

Actuarial valuation shows COLA change, investment returns led to funding gains

STRS Ohio's annual valuation report, prepared by Segal Consulting, shows pension funding levels improved during the fiscal year ending June 30, 2017. The report provides a detailed look into the financial health of the pension fund. The most common ways to express the system's financial condition are through the funded ratio and the funding period. The valuation report shows the funded ratio — the

value of assets compared to actuarial accrued liabilities (benefits earned by members of the system) — improved to 75.1% from 69.6% the previous year. The funding period — the time needed to pay off the system's unfunded

liability under current assumptions and benefit levels — also improved, decreasing to 18.4 years from 26.6 years in the previous year's report. Segal shared that without the board's action to reduce cost-of-living increases granted on or after July 1, 2017, to 0%, STRS Ohio's funded ratio would be just 66.6% and the funding period would have increased to 50.4 years — well above the state of Ohio's 30-year target.

STRS Ohio executive director Michael Nehf said the positive report is a welcome sign, but would like to see further funding improvement. "Reaching a 75% funded ratio is a step forward for STRS Ohio, but the funding position needs to further strengthen to improve our resiliency in a volatile market environment" said Nehf. Despite the improvement in the funding status, because of the volatility around investment returns, staff estimates STRS Ohio faces about a 30% chance that the pension fund could drop below a 50% funded ratio in the next 10 years.

Investment returns for the 2017 fiscal year topped 14% and also helped account for part of

the funding improvement. Segal noted that the pension fund has a net \$155 million in deferred investment gains that will be recognized over the next three years. STRS Ohio uses a common actuarial technique called "smoothing" to spread investment market volatility over a four-year window rather than a one-year "spike." The previous year's valuation report showed a net \$2.8 billion in deferred losses to be recognized.

The valuation report measures two sets of assumptions — economic and demographic — against the retirement system's actual experience from the past year. Economic measures include the rate of inflation, return on assets, salary increases and payroll growth. Demographic measures include retirements, disability inceptions, withdrawals and mortality (the number of deaths among active members and benefit recipients).

The report included the updated actuarial assumptions the board adopted in March 2017. These new assumptions included reducing the expected investment return to 7.45%, updating to generational mortality tables to recognize that STRS Ohio retirees are living longer, reducing the inflation assumption and reducing overall expected payroll growth.

Other key points from the report include:

- STRS Ohio's Defined Benefit and Combined Plans paid about \$7 billion in benefits during the 2017 fiscal year.
- The unfunded actuarial accrued liability decreased to \$23.9 billion from \$30.6 billion.
- Total covered payroll increased by 4.1%, exceeding the system's payroll growth assumption.

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Health Care Fund status update

The annual actuarial valuation of STRS Ohio's Health Care Fund shows that strong investment returns and good claims experience had a positive effect on the fund. In addition, limiting future subsidy increases for Medicare enrollees to 6% and freezing future subsidies for non-

Medicare enrollees significantly improved the funded status. The fund balance as of Jan. 1, 2018, was \$3.69 billion — an increase of \$469 million from the previous year's valuation report. Segal Consulting said assuming the fund earns 7.45% in all future years and all other plan experience

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Board approves 2019 health care premiums

The State Teachers Retirement Board approved health care program and dental and vision premiums for 2019 at the May board meeting. Staff works with health care consultants and actuaries to develop expected costs for the health care plans. Lower than anticipated health care claims during the review period for STRS Ohio's self-insured plans had a positive impact on 2019 premiums for these plans. This means premium increases will be smaller than the consultants' original projections. About 92% of enrollees will have a \$0 increase. Premiums for 2019 are now posted on STRS Ohio's website.



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matches assumptions, the fund is now projected to remain solvent for all current members.

The valuation also showed that benefit payouts for 2017 totaled \$517 million, an average of more than \$1.4 million per day. The positive news for the Health Care Fund is tempered somewhat by the volatile nature of various components of the valuation report. Examples of these components include investment returns, government subsidies and rebates, plan enrollment and utilization, and Affordable Care Act taxes. These were areas that led to gains for the Health Care Fund in 2017, but are not predictable for 2018 and beyond. The health care valuation report is completed on an annual basis; however, the timing of the next health care valuation has been moved to July 1, 2018, to align with the next pension valuation.

In the months following the health care valuation, the board has discussed steps that STRS Ohio could consider to reduce the investment rate of return volatility for the Health Care Fund. Staff shared potential pros and cons of lowering the investment risk in the fund portfolio. Staff shared that with no current employer funding, the Health Care Fund is more susceptible to the economic cycle, and reducing investment risk means reducing the severity of possible negative investment return outcomes. However, reducing investment risk would also reduce some potential gains if investment markets continue to climb significantly above current levels. The board indicated it will continue its discussion on the Health Care Fund at future meetings.

Benefits, Investments and Financial News Update

STRS Ohio investment returns, costs stack up well against peers

In December, CEM Benchmarking, a leading global research company, shared the results of its 2016 investment benchmarking study with STRS Ohio. The report compared investment data — both performance data and costs — for the five-year period ending Dec. 31, 2016, from more than 300 pension funds from around the world. Results of the study showed STRS Ohio's five-year total return of 9.7% ranked in the top quartile of CEM Benchmarking's U.S. public fund universe. STRS Ohio's strong performance was primarily due to its asset mix, which has a higher weighting in U.S. stocks and a lower weighting in fixed income than most other funds.

STRS Ohio also ranked third in its peer group of 17 large U.S. public pension fund sponsors for lowest investment costs.

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STRS Ohio's strategy of using internal investment managers for about 70% of the system's assets was the primary reason for its overall low costs. The report showed that STRS Ohio saved about \$101 million in calendar year 2016 by using the internal management approach. The savings is based on the peer group's median external management costs.

For years, STRS Ohio has been recognized for its cost-efficient method of relying heavily on internal asset management. In recent years, other large public pension funds, including the California Public Employees Retirement System, as well as the California and Texas Teachers Retirement Systems have expressed plans to follow suit and increase their use of internal management to gain cost efficiencies.

Member survey results reveal impressions of STRS Ohio

Research with STRS Ohio members and retirees show that 95% of retirees and about 80% of active members have positive overall impressions of the Retirement System. The membership survey was completed in late 2017. Other notable findings included:

- Most retirees (85%) and active educators (72%) indicated STRS Ohio has earned the trust and confidence of its members.
- Compared with last year, fewer active members (61%) consider the pension they expect to receive an excellent/good value considering the amount they contribute to the system, while 86% of retirees consider their pension an excellent/good value.
- Most members continue to be satisfied with STRS Ohio communications — including email updates — with about eight out of 10 active members and nine out of 10 retirees indicating that STRS Ohio keeps them well-informed about pension- and retirement-related issues.
- 75% of active educators are setting aside additional savings for retirement — in addition to their retirement plan with STRS Ohio and the money they're saving for health care.
- More than nine out of 10 retiree households reported at least one source of income in addition to their STRS Ohio pension. Investments and spouse's pension are the most common forms of additional income. Survey respondents indicated on average, STRS Ohio provides 58% of retirees' household income.



Building your nest egg

If you are looking for an optional investment account in addition to your STRS Ohio retirement plan, you might consider an individual retirement account (IRA), a 403(b) plan or a 457(b) plan. These are individual investment accounts that can supplement the retirement income that you will receive from STRS Ohio. These accounts each have their own plan characteristics, such as maximum annual contribution limits, withdrawal limitations and fees.

A financial advisor can help you determine if one of these plans is right for you. The Ohio Public Employees Deferred Compensation Program is a supplemental 457(b) retirement plan that is available to all Ohio public employees. You can learn more about this option at www.ohio457.org.

FAS Final average salary limitations can affect your retirement benefit

Members who plan on retiring in the near future and are considering taking on extra duties to increase their salary should be aware of the limits on earnings used to calculate the final average salary (FAS) that is used in the retirement benefit formula.

FAS is the average of your five highest years of earnings — subject to certain limits. Many members do not realize that there are limits on earnings that can be used in the calculation of FAS. These limits are required by law and exist to help ensure that members' retirement benefits have been properly funded.

Working extra duties will allow you to receive more annual income during your working years, but may not always provide a higher FAS at retirement because of the statutory provisions. Your FAS will be limited if the extra earnings you receive cause the percentage increases in your two highest years of earnings to be greater than the increases in the three years before the earlier of the two highest years. Compensation for a partial year may also be limited.

Examples of extra duties in two highest years of earnings that may trigger a limit to your FAS:

- **Accepting a supplemental contract, summer school teaching (K-12) or summer session (college and university) that was offered to all qualified educators.**
- **Assuming extra duties that required working extra days or hours.**
- **Working additional duties for three years, but not teaching through the last day of the school year in the last year.**
- **Performing services for the school district for years with no pay and then getting paid for those duties only in the last year, last two years or last two years and a partial year.**
- **Receiving a supplemental contract for services performed as a mentoring teacher as part of the licensing requirement for teachers in your district.**

- **Working overload assignments in addition to your regularly salaried employment, even if that was required.**
- **Accepting new employment or more pay in a position covered by the Ohio Public Employees Retirement System or the School Employees Retirement System in addition to your employment covered by STRS Ohio.**
- **Being assigned extra duties in the last two years as a result of a collective bargaining agreement.**
- **Accepting an interim or short-term position that results in a significant increase in pay.**
- **Accepting a new part-time position with another STRS Ohio-covered employer.**

These are some common reasons for FAS limits, but they are not the only examples. Remember, while all of these earnings may not be included in your FAS, at least a portion of the earnings are included in many cases — resulting in a higher FAS than if the extra duties had not been performed.

Please be sure to discuss your future retirement with an STRS Ohio benefits counselor at least twice before retirement. If you earn additional amounts beyond your contract for regular teaching duties, you should talk with a counselor at least four years before you retire. Also, if you do not plan to work through the last day of your contract in your last year of teaching, be sure to discuss this plan with a benefits counselor before your retirement. For more information or to schedule a counseling session, call STRS Ohio toll-free at 888-227-7877.

MEMBER EDUCATION OPPORTUNITIES

Location announced for summer *Information Fair*

We're bringing our popular STRS Ohio *Information Fair* to the Holiday Inn in Perrysburg, on Wednesday, Aug. 8, from 10 a.m. to 1 p.m. Come learn about your STRS Ohio benefits, assess your retirement readiness and identify next steps for reaching your retirement goals. Attend retirement planning presentations, visit information booths and obtain answers to your STRS Ohio benefits and retirement questions. **Registration begins June 24.** Register at www.strsoh.org using your Online Personal Account or by calling 888-227-7877 (toll-free).

July retirement planning programs and counseling sessions offered

STRS Ohio will be traveling the state this summer offering our retirement planning seminars as well as benefits counseling sessions. See below for further information.

Beyond the Classroom is for Defined Benefit Plan participants five to 10 years from retirement. Get details about retirement options and financing retirement. Learn about calculating your final average salary, retirement benefits, plan of payment options and health care funding.

Financial Fitness: Your Pathway to Retirement is targeted to STRS Ohio members who are early- to mid-career. Obtain details about improving your overall financial health by budgeting and eliminating debt and integrating other retirement income sources.

An individual counseling session offers the opportunity to review what you'll want to know leading up to your retirement date. We recommend this appointment three years before and again six to 12 months before retirement. STRS Ohio will be in Akron and Cincinnati this July, but also offers appointments at our Columbus office and by teleconference.

For dates, times and locations, please go to www.strsoh.org and select "Counseling & Seminars" under the During Your Career section. Advance registration is required and begins 45 days prior to the event date. Register using your Online Personal Account or by calling 888-227-7877 (toll-free).



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SOCIAL



Robert A. McFee and Jeffrey Rhodes elected to Retirement Board; Mayerfeld reappointed; new representative seated

Robert A. McFee and Jeffrey Rhodes were elected to contributing member seats on the Retirement Board in voting that concluded on May 7. The term for these seats runs from Sept. 1, 2018, through Aug. 31, 2022. McFee is a mathematics teacher for Willoughby Eastlake City Schools and Rhodes is a technology education teacher for North Royalton City Schools.

Earlier this year, Treasurer of State Josh Mandel reappointed Yoel Mayerfeld to an investment expert seat on the Retirement Board. Mayerfeld is the Principal & Managing Director of Chase Properties, an Ohio-based company with offices in Beachwood, Ohio. The term for this seat runs through Jan. 7, 2022.

In April, the Speaker Pro Tempore of the Ohio House of Representatives and the President of the Ohio Senate jointly appointed David Gruber to an investment expert seat on the Retirement Board. Gruber is the director of Risk Advisory Services for Holbrook & Manter, CPAs. The term for this seat runs through Nov. 4, 2020. The seat was formerly held by Craig Brooks.

Online communication options save STRS Ohio printing, postage costs



STRS Ohio now offers an electronic version of *STRS Ohio News for Active Members* delivered straight to your email account. Nearly 70,000 members now receive an e-newsletter instead of a paper copy, saving the retirement system the costs of printing and mailing these materials. Members who have an email address on file with STRS Ohio should receive an electronic version of the newsletter in their inbox. To opt out of the printed version, log in to your Online Personal Account on the STRS Ohio website (www.strsoh.org) and indicate that you prefer to receive newsletters by email. STRS Ohio is also pleased to offer the online availability of the *Annual Statement of Account*, sent to members in mid to late September each year. You may opt out of the printed *Annual Statement* via your Online Personal Account.

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