Senate Finance Committee

House Bill 64

Interested Party Testimony

Michael Nehf, Executive Director

State Teachers Retirement System of Ohio

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Good morning, Chairman Oelslager, Vice Chairman Coley, Ranking member Skindell and members of the Senate Finance Committee. I am Michael Nehf, Executive Director of the State Teachers Retirement System of Ohio. I appreciate the opportunity to appear before the committee this morning for the purpose of speaking to language in Substitute House Bill 64 that would set the Alternative Retirement Plan (ARP) mitigating rate at 4.5%. STRS Ohio is concerned about the effect that this provision will have on the system’s fiscal integrity.

Up until 1997, all Ohio educators participated in STRS Ohio’s Defined Benefit Plan. In 1997, House Bill 586 requiring all Ohio institutions of higher education to offer ARPs through private vendors became law. Participation in an ARP would be in lieu of participating in STRS Ohio. When House Bill 586 was passed and enacted, the legislature correctly recognized ARPs would have a negative financial impact on STRS Ohio — at least in part a negative impact on the funds available to pay off STRS Ohio’s unfunded liability. The mitigating rate is a portion of the employer contribution that is used by the retirement system to offset the negative impact of participation in a defined contribution plan. In 1997, the mitigating rate was set at 6%.

Last year, the State Teachers Retirement Board considered an increase to the mitigating rate for the DC Plan administered by STRS Ohio. This followed a study by the system’s actuarial consultant, who calculated the mitigating rate using two methods — the first resulted in a mitigating rate of 7.2%, and the second resulted in a mitigating rate of 12.03%. The actuary strongly recommended an increase in the mitigating rate of at least 1%. Consistent with the actuary’s recommendation, and recognizing the importance of constituent support around this issue, STRS Ohio was set to compromise and consider a 1% increase in the mitigating rate — from 4.5% to 5.5%. At the same time, as a matter of law, the mitigating rate for the ARP program would also have increased. However, before the board took action on this measure, the legislature approved a moratorium on the mitigating rate applied to ARPs at 4.5%.

As you meet and consider this language today, the provision in House Bill 64 limits the ARP mitigating rate to 4.5%. STRS Ohio’s concern is that its actuary recently affirmed its recommendation from last year — that the mitigating rate be increased to a minimum of 5.5%. The State Teachers Retirement Board voted in April to phase in this increase over the next two fiscal years — so that the mitigating rate would become 5% on July 1 of this year and then 5.5% effective July 1, 2016. As a fiduciary to the retirement system, the actuary believes that 5.5% is an appropriate rate at this time — not 4.5%. Following the board’s action in April, STRS Ohio has been communicating this change with schools throughout the state to prepare them for the July 1, 2015, implementation of the first phase of the increase.

As those of you who served on this committee last year may recall, when the moratorium was put in place, there was also a requirement that the Ohio Retirement Study Council research the historical impact of the mitigating rate and whether its purpose is being served, and, to report its findings by the end of last year. The Council staff submitted the report at the Council’s December 2014 meeting and in that report it is confirmed that participation in ARPs has a negative financial impact on STRS Ohio.

Mr. Chairman, members of the committee, when I appeared before you last year the board and I were concerned that the ARP mitigating rate was being capped when an increase was necessary to help preserve the fiscal integrity of the system. However, we understood that the Inter-University Council had expressed concerns with the STRS Ohio’s action.

Now, a year later, the ORSC study has been completed and STRS Ohio has worked with the Inter-University Council — who no longer opposes the phased-in increase of 1% over the next two fiscal years — and yet language in House Bill 64 would again cap the mitigating rate at 4.5%. If the committee feels strongly that a cap should be put in place at this time, I ask that you consider a compromise mitigating rate of 5%. This would be consistent with the actions that schools have taken to prepare for a half-percent increase in the mitigating rate effective July 1, 2015.

In summary, I ask you to consider these four key points:

* The ORSC’s December 2014 study confirmed that ARPs have a negative financial impact on STRS Ohio.
* In January 2015, STRS Ohio’s actuarial consultant recommended an increase in the mitigating rate to help preserve the fiscal integrity of the fund — and the increase we are seeking is at the low end of the actuary’s recommendation.
* STRS Ohio worked with the Inter-University Council of Ohio earlier this year on a mitigating rate proposal and the IUC no longer opposes the modest increase we are seeking.
* In April 2015, following the Retirement Board vote to increase the mitigating rate in half-percent increments in 2015 and 2016, STRS Ohio communicated this change with schools throughout the state, who have been preparing their systems to increase the mitigating rate to 5.0% beginning July 1, 2015.

Chairman Oelslager, Vice Chair Coley, Ranking Member Skindell and members of the Senate Finance Committee, on behalf of the board of the State Teachers Retirement System and the nearly 498,000 active, inactive and retired members they represent, thank you for your time and attention to this important matter. I would be pleased to answer any questions the committee members may have.