

PUBLIC PENSIONS: MYTH VS. FACT

TEACHERS RETIREMENT ASSOCIATION OF MINNESOTA

MYTH: Pensions are a huge drain on government resources in Minnesota.

Fact: Nationwide, public pensions currently account for only 2.8 percent of state and local spending. For Minnesota, it's only 1.6 percent. That's according to a recent study by the National Association of State Retirement Administrators (NASRA). Census data compiled by NASRA indicate that the percentage of government spending dedicated to pensions in Minnesota falls below that national average.

MYTH: Taxpayers are on the hook for all of Minnesota's public pension costs.

Fact: Over the past 20 years, investment income earned on contributions made by both members and employers are responsible for 73 percent of

the revenue to pay benefits. Taxpayers (through employer contributions) have paid 14 cents on the dollar of the total revenues of the three statewide pension systems. Deductions from our members' paychecks made up 13 percent of pension plan income. (2011 TRA Comprehensive Annual Financial Reports of TRA)

MYTH: TRA's public pensions are excessive and far better than the retirement average taxpayers can expect.

Fact: While TRA pensions provide members with a monthly income for life, the majority of our retirees receive modest benefits. **The average monthly pension this year is \$2,300.** Seventy-four percent of our members receive under \$3,000 per month. Those receiving larger pensions tend to be teachers who spent their entire 30-plus-year careers in the classroom.

CREATING OPPORTUNITIES FOR A SUCCESSFUL RETIREMENT

There are a lot of misconceptions, misunderstandings, misinformation and flat-out MYTHS about TRA and public pension plans today.

Here are some FACTS to help set the record straight.



MYTH: Public pensions hurt the state's economy.

Fact: TRA actually pumps more money into the state's economy every year than it draws from taxpayers through employer contributions. In fact, benefits paid to Minnesota residents were more than five times the contributions made to TRA by employers last year. The same is true for the Minnesota State Retirement System and the Public Employees Retirement Association. (See map, county breakdown at <http://minnesotatra.org>.)

Even more telling, **state and local taxes paid by PERA, MSRS and TRA retirees, and the holders of the 22,500 Minnesota jobs created by retiree spending, exceeded public employer pension contributions by \$80 million in 2007 alone.** (*Measuring the Impact of Minnesota's Retirement Systems, 2008*)

MYTH: Retirement benefits leave Minnesota because retirees leave the state.

Fact: Eighty-seven percent of TRA retirees remain taxpaying Minnesota residents after they leave public service. Of the \$1.46 billion in benefits TRA paid in 2011, \$1.3 billion was paid to state residents. That's money spent at Minnesota businesses, sustaining and creating jobs across the state. And let's not forget, those

retirees are also paying state and local taxes. (*2011 TRA Comprehensive Annual Financial Report*)

MYTH: Since private industry has adopted the 401(k) retirement plan, it must be the most cost-effective way to pay for retirements.

Fact: Assuming a 5 percent employer and 5 percent employee contribution rate, **the costs to transition to a 401(k)-type plan for Minnesota's public employees would be nearly \$3 billion over the next decade** for all three systems. Costs increase during a transition period because once a plan is closed to new members any unfunded liabilities remaining in the existing pension plan must be paid off over a shorter time frame. (*2011 Minnesota Retirement Plan Design Study*)

One aspect of retirement plan design is rarely addressed -- the *relative cost* of providing a given level of benefits for participants. Here, traditional pension plans like TRA have a distinct advantage over individual account type plans like 401(k)s. According to the National Institute on Retirement Security in its study "A Better Bang for the Buck," **pension plans can deliver the same retirement benefit for an individual at a cost that is 46 percent lower than a 401(k) plan.** That's due to superior investment returns and longevity risk pooling.

MYTH: TRA has an unfunded liability of \$4.9 billion that taxpayers just can't afford.

Fact: Over 78 percent of TRA's liabilities are funded. While TRA does have a \$4.9 billion unfunded liability, it is not due tomorrow. In fact, **that liability is spread out over the next 25 years.** It's like the unpaid portion of a mortgage. Few homeowners have enough cash on hand to immediately pay it all off. That's why they make monthly payments. It's the same with TRA. Regular member and employer contributions, and most of all, investment growth over time, are expected to erase that liability as the plans approach their full-funding dates. (*2011 TRA Comprehensive Financial Report*)

And it's not like TRA is ignoring that liability. Our history shows that we address problems as they occur, with a positive effect on the state's bond rating. Just a few years ago, TRA had no unfunded liability. The severe market downturn changed that. But we have addressed funding shortfalls with periodic benefit and contribution adjustments rather than letting problems get out of hand.

MYTH: TRA and other public pension plans are hiding the true scope of their future liabilities because they don't report their level of funding based on true *market value*.

Fact: TRA does monitor and report its status based on both the market value and actuarial value of its assets. The actuarial value measure smooths the value of assets held over a five-year time span. **This counteracts much of the short-term volatility of the markets**, providing a clearer picture of long-term trends.

As you can see in the chart below, our funding ratios are actually rebounding faster based on market value than they are the way we normally recognize our funding. (2009-2011 TRA Comprehensive Annual Financial Report)

MYTH: Public employees automatically receive a cost-of-living increase in their pensions every year.

Fact: While some retirees do receive annual adjustments in their pensions, **TRA has frozen annual increases until 2013, when the annual increase will be 2 percent.** Under current law, even when the plans reach 90 percent funding, the annual

increase will be a flat 2.5 percent – still slightly below the expected rate of inflation over the last 20 years. (Omnibus Pension Bill, 2010)

MYTH: TRA is going broke.

Fact: While TRA suffered substantial investment losses during the recent recession, even during the depths of the market meltdown TRA had assets of nearly \$14 billion. Those assets **rebounded to over \$17 billion at the end of Fiscal Year 2011.** Legislation in 2010 was crafted to ensure pensions are adequately funded decades into the future. (2011 TRA Comprehensive Financial Report)

MYTH: If something isn't done now, the pension liability for the taxpayer will only get bigger.

Fact: Something has been done. Lost in much of the debate over public pensions in Minnesota is the monumental legislation passed in 2010. **The Omnibus Pension Bill lowered TRA's future liabilities by \$1.75 billion**

(\$6 billion for all three retirement systems) and is already having a profound impact on our funding levels (see below). Approximately 77 percent of those savings came through higher employee contributions and benefit changes for both active members and retirees.

MYTH: The expectation that TRA can earn average investment returns of 8.5 percent is unrealistic and should be reduced to around 4 percent, the average of safe investments such as government bonds.

Fact: Before the recent recession, the State Board of Investment regularly bested an annual return of 8.5 percent on TRA's assets. Those assets earned 23.3 percent in Fiscal Year 2011.

Based on 2011 year-end valuations, **SBI's investments – a mix of stocks, bonds, real estate and private equity – have maintained an annualized return (after expenses) of 10.13 percent**

	MSRS (market value)		PERA (market value)		TRA (market value)	
	2009	2011	2009	2011	2009	2011
Funding Ratio Assets as % of benefit liabilities	65.6%	87%	53.8%	75.2%	59.8%	78%
Unfunded Liabilities Shortfall between assets and liabilities	\$3.6 billion	\$1.4 billion	\$8.7 billion	\$4.4 billion	\$9.3 billion	\$4.9 billion
Assets	\$6.9 billion	\$9.2 billion	\$10.1 billion	\$13.4 billion	\$13.8 billion	\$17.3 billion

2010 TRA Pension Legislation Changes: Funding Stability

Stakeholder	Plan Provision	Previous Law	After 2010 Law	
Active members + employers	Contribution rate increase	5.5 %	July 1, 2011	6.0 %
			July 1, 2012	6.5 %
			July 1, 2013	7.0 %
			July 1, 2014	7.5 %
Inactive members (not teaching and have left contributions with TRA)	Refund of member contributions interest rate	6.0 % interest		4.0 %
Inactive members	Deferral interest rate (for delayed receipt of retirement benefits)	2.5 % - 5 % depending upon age + date of hire		2.0 %
Retired members (return to work and exceed earnings limit)	Interest rate on account	6.0 % interest		0.0 %
Retired members + beneficiaries	Post-retirement increase	2.5 % increase	January 1, 2011	0.0 %
			January 1, 2012	0.0 %
			January 1, 2013	2.0 %
			and thereafter until: Market value funding ratio reaches 90 %	
				2.5 %

over the last 30 years. That's despite two recessions in the past decade.

It is not necessary to force TRA to use a safe investment return of 4 percent, since it has regularly exceeded that rate. Public pension plans invest for the long term because we are in it for the long term. We are not only paying pension benefits today, but will be funding pensions decades from now, and want to invest accordingly.

MYTH: Public retirement systems are hiding the "true" cost of public pensions from taxpayers.

Fact: Most public pension plans are very transparent in their financial and benefit

reporting. Every year, TRA issues and posts online (www.minnesotatra.org) a **Comprehensive Annual Financial Report** that goes into great detail on every aspect of the fund's income and expenses, investment selection and performance, and benefit structure. This report must meet stringent reporting requirements set by the State of Minnesota and the Government Accounting Standards Board. For 13 years, our report has received a *Certificate of Achievement for Excellence in Financial Reporting* from the Government Finance Officers Association of the United States and Canada. The Association also undergoes an annual audit by the Legislative Auditor's Office.

We hope this information helps readers better understand some of the accusations recently leveled against TRA and other public pension plans. All we ask is that everyone take the time to study and evaluate all sides of the retirement plan debate before drawing conclusions about the value of public pension plans today.