

**FOR IMMEDIATE RELEASE: June 7, 2007**

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## **Ohio's Teacher Pension System In Urgent Need of Overhaul**

*Economists say obsolete, costly system is unsustainable,  
undermines school efforts to recruit and retain high-quality teachers*

**[COLUMBUS, OH]:** A study released today by the Thomas B. Fordham Institute warns that Ohio's teacher pension system faces immense and growing fiscal challenges and must be overhauled if it is to meet the needs of current and future teachers, school districts, taxpayers and the state. Most worrying, the authors conclude, the current system weakens efforts by school districts to recruit and retain the high-quality teachers that Ohio's children need and deserve.

*Golden Peaks and Perilous Cliffs: Rethinking Ohio's Teacher Pension System* analyzes Ohio's teacher retirement system, particularly the incentives for work and retirement that are built into its defined-benefit formula. The analysis was conducted by two nationally renowned economists: Dr. Robert Costrell, professor of education reform and economics at the University of Arkansas, and Dr. Michael Podgursky, professor of economics at the University of Missouri.

Four major conclusions emerged from Messrs. Costrell and Podgursky's careful analysis of the state's teacher pension system:

1. The system is obsolete and in need of an overhaul. It was designed for a different era in which employees were far less mobile and life expectancies were considerably shorter. Many individuals retiring today can expect to collect pensions for as many years as they taught.
2. The system is too expensive to be sustainable. Ohio's State Teachers Retirement System (STRS) faces \$20 billion in unfunded liabilities – more than \$4,000 per Ohio household. These unfunded liabilities are commitments made to current and retired employees that the program's current assets cannot cover.
3. The system is out of step with Ohio's current teacher needs, labor markets and career patterns. The pension system provides impressive benefits to teachers who make it through a thirty-year career; however, these benefits come at a serious cost to younger teachers and those seeking to attract, employ and retain them. The system contains powerful, perverse incentives that seriously hinder teacher recruitment and mobility, and that foster generational inequities between younger and older teachers.
4. The system is not likely to fix itself. It will take leadership from state policymakers to reform and modernize the system, repairs that ought to be factored into current discussions of school finance in Ohio. If not, the spiraling costs of the teacher pension system ultimately will impact the state's general operating budget.

“Ohio’s teacher pension system is a ticking time bomb that, left unattended, will lead to harmful consequences for teachers, school districts, taxpayers and the state,” said Terry Ryan, the Fordham Institute’s vice president for Ohio programs & policy. “Of particular concern is the negative impact that the present system already has on school districts’ ability to recruit and retain high-quality teachers. We hope this path-breaking study prompts state officials to make the necessary reforms and give Ohio a pension system suited to the educational needs, fiscal realities and labor market characteristics of the 21<sup>st</sup> Century.”

The study identifies four major shortcomings in Ohio’s existing “defined-benefit” teacher pension system:

1. It encourages early retirement. Over time, the pattern of pension wealth accrual built into Ohio’s teacher pension system has created powerful incentives for teachers to retire in their fifties. The average retirement age for Ohio teachers is fifty-eight, which is well below the current minimum age for regular retirement in the Social Security system, and below the private sector generally. With rising life expectancies, the cost of Ohio’s defined benefit system will continue to rise as increasing numbers of teachers retire at a relatively young age. Early retirement also creates a heightened demand for health insurance, since Medicare coverage does not begin until age sixty-five, putting increasing strain on Ohio’s already severely under-funded teacher retiree health insurance fund.
2. It hinders teacher mobility. Young teachers who move from Ohio’s pension system to another teaching or non-teaching job suffer serious losses in pension wealth. Teachers with ten or more years of seniority suffer very large losses if they move into another line of work or to another state. Additionally, Ohio’s high payroll contribution rate (currently 10 percent and likely to rise) may hinder recruitment of new teachers.
3. It lacks transparency. Ohio’s teacher pension system is remarkably complex and opaque. Relatively few people understand its intricacies, which have allowed the system to evolve into a costly and completely irrational structure – a set of “golden peaks” and “perilous cliffs” in pension wealth accumulation that defy any logic – with limited public awareness of how the system works and what the implications of its workings are over the long term.
4. It is rife with ad hoc fixes. Because the system now encourages early retirement, Ohio has responded by adding ad hoc incentives for continued employment, making the system even more complex and costly. Today, it permits teachers to collect their pensions while continuing to work full time as a teacher (known as “double dipping”) – at a time when the assets of the pension system fall far short of accumulated pension and health insurance liabilities.

Drs. Costrell and Podgursky recommend that Ohio lawmakers rethink the state’s teacher pension system in accord with these essential principles:

- Neutrality. Each additional year of work should add additional pension wealth in a fairly uniform way. There should be no sudden peaks or valleys at any particular point along the years-of-service continuum.

- Transparency. The accrual of retirement benefits should be simple and clear. There should be no opportunities for “gaming” the system.
- Portability. Young professionals change jobs and move around a lot. The current system penalizes young mobile teachers by redistributing income from them to high-seniority incumbent teachers. Portability could help attract more of Ohio’s energetic, talented young individuals to work in education.
- Sustainability. The pension system should be self-funding. It should not be subject to the pattern of benefit enhancements when the stock market is up, followed by funding shortfalls and employee and employer contribution hikes when the market sours. Benefits should be tied to contributions.

With those principles in mind, Drs. Costrell and Podgursky recommend that Ohio transition from its *defined-benefit* teacher pension plan to either a *cash-balance* or a *defined-contribution* plan. These alternative approaches have several advantages:

- They are essentially neutral in the incentive they offer for the timing of one’s retirement or other separation from a teaching position.
- They have much better funding properties.
- They are far more transparent than traditional defined-benefit plans.

The study’s authors note that the Ohio General Assembly has created embryonic cash-balance and defined-contribution programs that, with some modifications to their design, could provide a solid foundation on which Ohio could build an exemplary teacher pension system that better serves both its fiscal and its educational needs.

The complete *Golden Peaks and Perilous Cliffs* report can be viewed and downloaded at <http://www.edexcellence.net/institute/publication/publication.cfm?id=371>.

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