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| |  | | --- | | **A Perspective of the Evolving Teachers’ Retirement System - How did we arrive at this place?** *by Gayle Harbo*  CONTRIBUTION RATES  Employer Contribution Rates were established in the 1955 act creating the joint contributory system (employee, employer and the state/territory). By 1977 each entity contributed about 7% of salary, so 21% of salary was paid into the system for each member. Between 1966 and 1975, retiree health care evolved from health care available only if the retiree was age 65 and not eligible for Medicare (1966), to free medical insurance for all retired teachers (1975). For retirees reaching age 65, Medicare Part B was required, paid for by the retiree. The monthly Medicare Part B premium, for some, may now be as high as $200 a month. Health care legislation was passed during the time of the pipeline construction as a benefit to encourage teachers to stay in the teaching profession rather than take the more lucrative pipeline jobs.  During 1987 the recommended joint contribution rate for the employer and the state was just over 26%; employees paid 7%. During FY's '86 and '87 of the Sheffield Administration the state failed to fund its share to the TRS system. In FY’88 the state began funneling its share of the contribution through the local school districts, so the contributions became employee/employer.  In 1990 a second tier was established for the TRS system. Tier II was an attempt to contain medical costs and the original provisions required that retirees be over age 60 or have 25 years of membership service before free medical insurance was available. Unfortunately the Legislature tinkered with these provisions and they were changed so a person under age 60 but retired for 8 years also qualified for free medical insurance. In 1991 the employee contribution was raised to 8.65% and remains at this level in 2011 for employees in Tiers I and II. Applying for Medicare Part B at age 65 continues to be a requirement and at age 65 Medicare becomes the primary plan and the Alaska Care insurance cost per retiree drops significantly. Medicare Part D also provides the state Alaska Care system with a quarterly rebate because of the prescription coverage Alaska Care provides.  The Teacher Retirement Systems Board, with the concurrence of the actuary, Mercer, in 1992 established an employer contribution rate of 12% for a long term 20 year period to give employers stability for preparing budgets. Though the recommended actuary rate may have been higher or lower during this time the Board stayed with the 12% rate until 2002, with the exception of 2000 and 2001 when the rate was dropped to 11%. The TRS Board, which was abolished in June 2005 with the passage of SB141, was advisory only, required to met at least twice a year, and its actions could be overruled by the Commissioner of Administration.  FUNDING RATIO – THE COMPARISON OF SYSTEM ASSETS TO SYSTEM LIABILITIES  The funding ratio is a quick way to view the relative health of a retirement system. Its history through 2004 shows lows of 67% in 1980 and 63% in 2004, with highs as much as 101% and 103%. Computing this ratio is different for Alaska than almost all other state systems because the Alaska liabilities include the cost of health care for Tier I and II retirees. Escalating health care costs since the late '90s along with declining investment earnings during the recession of 2000 – 2003 resulted in a rapid drop of the funding ratio. The impact of health care costs was increased by errors of the actuary Mercer. Mercer used a blended rate to predict future health cost increases,, but did not change the assumption every year and when the actuary, Milliman, audited Mercer in 2002 they found that the number Mercer used was 14% too low. In a lawsuit against Mercer, by the state, it was later found that the Mercer actuaries not only erred, but lied and covered up the errors for more than one valuation. The CFO for the Division of Retirement and Benefits said in a September '04 Joint Board meeting that after Mercer addressed this error and finally changed assumptions that “half the increase in employer rates, as they go up, is due to the change in the medical assumption increase.”  Buck Consultants hired in the fall of 2005 as the actuaries for the retirement systems analyzed Mercer's 2004 valuation and found that Mercer's figures for PERS health care costs were off by an additional 7% from the figures cited in the Milliman audit, further lowering the PERS funding ratio. A presentation by Buck Consultants to the ARM Board in March of 2006 shows the health care liabilities of PERS to be more than 3 times the pension liabilities and for TRS the liabilities for pension and health care almost equal.  The deceit of the Mercer actuaries makes one question the validity of any of the funding ratios calculated during the time of their employment.  With two recessions since 2000, it has been difficult for pension systems in most states to maintain funding ratios above 80% (systems with ratios above 80% are considered healthy). Alaska includes health care costs in its liabilities, something not done in most other states. For FY'10 the TRS funding ratio , including booth pension and health care, was 54%.  IMPACT OF LEGISLATION ON SYSTEM LIABILITIES  The TRS system was created by legislation and therefore can be modified by legislation. Several legislative acts have resulted in severe negative impacts to the system. The several impacts result from some members (usually elected officials) retiring, once vested, with little retirement contribution, but with health care for life.  To mention a few:  Several Retirement Incentive Programs ( RIPs) initiated by the legislatures in the late '80s and early '90s allowed system members to retire early by purchasing 3 years of credit. The first program offered in 1986 during the Sheffield administration allowed a teacher as young as 39 years of age to retire and have health care coverage for life. Unfortunately, the actuary at the time, Mercer, indicated this would not harm the system. How wrong they were. There were several subsequent RIP programs which further contributed to the liability with the escalation in the late 90's of health care costs.  Allowing members, other than full time employees (teachers and public employees), to participate in the system. School Board members, city council members, borough assembly members and legislators are allowed to participate in the defined benefit plans of TRS and PERS. While most of these people join PERS there are many also in the TRS system. They contribute very little to the retirement system, but when vested they can retire and receive the $12000 annual benefit of health care for life. In the PERS system the '09 CAFR indicates 9017 retirees receive a monthly pension of $900 or less and in TRS, 1064 receive a benefit of $900 or less, yet they receive free health care for life.  Employees of the legislature prior to May 30, 1987 had to work only 60 days a year for 5 years, a total of 300 work days to vest: after May 29, 1987 they needed to work only 80 days a year for 5 years, a total of 400 work days to vest, yet when they choose to retire they will have full health care coverage. Very, very expensive.  SB141 passed in May 2005, eliminated the PERS, TRS and ASPIB Boards and replaced them with a single board, the Alaska Retirement Management Board. The law also required new hires as of July 1, 2006 to participate in a defined contribution (401K type) plan and closed the defined benefit plans to new entrants. The new law did not affect the Judicial system members (judges). Though the cost of the new DC plan is as expensive or more expensive to employers and the state, it will not provide adequate health care to retirees. The DC plan is also a drain of state resources since employees who terminate after two years can take their money and a portion of the employers contribution with them when they leave. Under the defined benefit plan, employer contributions for terminating employees stayed in the pension trust funds. The turnover rate for DC employees has been close to 40% for PERS members and 30% for TRS members since July 1, 2006.  It is ironic that the legislature which passed SB141 by only 1 vote in the House, depended on the actuary, Mercer, for supporting data and later this same actuary was sued by the State for providing erroneous information regarding health care costs in its valuations. Not only did Mercer err, the actuaries lied about their errors .These errors further compounded the understatement of the liabilities of the systems.  An unintended consequence of SB 141 resulted from the provision that non-vested members of PERS and TRS who had withdrawn their contributions, but were not vested, had to repay the contributions prior to July 1, 2010 or suffer automatic conversion to the defined contribution system. The actuary, Buck Consultants, reported that more than 1200 rehires occurred before July 1, 2010, thus re-establishing the accrued unfunded liability of theses members. Many of these rehires worked only long enough to get vested and then left for other work, but they will get health care for life.  Two bills enacted following SB 141impacted the systems significantly. SB 123 effective July 1, 2007 established Health Trusts for the 4 existing DB plans, separate from the pension plans. This is the first time the health care dollars were separated from pension dollars and contributions are required annually to each fund as determined by the actuary. SB 125 established a single payer plan for PERS employers of 22% and set a rate in statute for TRS employers of 12.56%. It also requires that the state contribute to the DB pension funds the dollar difference generated by these two rates and the dollars required by the actuarial determined rate adopted each fiscal year by the Alaska Retirement Management Board. The adopted rate for TRS is far to low, as can be noted from amounts contributed in the '80s, but the University of Alaska lobbied the Legislature for the lower rate so they would not have to contribute more to their employees in the 401K plan for the Other Retirement Plan (ORP) established in the early '90's to pull employees from the TRS system and give new employees a retirement plan choice.  MEMBERSHIP  A December 1985 issue of TRS Newsbreak states under the “Highlights” section : As of June 30, 1985 there were 9053 active members in the TRS system. Combined employer and State matching contributions in FY '85 amounted to 17.96% of employee gross pay. In 1985 only 1940 retirees received pension benefits.  Changes in the University of Alaska hiring practices and retirement offerings severely affected the TRS membership from the early '90s to date. The Other Retirement Plan offered to TRS members and new employees provided a 401K plan where the University matched employees contribution with the contribution rate adopted by the TRS Board. It offers no health care for retirees. Many University employees do not stay if they do not receive tenure. This worked until 2002 and 2003 when the TRS Board adopted rates of 16%, then 21%. This is the reason the U of A lobbied so hard for the too low rate of 12.56%. Another adverse effect on TRS is the University practice of employment of adjunct teaching faculty who have no benefits and are paid on a per class basis. Most adjuncts have other full time jobs. These adjuncts now teach almost 50% of classes offered.  In 1992 there were only 9238 active members, 3602 retirees. By June 30, 2006 at the close of Tiers I and II to new DB members there were 9710 active members and 9386 retirees, a sign of a very mature system. At the end of FY'10 there were 8226 DB members and 2269 DCR members and 10255 benefit recipients. Instead of the four trust funds prior to July 1, 2006 there are now 14 funds to administer and the cost of administration has gone up significantly, from 2.4 million for FY'07 to almost 6million for FY'10.  IMPACT OF THE DEFINED BENEFIT PLANS ON THE ECONOMY  Five years have passed since the first hires under the Defined Contribution (401K) plan began. Those members of this plan who have completed 5 years can take their money and all the employer contributions and head for greener pastures. The turnover rate is already close to 30% for those employed in the TRS system. Though there are no retirees from this plan, the Division of Retirement Benefits supplement to the Treasury report to the ARM Board shows a combined monthly withdrawal of almost 1million dollars from the DCR employee/employer contributions of PERS and TRS. This money leaving the state does not include the dollars lost in training these short time employees.  What kind of stability does this provided to classrooms, school programs and community? In an environment already challenging with high costs of fuel, gas, electricity and food, not to mention severe weather conditions, the reasons for DCR members to stay are not sufficient if they are also faced with an uncertain retirement. Figures show that the current DCR plans cost the state as much, or more, than the Tier II TRS and Tier III PERS plans which they replaced. If any of these people do stay until retirement they will probably have to apply for Medicaid to help them with health care when the dollars in their Heatlth Reimbursement plans run out.  What positive impact do retirees from the Defined Benefit system have on Alaska's economy? Nearly 2.5 billion dollars a year in pension benefits, health care dollars and other retirement income flow into Alaska each year. This is equivalent to the dollars paid to Alaska fishermen or to the value of mineral production in the state and nearly equal to the dollars spent each year by tourists. (ISER Sept.'06 summary pg 7).  Sixty percent of TRS retirees, receiving defined benefit pensions, choose to stay in Alaska. The pension dollars and health care benefits paid out to these residents amount to almost $300 million dollars . When retirees reach age 65 and qualify for Medicare, additional Federal dollars come to the State to provide that care.  The more than 6000 TRS retirees who choose to remain in Alaska also receive and spend their annual Permanent Fund Dividend in Alaska. Most own their own homes, pay property tax and contribute countless hours of volunteer work to community organizations. If we also consider the more than 22000 PERS retirees ( two-thirds live in Alaska) the amount infused into the Alaskan economy by DB retirees is very impressive.  Benefit dollars flowing into the Alaska's communities provide enough to create almost 8000 jobs for younger Alaskans, many in the health care industry. National studies have shown that for every dollar paid into a public pension fund, six dollars are generated back into the economy. The public perception that tax payers fund these plans need to realize that, according to the actuary, Buck, from 1979 – 2009, in spite of multiple recessions, 71% of pension dollars to pay PERS DB retirees and 73% of the dollars to pay TRS DB retirees, came from a total of the employee contributions and the interest income from the invested funds.  CONCLUSIONS  The State of Alaska established a sound and well funded Defined Benefit plan for Teachers and state employees and with the exception to the two years when the State did not pay its obligation to TRS, it has been committed to provide it retirees with a secure future.  Action by the Legislature has, over the years, been responsible for added provisions to the retirement system that were ill conceived and not well founded or well thought out. In the mid-80's the combined state and employer contributions were greater than those paid in 2005, the year SB 141, establishing a DCR plan for new hires July 1, 2006. In 1987 the combined state/employer contribution was at 26%. employees contributed 7%. Had this rate remained in place the funds would be in great shape. For reasons not known to this writer, separate health and pension trusts were not established when legislation for health care for retirees was passed in 1975. Mercer, the actuary from the mid-80's, provided poor or misleading information to the Administration and the Legislature, first in the 80's when they said the Retirement Incentive Programs would not affect the unfunded liability and again when they made errors estimating health care costs and lied about their errors. It does not take a rocket scientist to figure out that the incentive programs, allowing members as young as 39, to retire and have free health care for life would have a huge detrimental effect on the unfunded liability.  The legislature also allowed people who contributed very little to their retirement, because of low salaries or few days of employment to vest, to belong to the PERS and TRS systems and because of the “health care for life provision” there has been a tremendous impact on the unfunded liability.  Defined Contribution plans do not save money in the long term and provide no security to employees who have dedicated themselves to the State. Money employers contributed is now leaving the state monthly as these DC members terminate. Under a Defined Benefit program this money would stay with the system and earn interest. Two recessions since 2000 have devastated personal accounts, but the long term earnings of the DB funds is about 9% and the money is invested more efficiently and at lower cost than the individual funds of DCR participants.  The powers that be need decide what they want for Alaska's future – for those of us who care deeply about our homes, communities and the future of our children and grandchildren, a stable population, retirees proud to work in their communities and a workforce in our schools that feels committed, innovative and caring are the most important aspects of employment. | |