as a pension.

The current 35-year enhanced benefit formula would be eliminated. Those who have 30 years of service; who are age 55 with 25 years of service; or who are age 60 with five years of service as of July 1, 2015, would receive the greater of:

(a) The benefit as of July 1, 2015, under the current formula; or
(b) The benefit upon retirement under the new formula.

In short, members who are eligible for service retirement would receive no less of a base pension benefit than they could have received on July 1, 2015.

Increase in Final Average Salary (FAS) Years Beginning Aug. 1, 2015

— ***FAS calculation would be based on the five highest years of earnings.***

Pension benefits are determined by a member's age, years of service and FAS; the current FAS period is three years.

Reduction in Cost-of-Living Adjustment (COLA) Beginning July 1, 2012

— ***Beginning July 1, 2012, current retirees would receive an annual 2% COLA; members retiring Aug. 1, 2012, and later would also receive a 2% COLA, but it will not begin until 60 months after the date of retirement.***

Currently, the COLA is 3%; both current and proposed COLAs are a fixed-dollar amount each year, not compounded.

Increase in Member Contributions Beginning July 1, 2012

— ***Increase member contributions by 3%, phased in 1% per year beginning July 1, 2012, through July 1, 2014.***

Currently, STRS Ohio members pay 10% of their salary to STRS Ohio in lieu of paying into Social Security. In the pension legislation, the Retirement Board will seek language that gives the board discretion to seek up to a total of 14% in member contributions. To achieve the 30-year funding period, the board's plan calls for only a 3% contribution increase phased in over three years. Authority for up to a 4% increase would give the board flexibility to address future funding experience.

Next Steps

In addition to STRS Ohio, low investment returns, demographic factors and the economic outlook have impacted the other four Ohio statewide public pension plans. As a result, each system has developed a board-approved plan for either maintaining or returning to a 30-year funding period. There is wide divergence among the plans due to the variations in each system's funding situation, demographics and plan design. **All of the changes contained in STRS Ohio's proposed plan require legislative action by the Ohio General Assembly and the governor, as all the plan components require changes in existing statute.**

Looking to the Future

STRS Ohio staff projects that these changes would save about $10.9 billion in accrued liabilities and would bring the pension fund to a 30-year funding period from its current status of infinity. Further, the current 1% employer contribution to the health care fund continues. The Retirement Board will continue to annually review the actuarial valuations of the pension fund and the health care fund to monitor both funds' progress over time. The board will also continue to work with its many constituents, as well as with the other Ohio systems and members of the Legislature, as a bill moves through the Statehouse.

The STRS Ohio plan:

- Provides retired teachers a reasonable and reliable Defined Benefit pension they won't outlive, reducing the likelihood they will have to turn to taxpayer-funded public assistance, Medicaid or social services in retirement. Further, these pensions can continue to provide a stable source of revenue for local economies and provide tax revenues to support needed government services (more than $4.3 billion in STRS Ohio pensions are paid annually to Ohio residents).
- Continues to offer a retirement plan that will help Ohio's public schools, colleges and universities recruit and retain quality educators.
- Provides a transition period for those teachers who are close to retirement, while recognizing that those further out from retirement have more time to plan for their future financial security.
- Preserves all past cost-of-living adjustments (COLAs) and ad hoc increases for current retirees.
- Allows retirees' pensions to continue to grow in the future, but at a slower rate.

Most importantly, the Retirement Board and staff, as fiduciaries of the system, have developed a plan that helps ensure the long-term solvency of STRS Ohio.

At STRS Ohio, we know there are no easy solutions to the challenges we face — and we know some decisions will not make all members happy. We pledge to continue to use our newsletters, Web site, e-mail news service and face-to-face meetings to do what we can to make sure members know the progress of the legislation and any changes going forward.

Retirement Systems Stress Value of Defined Benefit Pensions

In recent months, there has been significant focus on the financial status of public pension plans around the country and whether they are sustainable. In Ohio, the attention has been on STRS Ohio, as well as the Ohio Public Employees Retirement System (OPERS), School Employees Retirement System (SERS), Highway Patrol Retirement System and the Ohio Police & Fire Pension Fund. Adding to the discussion have been comments regarding the value and funding of the Defined Benefit pensions available to Ohio's public employees. With millions of Americans now seeing their pensions, health care and jobs disappear, "pension envy" has emerged as an issue. Some Americans perceive public pensions as too generous and believe they are being funded solely on the backs of the taxpayers.

In fact, these earned pensions represent good public policy for helping to maintain financial security for Ohio's older citizens.

Defined Benefit Pensions Are Good for Their Members and Good for Ohio

- **Defined Benefit pensions provide financial protection for both plan members and taxpayers.** Members are provided a lifetime benefit they won't outlive — a problem now faced by so many whose savings or 401(k) plans were depleted by the recession. They now face the possibility of slipping into poverty in their "golden years," having to turn to taxpayer-funded public assistance, Medicaid or social services. Ohio is already struggling to budget a higher level of resources to cover new people seeking assistance.
- **Defined Benefit pensions are both efficient and economical.** A 2008 National Institute on Retirement Security (NIRS) report found that a defined benefit pension can deliver the same retirement income at almost half the cost of a defined contribution account due to pooling of investment risk, continual diversification of assets and professional investment management. The cost to manage a 401(k)-style defined contribution account is about $1 per $100 of assets. Due to managing the majority of its investment assets in-house, STRS Ohio's investment management costs are about $.24 per $100 of assets.
- **Defined Benefit pensions provide a stable source of revenue for Ohio's local economies.** According to NIRS, in 2006 nearly 360,000 residents of Ohio received a total of $8.41 billion in pension benefits from state and local pension plans, with $8.29 billion paid from plans within the state and the remainder originating from plans in other states. Of the more than 133,000 individuals receiving pension benefits from STRS Ohio, 86% live in Ohio. In calendar year 2010 alone, pension benefit payments from STRS Ohio of about $4.3 billion were distributed among Ohio's 88 counties.
- **Defined Benefit pensions support Ohio workers.** NIRS has also reported that retiree expenditures stemming from the pension plan payments in 2006 supported more than 79,000 Ohio jobs that paid $4.3 billion in total income to state residents.
- **Defined Benefit pensions support the services provided by local, state and federal governments through the taxes paid on these pensions.** Public employees are also taxpayers. In 2006, taxes paid by retirees and beneficiaries in Ohio directly out of pension payments, as well as taxes attributable to expenditures (e.g., sales tax), accounted for $702.5 million in state of Ohio and local tax revenue, according to NIRS.
- **Defined Benefit pensions play a critical role in reducing the risk of poverty and hardship among older individuals.** Defined benefit pension income saved taxpayers $7.3 billion in public assistance expenditures nationally in 2006 alone because retirees had a regular monthly pension payment that helped sustain them above the poverty level.

For many decades, the public employees of Ohio have been provided with dependable retirement income during economic ups and downs through pensions provided by Defined Benefit Plans. The contributions to pension funds such as STRS Ohio — both from members and employers — are part of the members' compensation package paid in return for work performed. At the conclusion of the members' career, this deferred compensation and investment returns earned by the systems are used to provide pension benefits in lieu of Social Security. Going forward, Ohio's public pension plans — including STRS Ohio — can continue to provide this valued financial security by making reasonable, measured changes.

The starting point for discussions with the Ohio Legislature for needed changes in state statute must be the preservation of the Defined Benefit pensions offered by each system. As noted above, these plans are major economic drivers for the state; are administratively efficient and economical; and provide a stable retirement income for public workers in Ohio, thereby reducing the burden on taxpayers and Social Security.

For further information about NIRS reports, visit www.nirsonline.org.

State Teachers Retirement System of Ohio

Resources

WEB SITE

www.strsoh.org
24 hours a day

contactus@strsoh.org to e-mail

CALL

Member Services Center
1-888-227-7877 (toll-free)
8 a.m. to 5 p.m.
Monday through Friday

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