SPECIAL EXECUTIVE DIRECTOR UPDATE

March 14, 2017

The Strength of ATRS

ATRS is now 80 years old. In 1937, the legislature created ATRS as a method to recruit, retain, and reward career educators and those helping deliver the educational curriculum in Arkansas public schools. The Arkansas Teacher Retirement System has never been late on paying a retirement benefit to its members and only pays lifetime benefits to retirees. ATRS has survived several wars, economic downturns, droughts, floods, triumphs, and tragedies. Its mission and focus is to ensure that the schools have the best of the best available for our children.

The ATRS legislative bill package in the 2017 session is a package designed to allow ATRS to continue fulfilling its mission through a financial crisis in the markets or other economic downturns. The ATRS Board is determined to protect ATRS and its members by being prepared for whatever may come. Here are 2 questions that appear to be on members' minds as the session continues.

Question No. 1: Is ATRS financially strong?

Short Answer: Yes.

Question No. 2: Why pass these scary bills unless ATRS is in financial trouble?

Short Answer: ATRS views this bill package as you view purchasing insurance. You hope and do not expect your house to be damaged in a fire or a tornado. At the same time, you stay prepared by spending money for insurance to financially protect your home and valuable assets. The ATRS bill package is essentially an insurance policy to protect the system and allow it to repair damage caused by a financial downturn, accounting changes, or other actuarial events.

ATRS IS FINANCIALLY SOUND

One measure of soundness is looking at investment returns. As of December 31, 2016, ATRS has an investment return of 8.4% since inception. In addition, for 3, 5 and 10 year periods from December 31, 2016, ATRS is in either the top 1% or 2% of pension plans with over one billion dollars under management. The ATRS Board has proven it is a leader in not only protecting, but growing the trust fund that belongs to its members. Thus far in this fiscal year, the ATRS Board has achieved a double digit return that we hope continues to grow through June 30, 2017.

In the 2008 financial crisis, ATRS stood virtually alone in how members were affected as the impact of the financial crisis was handled. The 2008 and 2009 financial crisis was a difficult time for pension plans across the United States. Many cut costs of living adjustments (COLAs), increased employer contribution rates and materially increased member contribution rates. In addition, many lengthened the time before members could retire and decreased multipliers for members.

What did ATRS do? The member contribution rate was not changed and has not been changed for **47 years.** The employer contribution rate remained unchanged and has not been changed for **12 years**. The COLA was not changed, the multipliers were not changed, ATRS did not lengthened the time for retirement eligibility, and in several instances, enhanced benefits such as making the death benefit tax free, removing the earning limitation for retirees, adding post 10 year T-DROP interest, and creating the cash balance account among several others.

On an actuarial basis, ATRS is 81% funded with a 29 year amortization period to pay off its unfunded liabilities. Historically, an 80% funded ratio and a less than 30 year amortization were considered the gold standard in financial strength. ATRS currently exceeds both those standards on the positive side. At the same time, in 2007, few were predicting the 2008 and 2009 financial crisis and the magnitude of that crisis.

MODIFYING THE ATRS "INSURANCE POLICY"

ATRS tries to do a good job of listening to members and also to elected officials in the State. Two things become clear. ATRS members are comforted by ATRS providing lifetime benefits that ensure a member never outlives their retirement and that the ATRS retirement benefit provides a good quality of life for members in retirement.

From elected officials, ATRS clearly understands that the State of Arkansas has many financial priorities and that ATRS cannot look to the State to bridge funding gaps every time a financial crisis or economic downturn occurs. If ATRS requests a higher employer contribution rate, the money has to be redirected from other programs. The programs may be healthcare for the elderly and poor Arkansans, other educational programs, and other priority programs within the State of Arkansas. ATRS has clearly understood that ATRS does not have a blank check from the State of Arkansas. Essentially, ATRS understands that a 14% to 15% employer contribution rate is a ceiling with ATRS having the responsibility to provide quality benefits within that range.

Beginning in 2009, ATRS began addressing costs within ATRS that benefited a few at the cost of the many. Programs were tightened up and the opportunities to manipulate benefits were reviewed and addressed in the 2009, 2011, 2013, and 2015 sessions. The result is that ATRS has a leaner cost structure without affecting basic benefits that ATRS members have always enjoyed and have come to expect.

Beginning in 2013, the ATRS Board also began thinking about what to do understanding that state government expected ATRS to limit itself to a maximum 15% employer contribution. Should ATRS obtain "insurance protection" or be unprepared if another financial crisis were to strike again? The answer was clear. The ATRS Board responded to its fiduciary duty to ensure that ATRS could absorb a financial crisis by temporarily adjusting benefit structures and costs with the ability to restore those adjustments once a recovery occurred in the markets.

The ATRS Board understood that if it did not take appropriate action to maintain financial strength after another financial disruption in the markets, the duty to do so

would fall upon the General Assembly and the Executive Branch. Often when problems are addressed during a crisis, the solutions are far more stark and severe. The view of the ATRS Board was that the best course of action was to obtain and retain solutions outside of a crisis to be used with great discretion if a crisis ever occurred. That view prompted the changes made in 2013 and the changes proposed today in 2017. ATRS appreciates Governor Hutchinson and the Arkansas General Assembly for agreeing that the best solutions are ones that are originated before a crisis begins with the duty placed upon those that have the fiduciary duty to protect the ATRS members every day.

It is important to know that ATRS has a decades old right to change many aspects of benefits already. For instance, ATRS can change its 3 year final average salary calculation to a 4 or 5 year calculation just by a board action. It has not done so. ATRS has also had the ability for many years to lower the multiplier for both contributory and non-contributory service. It has not done so. The ATRS Board has had authority to adjust T-DROP interest rates for many years. It has not done so. This list is much longer with essentially the same answer in every case. It has not done so.

In 2013, the ATRS Board saw that its power to modify benefits needed to be adjusted. In 2013, several existing rights to reduce benefits were modified and some new rights were established. Apparently most members were not aware of these changes since in 2017, modifications of these changes have created a high level of concern.

For instance, in 2013, the ATRS Board recognized its existing ability to reduce the multipliers. The law before 2013 provided that if the ATRS Board reduced the multiplier for contributory or non-contributory service, it reduced all of a member's multipliers, even for service earned years or decades earlier. **Thanks to the ATRS Board, the 2013 law on multipliers ensured that all multipliers earned are final unless increased.** The ATRS Board ensured fairness to members in the 2013 law, and at the same time, obtained authority to adjust the multiplier slightly lower than its previous authority, obtained authority to restore any reduced multipliers, and limited the authority to reduce the multiplier to only when ATRS had over a 30 year amortization period. From the time that law passed, ATRS had authority until the last few months to decrease the multiplier and **did not do so**.

The 2017 proposed change in the 2013 multiplier law is to change from a 30 year amortization period to an 18 year amortization period based upon the recommendation of ATRS' actuaries that the goal of ATRS should be to target an 18 year amortization period as a long term goal. In fact, if you look at the legislation being considered in 2017 that has created a high level of concern, virtually all of it is merely adjusting the 30 year amortization goal to an 18 year amortization goal to ensure ATRS remains strong.

I could list every bill and essentially say the same things to shorten this special Executive Director Update versus lengthening it. I will just say that ATRS Board cares about members and works hard to protect members. ATRS is financially strong and has proven that it stands out among other teacher retirement plans in the country. The New York Times recently had an article rating the teacher retirement plans across the states. ATRS was ranked in the top 6 teacher retirement plans in the United States. That was not an accident, but a reflection of the kind of board that members have protecting them. The ATRS Board "purchased" an insurance policy to protect members in 2013 and currently is modifying that policy to reflect recommendations from its actuaries. That insurance policy exists for the same reason your insurance policy exists on your home and valuable property. The policy exists as a protection with the intent never to use the policy unless required. You are prudent to purchase the insurance on your homes and ATRS is prudent to "purchase" its insurance on the system that pays lifetime benefits to all retirees.