Public school teacher retirement plans

Executive Summary

Most public school teachers in the United States are enrolled in state or local pension plans. Missouri law (RSMo Section 169) requires all public school teachers to be enrolled in one of three pension plans, depending on where they teach. The majority of full-time teachers are enrolled in a statewide pension program — Public School Retirement System (PSRS). Both traditional district and charter school teachers in Kansas City and St. Louis must be enrolled in distinct regional retirement plans — Kansas City Public School Retirement System (KCPSRS) or Public School Retirement System of the City of Saint Louis (PSRSSTL), respectively.

Highlights

- Pension plans are most beneficial to teachers who serve for many years within the same state and often are considered a strong teacher retention tool.
- In some cases, non-pension retirement strategies (e.g., 401(k) plans) save money for states and employers. These plans also provide portable retirement funds that are most likely to benefit short-term teachers and teachers who move out of state.
- Two-thirds of states that operate public charter schools, including Missouri, require all charter school teachers to participate in the statewide or local teacher retirement plan.
- For charter schools, the relative value of participating in a pension plan is influenced by program cost, retirement program stability, representation of charter schools on pension boards, and employer penalties for opting out of pension plans.

Limitations

- Because there are few cases where individual teachers can choose whether to enroll in a pension or 401(k) plan, researchers often rely on modeling ideal plans to compare how different retirement strategies would impact a hypothetical teacher's lifetime earnings.
- Additional research is needed to determine how cost inefficiencies and charter school representation on pension boards has changed as charter schools have expanded in Missouri and other states.

Research Background

Employer-sponsored retirement plans can be categorized as defined benefit (i.e., pension) or defined contribution (e.g., 401(k)) plans.

In a *defined benefit plan* (i.e., pension), employers guarantee that vested employees will receive a specified payment amount during retirement. Under these plans, retired employees have the security of a known paycheck, regardless of gains or losses in the employer's pension investments over time. In contrast, *defined contribution plans* (e.g., 401(k)) allow employers to contribute a

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specified amount to an employee-managed account whose balance is paid out upon retirement. Defined contribution plans shift the investment risk to employees, who can choose where to invest their funds, but are responsible for any gains or losses to their retirement account.[1] Pension plans are relatively rare in the private sector but are most common among government employees, including public school teachers.

Tradeoffs associated with defined benefit and contribution plans for teachers can impact retirement income, teacher recruitment and retention, and employer costs.

Retirement income: Because most pension plans require several years of service before vesting and offer benefits based on total years of service, teachers who work for a short time, leave the state, or retire early are the least likely to benefit from a pension plan.[2,3] Because there are few cases where individual teachers can choose whether to enroll in a pension or defined contribution plan, researchers often model hypothetical retirement plans to understand the conditions that would give the highest retirement benefits to individual teachers. When existing pension plans were compared to hypothetical 401K plans in six states (CT, CO, GA, KY, MO, TX), a recent study found that in all states, 77% of educators would make more under a pension than an idealized 401K. Those who would be better off with a 401K are those who don't work long enough in the state to earn the lowest-tier pension.[2] In addition to length of service, financial literacy also impacts how much one can benefit from a defined contribution plan. Retirement income under a 401K, for example, depends on how much the employee chooses to contribute to their retirement and what investments they choose to make over time. Educated individuals with higher incomes are most likely to benefit from increased retirement wealth under a defined contribution plan.[4,5]

Teacher recruitment & retention: Because pensions provide a guaranteed benefits package based on years of service, pensions are often considered to be a strong teacher retention tool. Higher guaranteed retirement income can compensate for lower pay during employment and encourage teachers to serve for longer in order to receive their full retirement benefits.[6-8] However, the time required to vest and the inability to transfer pensions between jobs in different states can discourage the recruitment of potential new teachers who want more flexibility in their employment and retirement plans. Indeed, older employees are most likely to favor pensions, while younger employees are increasingly likely to favor portable, defined contribution plans.[9]

Employer cost: There are some cost savings for employers who manage pooled pension accounts compared to management costs for individual investment accounts. For a full-career teacher—hired at age 25 who works 30 years in the classroom—providing the same level of retirement income through a 401(k) account costs roughly twice as much in Colorado, Kentucky, Missouri, and Texas.[2] However, insufficient returns on employer pension investments can lead to budget shortfalls that impact future teacher pension funding and government spending overall.[10] In the last decade, cash-balance plans have been one alternative approach to provide a guaranteed rate of return for employees under a 401(k)-style contribution plan. In Kansas, the first state to adopt a cash-balance plan for teachers, there is evidence that employer costs were reduced under a cash-balance plan with modest reductions in employee benefits.[11]

Most states require all public teachers (district and charter) to utilize state/local pension plans.

State laws set requirements for public school teacher pension plans and whether or not these requirements vary between district and charter schools. Depending on the state, public charter school teachers may either participate in state pension plans or receive employer contributions toward a defined contribution plan such as a 401K.[12,13] Two thirds of states that operate public charter schools require teachers in charter schools to participate in the statewide or local teacher retirement plan (e.g., IL, KS, OH). Of the states that allow but don't require charter school teachers to use state retirement plans (e.g., FL, MI, OK), all but two states (AZ, NH) require the school to opt in or opt out of the state plan for all employees.

Charter school enrollment in statewide retirement programs varies in states where participation is optional. For example, only around 25% of charter schools participate in the state pension program in Florida and Michigan, while California and Louisiana have much higher participation rates (70-90%).[14] The most common alternatives to pensions are 401K and 403B retirement plans with some level of employer contribution. In states that allow charter schools to opt out of the statewide program, charter schools in urban school districts are slightly less likely to participate in state pension plans compared to rural and suburban schools.[14]

In a 2018 survey, 82% of charter schools that participated in their state retirement plans stated that they chose to use the state plan because it helps recruit and retain teachers. For charter schools that opted out of state pension plans, the most common reasons were lower costs (85%), investment flexibility for teachers (78%), portability of benefits (77%) and increased control over total teacher compensation (61%).[15] The ability for charter school representatives to serve on pension boards can also influence the relative costs and benefits of charter participation in public pension plans.[16]

All certified Missouri public school teachers (district and charter) must be enrolled in one of three state or locally run teacher pension plans.

Approximately 93% of Missouri's full-time public school teachers are covered by the statewide Public School Retirement System (PSRS). While working, teachers contribute 14.5% of their salary to PSRS, which is matched by employers to a total contribution rate of 29% annually. Teachers covered by PSRS are vested after five years and specific retirement benefits depend on (i) years of service, (ii) final average salary and (iii) a state-determined benefit factor (see PSRS Eligibility and Calculations). PSRS currently has 161,862 members and supports 64,595 retirees.[17] In 2020, PSRS retirees had an average age of 58.7 and taught for an average of 22.8 years before retirement.[18] Over the last 25 years, around 62 cents of every dollar used to pay retirees have come from investment earnings, while 20 cents/dollar have come from members and 18 cents/dollar have come from employers.[18]
Public district and charter school teachers in Kansas City and St. Louis must enroll in separate regional retirement plans — the Kansas City Public School Retirement System (KCPSRS) and Public School Retirement System of the City of Saint Louis (PSRSSTL), respectively. Unlike PSRS

members, Kansas City and St. Louis City teachers contribute to and receive Social Security. Under the Kansas City plan, teachers contribute 9% of their salary and employers contribute 12% of their total payroll to the retirement plan. As of January 2021, KCPSRS has 8,728 total members and 47% of members are currently receiving retirement benefits.[19] In the St. Louis plan, employee contributions are currently set at 6.5% and set to increase 0.5% each year until they reach a rate of 9%. Employers currently contribute 15.5% of their total payroll and the employer contribution rate decreases 0.5% each year until it reaches 9%. In 2020, PSRSSTL served 12,859 members and approximately one third (4,477 members) were receiving retirement benefits.[20] A 2014 report identified that cost inefficiencies due to the fragmentation of the Missouri public school teacher pension system, combined with difficulty transferring pension benefits between PSRS, KCPSRS and PSRSSTL can disproportionately impact employee benefits, teacher recruitment and employer costs in urban school districts.[16]

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