New study explores fiscal issues related to NYC teachers retirement system

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The volatility of the financial markets amid the COVID-19 pandemic has significant implications for taxpayer-supported pension systems nationally.

The Marron Institute of Urban Management at New York University today issued a new report looking at fiscal issues and risks related to the New York City Teachers' Retirement System (TRS), the second-largest of New York City's five major retirement systems as measured by assets.

With city contributions totaling $37 billion in 2018, or 6 percent of tax revenue, TRS has two important characteristics that distinguish it from most other public pension plans in the nation, the report's authors—Marron Institute collaborators Don Boyd, Gang Chen and Yimeng Yin of The State and Local Government Finance Project, Center for Policy Research, Rockefeller College of the University at Albany.

First, like other New York City pension plans, its contribution policy is more conservative than the typical public plan in the sense that city contributions rise relatively rapidly in response to investment shortfalls. This protects the solvency of the pension plan. The trade-off is greater risk to the city budget of sharp contribution increases in short time periods, relative to other commonly used contribution policies.

Second, in addition to their regular retirement benefit, TRS members may contribute to a Tax-Deferred Annuity (TDA) program that offers guaranteed fixed returns backed by the defined benefit pension fund and thus by city taxpayers. The guaranteed rate for most members is 7 percent, set by the state legislature. It is well above guaranteed fixed returns that may be purchased in the private market, which are currently 2 to 2.5 percent or less. TDA assets are invested by TRS along with regular defined benefit pension assets. The guarantee provides valuable benefits to plan members but creates special risks to the city. It does not have the constitutional protection that the regular retirement benefit has and therefore is more directly under the control of state and city policymakers.

If TDA assets earn more than the guarantee, the additional earnings accrue to the TRS pension fund, keeping city contributions funded by taxpayers lower than they otherwise might be. If TDA assets earn less than the guarantee, the pension fund must make up the difference, increasing costs to the city and its taxpayers, according to the report, titled "The New York City Teachers' Retirement System: Fiscal Issues and Risks."

Stock market declines of recent weeks illustrate the potential risk to city taxpayers. If TDA assets fall short of the guarantee by 10 percent—for example, if TRS were to lose approximately 3 percent in 2020—then TRS will have to make up the difference. TDA had approximately $25 billion of assets at the end of 2019, so this would mean a guarantee payment of approximately $2.5 billion, ultimately funded by city taxpayers.

City policymakers need to understand the risks that City pension funds create, and make informed decisions about those risks, the report's authors urged, noting the report provides valuable information designed to help them to understand those risks better.

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