



Texas TRS: Examining the 7.25% Assumed Rate of Return

In July 2018, the Teacher Retirement System (TRS) of Texas lowered its assumed rate of return from 8% to 7.25%. The TRS board voted for the lower rate at the advice of actuaries tasked with ensuring sound funding policy for the plan. The change is based on lower projections for what TRS investment returns can earn from its current portfolio. The adjustment to a lower assumed rate of return—and subsequent increase in required contributions—are important for ensuring long-term pension fund stability. The shift is consistent with national trends and will not result in changes to current retirement benefits.

1. An accurate assumed rate of return is necessary for the long-term stability of a pension plan.

- ❖ Financial experts are projecting long-term investment returns below 8%, which means the fund's assets aren't likely to grow at the rate previously assumed. Keeping an unrealistically high investment assumption would mean contributions into the plan will ultimately not be sufficient to pay retired teachers' benefits in the future.
- ❖ Lowering the rate to 7.25% also increases the recognized value of TRS promised benefits—known as projected liabilities or obligations. This will make it necessary to increase contributions if the plan is to maintain financial security for retired teachers.
- ❖ Adopting a more realistic projection of investment returns and the estimated value of pension benefits is important to ensuring Texas will uphold promises made to teachers.
- ❖ Keeping an 8% assumed rate of return would have hidden the actual hole needed to be filled to ensure that 100% of promised benefits are paid to beneficiaries.

2. The lower rate does not cut or change retirement benefits.

- ❖ The recognition of higher liabilities in no way changes the actual benefits promised to TRS employees and retirees. This is simply an accounting method change that results in a more conservative estimated value of future pension benefit payments.
- ❖ What will change is the cost of the program. To ensure benefits are fully paid, TRS will need to consider options to secure more money annually than previously calculated.
- ❖ While the change to the assumed return may delay the timeline for retirees receiving a cost of living adjustment (COLA) on their benefits, keeping the status quo and subsequently paying a COLA would have likely caused additional long-term funding harm to TRS.

3. TRS's move to a lower rate is consistent with national trends.

- ❖ According to the Center for Retirement Research, the national average for assumed rates of return for public pension plans has declined from 8% in 2002 to 7.38% in 2017.
- ❖ Public pension boards deciding to lower their assumed rates of return in recent years include the California Public Employees Retirement System, the Teachers' Retirement System of Illinois, the Michigan Public School Employees Retirement System, the Arizona State Retirement System, and many more.