# The Truth about TRS:

## Strong, Stable, and Essential to Texas' Future

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TASA
Texas Association of School Administrators

The Teacher Retirement System of Texas (TRS) has been a cornerstone of the public education system in Texas for more than 70 years. Since 1936, TRS has been the mechanism for providing retirement benefits to public school employees, which has assured the attraction, retention, and retirement security of the education workforce in our state. Over the years, the system has weathered various economic crises while performing its mission. TRS has worked in concert with its members, public education groups, and the legislature to evolve with changing times, address challenges, and meet the needs of an increasingly complex environment.

The latest national stock market crisis has created serious volatility in financial markets both nationally and internationally, and resulted in investment losses for retirement plans, whether defined benefit (DB) or defined contribution (DC), in both the public and private sectors. Though TRS, like many pension funds, suffered heavy investment losses along with most other investors in the market, it continued to fulfill its mission and quickly recovered most of its asset value thanks to strong investment controls, prudent benefits management, and excellent money management. Today, TRS is recognized as one of the healthiest pension funds in the nation.

Unfortunately, much of the recent attention from the media and others has focused on those state and local pension plans that were not well funded or maintained.[1] This has resulted in blanket attacks on public pension funds, without regard to the individual quality of various programs. Instead, a common implication is that DB funds are somehow inherently flawed and should be outlawed or converted to DC plans. This assertion is simply untrue, as demonstrated by the good performance of TRS. TASA, has compiled this information to address specific misconceptions about the TRS pension system, and general misconceptions about public pension systems and defined benefit programs.

## Overview

Currently, there are 1,797 public retirement systems in Texas overseen by the Texas Pension Review Board. The combined net assets of these systems are approximately $175 billion, and total membership exceeds 2.3 million active and retired members.[2]

In November 1936, voters approved an amendment to the Texas Constitution to create a statewide teacher retirement system, which was officially established by the legislature in 1937. TRS is the largest public retirement system in Texas in both membership and assets. The system provides benefits to public school teachers, and other public school employees, and to employees of state colleges and universities.[3]

1. Peng, J., and Boivie, I. 2011. *Lessons from Well-Funded Public Pensions: An Analysis of Six Plans that Weathered the Financial Storm*. Washington, DC: National Institute on Retirement Security.
2. Texas Pension Review Board. 2011. *Guide to Public Retirement Systems in Texas*.
3. Texas Pension Review Board. 2011. *Guide to Public Retirement Systems in Texas*.

TRS serves more than 1.3 million participants, of which over 1 million are public and higher education members and close to 300,000 are retired recipients. The system is a DB plan, and the trust fund is sustained primarily by three sources: contributions by working employee members, state contributions, and investment revenues.[4] It is important to note that of the 1,037 school districts, only 17 contribute to social security for all employees and only 31 contribute to social security for auxiliary or part-time employees only. Thus, the overwhelming majority of district employees are not eligible to receive social security benefits.

The Texas Constitution requires the TRS board of trustees to make prudent investments with system funds and provides the legislature with the authority to further restrict the board's investment discretion. The board is also charged with the general administration of the system.[5]

## Confusion/Misinformation

TRS is a retirement system into which the state and employees pay a percentage of their payroll. Some groups have implied that the defined benefits administered by the system is a gift, or some sort of free grant of salary for not working. This is patently untrue. The retirement benefits received by the members, like any retirement benefits, are earned by years of service and career-long financial contributions to the system by employees and employers.

Generally speaking, DB plans promise to pay a specified monthly benefit for life upon retirement, which can be a specified dollar amount or based on a formula established by law that is based on years of service, salary, and other factors, as is the case in Texas. DB plans are professionally managed. DC plans are those wherein employees are responsible for the management of their individual accounts and there is no guarantee of lifetime retirement income. Under both DB and DC plans, employees contribute a portion of salary to the fund. While there are other differences in each of these plans, the main objective of both is to provide retirement income to participants.

Additionally, some commentators have confused the TRS pension plan with TRS-Care, the retiree health plan.

4. Teacher Retirement System of Texas. 2011. *About TRS* (TRS Web Site). http://www.trs.state.tx.us/info.jsp?submenu=about&page_id=/about/about_trs
5. Teacher Retirement System of Texas. 2011. *Board of Trustees* (TRS Web Site). http://www.trs.state.tx.us/info.jsp?submenu=board&page_id=/about/board_of_trustees

Though both are administered by the TRS system, they are entirely separate financial systems. TRS-Care, like all healthcare systems in the nation, has been severely stressed by issues beyond its control, chiefly medical inflation. TRS-Care has therefore had to seriously adjust benefits and make frequent special requests for funding from the legislature. Legislative support of the TRS retirement benefits actually decreased last session.[6]

As stated above, the TRS pension system has recently been grouped with other public pension plans that have neither the strong actuarial standard nor the strong investment controls and expertise of TRS. Such comparisons are like comparing a strong defined contribution mutual fund with a fund that has clearly been mismanaged and pillaged. No convincing case has been made that DB plans are inherently flawed, nor that DC plans are inherently superior. Any analysis of the quality of retirement systems must, therefore, consider the actual qualities of the plans themselves rather than simply castigating one type of plan or another.

## Current Conditions of TRS Pension Fund

As of June 30, 2011, the system's net actuarial assets totaled more than $115 billion, up from $111 billion in June of 2010. The market value of the system grew from more than $95 billion to over $107 billion during the same time period.[7]

From 2010 to 2011, the most recent TRS actuarial report found that the assets outperformed the assumed rate of return of 8 percent, earning more than 15 percent net of expenses over the last year.[8] This represents $7 billion in gains. In addition, liabilities grew slower than expected due to lower than projected salary increases. Unfortunately, during the recent legislative session, the legislature lowered the state's contribution rate for both years of the current biennium after the fund's actuaries recommended they increase it by 1 percent.

Unlike some pension plans, the TRS plan is a sustainable well-funded program that is successfully weathering the recent major market declines and volatility. If all current contributions from the state, employers, and active employees remain constant and there are no benefit increases for retirees, the trust fund assets are sufficient to make benefit payments through 2075.[9]

6. House Research Organization. 2011. *Texas Budget Highlights Fiscal 2011-12*.
7. Teacher Retirement System of Texas. 2011. *Actuarial Valuation Report for the Year Ending August 31, 2011*.
8. ibid.
9. ibid.

Despite an unfunded liability of $24.1 billion, the system's actuarial funding ratio for 2011 was 82.7 percent, which exceeds the 80 percent industry standard threshold.[10] In addition, the State Auditor's Office (SAO) concluded in a November 2011 report that TRS's financial statements for FY 2011 were materially correct and were presented in accordance with accounting principles generally accepted in the United States.[11]

Critics of public pension plans are calling on reforms that include replacing the traditional DB plans with DC plans. They argue that DB plans are too risky for the state because funding obligations must be maintained over long periods of time and essentially create an entitlement program akin to Medicaid.[12] However, a report issued by the National Institute on Retirement Security (NIRS) found that a major investment advantage inherent in public pension plans is the very long investment range they require.

> *Because of this, funds can withstand short-to-medium-term investment losses, and stick to an asset allocation strategy in a disciplined way through different phases of an investment cycle. This allows pensions to achieve an investment return that is better than individual investors can achieve on their own, on average, over the long term. In addition, unlike an individual who ages and should adopt a more conservative investment strategy over time, pension funds do not age, and are able to take advantage of the enhanced investment returns that come from a balanced portfolio.*[13]

Critics also assert that tax funded programs such as the TRS pension plan "should be predictable and sustainable, and not reliant upon estimators, actuaries, market conditions, or the legislature's resolve to be fiscally prudent."[14] This assertion is ridiculous because standard business accounting practices that cover a myriad of businesses and industries, both public and private, rely upon estimators, actuaries, and/or market conditions in assessing current and future financial conditions and viabilities. Examples include insurance companies, banks, state legislatures (including Texas), mortgage companies, just to name a few. Finally, all state retirement programs, whether they are DB or DC plans, are reliant on state legislatures, because they are the bodies required to craft and pass the state's budget.

The success and long-term sustainability of the TRS pension system is the result of many prudent funding practices and legislative policy decisions made over the years. For example, in 2005, legislation was passed changing the retirement benefit calculation. Members meeting certain age and service credit requirements prior to August 31, 2005, were grandfathered from the changes, but all other members not meeting the grandfather provisions were subject to the following changes in law:

- Final average salary at retirement was changed to the highest five years of salary (instead of three years); and
- Members who take early retirement who are age 55 or older and have 20-24 years of service receive a larger reduction to their annuities.

The statute allowing members to purchase one to three years of additional service credit was repealed effective January 1, 2006, and increasing contribution costs for certain members purchasing out-of-state service credit was mandated. And most notably, the legislature established increased age eligibility requirements necessary to qualify for an unreduced annuity at retirement for those establishing membership in TRS on or after September 1, 2007.

## Conclusion

In the midst of a worldwide economic crisis, the TRS pension plan serves as a stellar example of a strong, well-managed plan that its customers can count on. Its performance and reputation makes it a valuable tool in recruiting and retaining the best job candidates to serve public school students across Texas. Education employees count on their TRS retirement benefits because, under federal law, the vast majority of them are not eligible for Social Security, and the TRS pension plan is their only retirement income option.

The TRS board and the Texas Legislature have implemented policies and procedures over the years to ensure the plan's predictability and sustainability for years to come. Texas educators are depending on state lawmakers to protect the benefits they've earned through years of service and to continue to monitor and make any necessary changes to the system to ensure continued long-term viability. ■

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10. ibid.
11. Texas State Auditor. 2011. *A Report on the Audit of the Teacher Retirement System's Fiscal Year 2011 Financial Statements.*
12. Texas Public Policy Foundation. 2011. *Reforming Texas' State & Local Pension Systems.*
13. Peng, J., and Boivie, I. 2011. *Lessons from Well-Funded Public Pensions: An Analysis of Six Plans that Weathered the Financial Storm*. Washington, DC: National Institute on Retirement Security.
14. Texas Public Policy Foundation. 2011. *Reforming Texas' State & Local Pension Systems.*