Background Information on Teacher Plan Post-Retirement Adjustments

If the standard of living is to be maintained during retirement, the income of the retiree must increase by the rate of inflation relevant for retirees. Although it is an imperfect estimate for retirees, the rate of price increase determined from the Consumer Price Index for Urban Wage Earners and Clerical Workers, published by the Bureau of Labor Statistics, can be used for this purpose. Although the objective of matching inflation seems reasonable upon policy grounds, in practice it may be necessary to compromise because of perceived risk or the cost of fully achieving the standard. The cost of providing the pension must be considered, and post-retirement increases matching inflation can be costly if inflation is high while investment returns are low.

Teachers in Duluth are covered by the Duluth Teachers Retirement Fund Association (DTRFA), while St. Paul teachers are covered by the St. Paul Teachers Retirement Fund Association (SPTRFA). Teachers providing services to areas other than Duluth and St. Paul are covered by the Teachers Retirement Association (TRA). At the present time, there is no consistency between these plans regarding the post-retirement adjustments they provide to their retired or disabled public school teachers and their survivors, and similarly there is a lack of consistency across all Minnesota public plans.

Although there have always been differences, a key factor creating the degree of difference that now exists is the response the various plan systems took following the Great Recession of 2008-2009. That recession had little impact on computed liabilities, but caused a considerable reduction in the assets available to meet those liabilities. In response, the administrators of the Minnesota State Retirement System (MSRS) plans, the Public Employees Retirement Association (PERA) plans, TRA, and DTRFA proposed broad changes to trim plan liabilities, which were enacted as Laws 2010, Chapter 359, Article 1, entitled "Financial Sustainability Provisions." The revisions included revised post-retirement adjustment procedures, vesting requirements, reductions in deferred annuity augmentation and refund interest rates. Contribution rates were increased for some plans. Given the emphasis on trimming liabilities, the usual policy objectives of consistency and equitable treatment of similar individuals were relegated to the back bench.

Following the changes enacted in 2010 and 2011, the post-retirement adjustment procedures for the three defined benefit teacher plans are as follows:

1. <u>TRA</u>. The fixed 2.5% per year adjustment provided in prior law was eliminated. Instead, TRA provided no post-retirement adjustments in 2011 and 2012. In 2013 and thereafter until financial stability is achieved, defined as when the market value of the fund is at least 90% of the accrued liabilities, the full annual benefit adjustment will be 2.0%, and the benefit recipient must be in receipt of the annuity for at least six months before qualifying for a prorated adjustment, and 18 months to qualify for a full adjustment. Once financial stability is achieved, the full adjustment will be 2.5% per year.
2. <u>DTRFA</u>. The procedure in prior law (a fixed 2.0% adjustment plus possible additional investment performance based adjustment based on five-year returns in excess of 8.5%) was eliminated. It was replaced by a transitional provision providing no post-retirement adjustment if the funding ratio based on the market value of assets is less than 80%, a 1.0% increase if the funding ratio based on market value is at least 80% but less than 90%, and a 2.0% if the ratio based on market value is at least 90%. When the funding ratio based on the actuarial value of assets is at least 90%, the transitional system is replaced by an inflation match up to 5%.
3. <u>SPTRFA</u>. Although the SPTRFA was in considerable funding difficulty, its 2010 session proposal to address the situation was quite limited. The only change the SPTRFA proposed was a one-year waiver of post-retirement adjustments. In 2011, SPTRFA law was revised to provide a 1.0% increase until the funding ratio, based on actuarial value rather than market value, if that ratio is 80% or less, and a 2.0% increase if the ratio is at least 80% but less than 90%. When the funding ratio achieves 90% or more, the SPTRFA will begin providing an increase matching inflation up to 5%.

The systems are not identical. Retired Minnesota teachers will be treated differently depending on the plan providing the coverage.