



Employer Contribution Governance Structure and Pension Funding Experience

A key factor in the pension funding experience is the myriad governance and funding policy structures in place to ensure pension contributions are made. Beginning with the paper published in 2015, "[The Annual Required Contribution Experience of State Retirement Plans](#)," NASRA grouped retirement systems based on how employer contributions to public pension plans are determined. This analysis employs the use of four broad classifications: *Actuarially Determined*; *Statutorily Fixed*; *Actuarially Determined with Limitation*; and *Other*, which, for purposes of this analysis includes plans governed by funding arrangements that differ from the three preceding categories, such as a state law or policy that supersedes an ADC requirement.

Figure A: Average ARC/ADC received for each employer classification: Actuarially Determined, Fixed, Actuarially Determined w/Limitation, and Other, FY 01 to FY 21

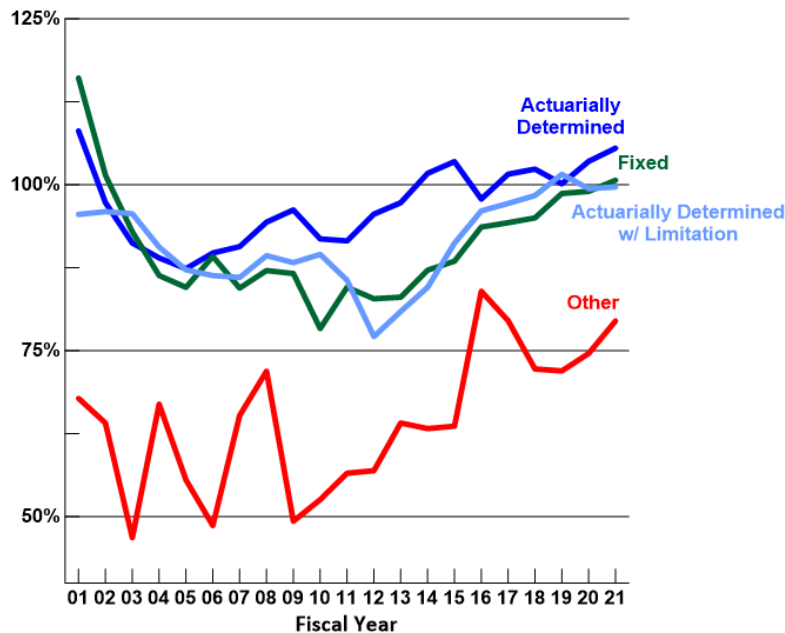


Figure A illustrates the variation in the ARC/ADC received among plans in each of the four classes.

- Following the sharp market decline that began in March 2000, the average percentage of contributions received by the plans in the *Actuarially Determined* category fell below 100 percent in FY 02, remaining below 100 percent, but above 89 percent, for 12 years before rising above 100 percent beginning in FY 14.
- The average ARC/ADC received by plans whose contribution basis was Actuarially Determined With a Limitation, (such as an annual increase of no more than 1.0 percent of payroll), is 86.6 percent for the measurement period.

- The average experience for plans whose employer contribution basis was *Statutorily Fixed* received an average of 90.7 percent of their ARC/ADC during this period.
- By contrast, the average ARC/ADC received by plans in the *Other* category, in which cases there is no legal requirement for the employer to make a particular contribution, 63.8 percent for the measurement period.

The *Fixed* moniker is a misnomer for some plans, specifically those that have the authority—or, in some cases, the legal requirement—to either propose or adjust on their own contribution rates or benefit levels, or both, should the plan’s actuarial condition fall outside a specified actuarial range. Such authority can have the outcome of reducing, or eliminating, the gap between the plan’s fixed contribution and its actuarially determined contribution.

Following are three examples of fixed rate plans that have legal authority to make adjustments to their plan design or financing structure or are required to propose such changes.

- 2013 legislation authorized the board of the Arkansas Teachers’ Retirement System to make changes to benefits and contribution rates as needed to maintain an unfunded liability amortization period of 30 years or less; this threshold was reduced legislatively to 18 years in 2017. Also in 2017, the Arkansas TRS board used this authority to bring the plan into compliance with this amortization threshold by approving graduated increases in contribution rates for employers and employees; and reducing benefit levels through a lower retirement multiplier and a longer final average salary period used to calculate retirement benefits. As a result of these changes, Arkansas TRS has received at least 95 percent of its ADC since FY 16.
- Ohio statutes require statewide pension plans—PERS, Police & Fire, SERS, and STRS—to submit a proposal to reduce their amortization period to below 30 years when the plan amortization period exceeds that threshold. In 2017, in response to a funding level that exceeded 30 years, using authority to make such changes granted by the Ohio Legislature, the STRS board voted to reduce the COLA to zero to preserve the fiscal integrity of the system and to bring the plan’s amortization period within the 30-year threshold. Since enacting this change, the percentage of ADC received by Ohio STRS has been consistently above 100 percent.
- South Dakota statute requires that when the fair value funded ratio of the South Dakota Retirement System (SDRS) falls below 100 percent and the actuarially determined contribution rate exceeds the statutory rate (6.0 percent; 8.0 percent for public safety personnel), the South Dakota Retirement System must recommend to the governor and legislature corrective actions—which can include benefit changes—to increase the funding level and reduce the plan cost. This statutory requirement was employed in 2017 to modify SDRS cost-of-living adjustment provisions to bring the plan’s funding condition and contribution rates back into compliance. The flexibility to adjust liabilities to a level supported by the plan’s fixed contribution rate has resulted in the SDRS reporting receipt of at least 100 percent of its ARC/ADC in nearly every year of the measurement period.

These and other examples illustrate that a fixed contribution rate in some cases does not, by itself, render a pension plan unable to affect its actuarial condition. A fixed contribution rate provides participating employers the benefit of stability and predictability of the plan's cost, and a mechanism for adjusting to ensure the plan remains within designated actuarial targets can balance the constraints of a fixed contribution.

Figure A also illustrates the practical effect employer contribution policies had on public pension funding beginning in FY 01. Funding policies for the employers in the *Other* category lacked legal authority to require employers to make an adequate contribution, and contributions from these employers remained well below 100 percent for the duration of the measurement period. Employers relying on fixed contribution rate policies, or whose policies are actuarially-based but with limitations, received a greater percentage of required contributions than those in the *Other* category, as these policies provided a legal requirement to make contributions. Figure A also shows that as the level of required contributions rose, contributions received by most plans in the *fixed* and *actuarially determined with limitation* categories also rose, indicating that these legal requirements serve as a basis of support, even if they were insufficient to fully fund the benefit.

By contrast, employers with a funding policy that includes requiring the actuarially-determined contribution predictably had the highest contribution rate experience: their contributions increased as required contributions rose. The 10-year period during which the average contribution received by plans in the ADC class fell below 100 percent illustrates that even a legal requirement to pay the actuarially-determined contribution does not, by itself, ensure that the full required contribution will always be made.

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