

Shifting demographic patterns have resulted in a teacher shortage that is threatening the quality of classroom instruction in America's public schools. This article examines how many states are redesigning pension plans to alleviate this growing problem.

Alleviating Teacher Shortages through Pension Plan Redesign

By Laura Palmer Werneck

Over the next 10 years, America will need to hire or retain more than 2 million teachers to meet the demands of rising enrollment and to replace an aging teaching force, according to Recruiting New Teachers (RNT), a national non-profit organization dedicated to improving teacher recruitment and development. Faced with this daunting task, many states are turning to pension reforms to keep retirement-eligible teachers in the classroom while they search for a more permanent solution. This article explores the demographic changes that resulted in the short supply of teachers and outlines some of the ways states are redesigning public pension plans to mitigate the effects of the shortage.

Teacher Supply and Demand

As Exhibit 1 illustrates, the U.S. Census Bureau documented a 20.5 percent increase in K-12 student enrollment in public schools from 1985 to 2001. Demographers believe this increase was caused primarily by the matriculation of the children and grandchildren of the baby boomers—the 76 million Americans born from 1946 to 1964. The leading edge of the baby boomer generation is now reaching prime retirement age, evidenced by the 16 percent increase in the population of persons ages 50-74 from 1985 to 1999.

The simultaneous increase in student enrollment and retirement-

eligible teachers has contributed to the nationwide teacher shortage. Overall, teaching positions are expected to increase by 23 percent for secondary schools and 12 percent for elementary schools.¹ A January 2000 RNT survey revealed a particularly urgent need for special education, science, and math teachers in major urban school districts. Of course, demographics alone do not account for the shortage. Low compensation, poor teaching conditions, and pressure to reduce class sizes also are contributing to the problem.

Tackling Teacher Shortages

To alleviate the shortage, efforts to recruit and retain quality teachers are being made at both the state and district levels. Traditional strategies include loan forgiveness and scholarship programs, signing bonuses that include moving expenses, and salary increases targeted at individuals willing to teach high-demand subjects or in hard-to-staff schools. A relatively new trend is to turn the problem of retiring baby boomers into a temporary solution. By offering incentives through restructured pension plans, many states are hoping to lure retirees back to the classroom and to keep retirement-eligible teachers in the classroom for several more years.

Generally, teachers have three options when they become eligible for retirement: collect pension benefits and stop working, collect pension benefits and draw a salary from a new job, or continue teaching and postpone pension benefits. Faced with these choices, approximately 50 percent of all Washington educators, for example, leave the public school system once they are eligible for retirement. Because of teacher shortages, states are now experimenting with pension plan designs that would offer several new alternatives to retirement-eligible teachers. Specifically, the following three pension alternatives have emerged:

- allow teachers to draw a salary and pension concurrently;
- implement DROP plans; and
- alter the pension benefit formula.

Concurrent Salary and Pension Payments

States have historically barred teachers from simultaneously earning a salary and drawing pension benefits. In light of the teacher shortage, however, an increasing number of states are permitting retirees to return to teaching after a stipulated hiatus and to continue receiving pension benefits in addition to their regular salary. Retirement systems in California, Florida, Louisiana, and New Mexico all have policies that allow teachers who have been retired for at least one year to continue receiving full pension bene-

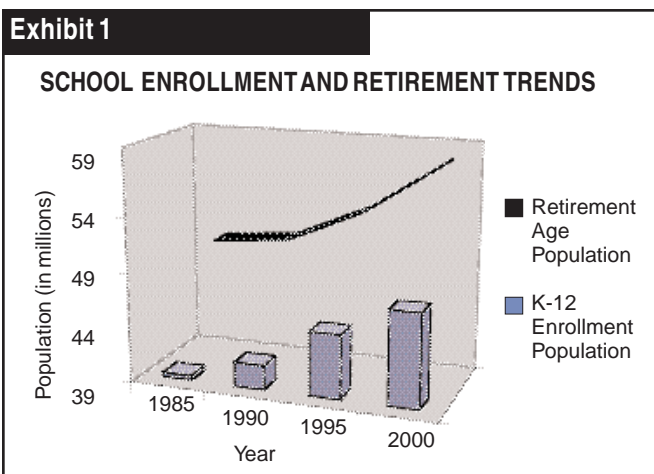


Exhibit 2

PENSION REFORM POLICY BY STATE

STATE(S)	POLICY
California, Florida, Louisiana, New Mexico	After a one-year break, retirees receive full pension benefits and salary. California's policy sunsets in 2008, while an exception to the one-year rule in Florida allows retirees to return to teaching after only one month if they limit their hours to 780 or are hired as substitute or hourly teachers.
Washington	After a 30-day break, retirees receive full pension benefits and salary to a maximum of 1,500 hours per fiscal year.
Ohio and Tennessee	After a two-month break, retirees receive full pension benefits and salary. Tennessee retirees, however, cannot work more than 100 days in a 12-month period.
Vermont	After a qualified break, retirees can choose to either receive full pension benefits and a salary capped at 60 percent or to receive full salary and discontinue pension benefits, which will be recalculated at retirement to reflect additional service.
Alaska	In districts with teaching shortages, retirees can return to teaching at any time. These teachers can choose to either receive full pension benefits and salary with no accrual of additional service or to receive full salary and discontinue pension benefits, which will be recalculated at retirement to reflect additional service.
Maryland	If re-employed in a "reconstituted" school, in a county with a teacher shortage, or in high-demand subject areas, retirees can return to teaching at any time and receive full pension benefits and salary.
Texas	After a one-year break, retirees receive full pension benefits and salary in teacher shortage areas.
Nebraska	Allows teacher rehires to contribute to their retirement while receiving pension payments and a salary.
Alabama, Arizona, Colorado, Idaho, Illinois, St. Louis, Oregon, Tennessee, Vermont, and Washington.	Retirees receive full pension benefits and salary, subject to limitations on working hours.
Alabama, Connecticut, Delaware, Kansas, Michigan, Montana, New York, Oklahoma, Rhode Island, South Carolina, Utah, and Vermont.	Retirees receive full pension benefits and salaries that are subject to limitations on earnings.

Note: This table is not meant to be a comprehensive representation of state pension policies; it is intended to provide the reader with a general sense of how different states are structuring pension plans in response to increasing teacher shortages.

Sources: See Notes.

fits once they return to teaching. Washington recently implemented a policy that allows retirees who separate for 30 days to be re-employed for up to 1,500 hours per fiscal year while continuing to receive pension benefits. In Ohio, teachers can return to work after two months without a disruption in their pension benefits. Exhibit 2 provides a general overview of the different pension policies states have adopted to cope with the teacher shortage.

In Alaska and Maryland, no break in service is required for teachers in school districts that have or are projected to have teacher shortages. Retirees in Alaska have two options upon returning to teaching: they can choose to either receive full pension benefits and salary with no accrual of additional service or to receive full salary and discontinue pension benefits, which will be recalculated at retirement to reflect additional service. In Maryland, where teacher shortages have reached crisis levels in every region of the state, retirees can receive full pension benefits and salary if they are re-employed in a county or a subject area in which there is a teacher

shortage, or by a "reconstituted"² school.³

Unlike most plans, the Nebraska Public Employment Retirement System allows teacher rehires to make additional contributions to their retirement plans while receiving retirement payments and a salary. In this case, the new contributions and additional service cannot be used to increase the original benefit. If the re-employment period is more than five years, the benefit formula will be recalculated based only on the additional service. If the re-employment period is less than five years, the refund is equal to the additional contributions plus interest. Similarly, Florida teachers who return to work after at least a one-year hiatus can earn a second retirement benefit after six years if they are at least 62 years old. This policy is particularly attractive to teachers who move to Florida upon retirement.

Many states are now revising policies that impose limitations on the salaries and/or working hours of retirees who return to teaching. In Vermont, for example, eligible teachers are now compensat-

ed at 60 instead of 50 percent of average teacher compensation, while continuing to receive full pension benefits. As teacher shortages become more acute, other states are likely to liberalize such restrictions.

Deferred Retirement Option Plans (DROP)

To retain retirement-age teachers, several states are employing a different strategy—the Deferred Retirement Option Plan (or Program), otherwise known as DROP. In essence, these programs allow retirement-eligible teachers to build up savings on a tax-deferred basis by diverting regular pension benefits into a separate account where the money accumulates while the teacher continues to work. Louisiana was one of the first states to provide this alternative to teachers. There, members can choose to “freeze” their monthly retirement benefit, which is deposited in a special teacher retirement account while they continue to teach and earn a full salary. Take-home pay typically increases since regular contributions to the primary pension plan cease during DROP participation. After the DROP period ceases, the account begins earning interest at .5 percent less than the retirement system’s actuarially realized return on investments. For example, if the system’s “actuarially realized” return is 8 percent, the DROP account earns 7.5 percent. Interest earnings are deposited each year in DROP accounts to reflect earnings during the previous fiscal year ended June 30.⁴

Members are only eligible to participate in DROP if they are currently employed in the system. Retirees and terminated employees cannot participate in the program. DROP participants select in advance the term of their participation, which can be as long as three years depending on eligibility. The decision to participate is irrevocable; the term of participation cannot be extended and can only be shortened by termination or death. During the DROP period, teachers may not contribute to the retirement plan. Retirement benefits are frozen at the time the teacher elects to participate in DROP. When the DROP period ends, the participant can either continue working and making retirement contributions (while earning additional service credit for the time worked after DROP) or terminate employment and retire. Participants can only withdraw the DROP funds upon retirement. However, participants may choose to receive their benefit in a single lump sum payment or in regular monthly or annual disbursements. DROP participants who have been retired for at least one year may return to work and keep the full retirement benefit while earning a full salary.

Although DROP is an attractive option for many eligible teachers, plan administrators urge members to weigh the option carefully before deciding to participate. To assist potential participants in the decision, the program publishes material explaining the different options and the costs and benefits of participation.

Florida also offers a version of DROP. Florida’s DROP program was created to encourage retirement-age teachers to continue working for an additional five years. As in the case of Louisiana, pension benefits are diverted to a tax-deferred savings account. In Florida, however, these accounts earn interest during participation in the program. At the end of the five-year DROP period, participants have a number of options for receiving their benefits. They can withdraw the DROP funds, roll them over into a tax-deferred annuity, or begin receiving them along with their regular retirement benefit.

Longevity Rewards and Bonuses

Another strategy for retaining retirement-eligible teachers is to build longevity incentives into pension formulas. These formulas are typically a function of compensation, length of service, and a percentage multiplier. As such, it is relatively easy to create incentives for teachers to continue working by adjusting these formulas.

In Missouri, for example, the multiplier is increased from the

normal rate of 2.5 percent to 2.55 percent for teachers with 31 or more years of experience. This higher multiplier is applied to all years of service, not just to those in excess of 31. In contrast, Ohio applies a more generous multiplier only to those years in excess of the 30-year standard. Teachers retiring after 30 years of service would receive 66 percent of their highest average salary based on a multiplier of 2.2 percent. However, the multiplier increases by one-tenth of a percent for each additional year of service, starting with 2.5 percent the 31st year. Teachers working an extra two years would increase their pension benefit from 66 percent of their salary to 71 percent $((30 \times 2.2\%) + 2.5\% + 2.6\%)$. This percentage would increase every year until reaching 100 percent after the 39th year.⁵ Exhibit 3 illustrates how extra years of service can enhance pension benefits under the Ohio system.

Another teacher retention strategy not directly related to pension formulas is the longevity bonus. In California, for example, some teachers are rewarded with a cash bonus for additional years of service. This bonus starts at \$200 per month for 30 years of service and is increased by \$100 every year to a maximum of \$400 per month. The goal of all of these measures, of course, is the same: to keep teachers in the classroom by rewarding extra years of service.

Policy Dilemmas

As the supply of teachers continues to decline, elected officials and school administrators alike must grapple with competing public policy goals to arrive at the best solution to the problem. While many states are devising incentives to retain retirement-age teachers and rehire retirees, others are moving in the opposite direction. New York, for example, continues to offer early retirement incentives to older teachers. By compensating fewer experienced teachers, the state hopes to free up funds that can be used to recruit younger, less expensive teachers. However, many states are finding that early retirement incentives only exacerbate the teacher shortage, at least in the short run.

The targeting of incentives presents a second dilemma. On the one hand, it seems only fair to offer the same benefits to all members of the system. On the other hand, however, it may be considered inefficient to offer a longevity bonus to a teacher who would have worked additional years with or without the incentive. This explains why many states limit retirement incentives to those teachers who have discontinued work for a period of time. This is also consistent with more recent policies that limit retirement enhancements to high-demand teachers.

Although pension reform seems a viable means of alleviating teacher shortages, it still is hotly debated. Some state legislators argue that it is inappropriate to enlist the help of retirement systems to retain and attract teachers. Others contend that public retirement systems were originally devised to do just that—to make governments more competitive in the labor market. Whatever the case, an increasing number of states are turning to their retirement systems in a desperate attempt to meet the demand of ever-increasing public school enrollments.

Exhibit 3

THE EFFECT OF SERVICE CREDITS ON PENSION BENEFITS IN OHIO

Years	Multiplier	Benefit
30	2.2*	66%
31	2.5	69%
32	2.6	71%
33	2.7	74%
34	2.8	77%
35	2.9	89%
36	3.0	92%
37	3.1	95%
38	3.2	98%
39	3.3	100%

*Increases to 2.5 after 35 years

Conclusion

Although these policy dilemmas are not easily resolved, states would be well advised to carefully assess the impact of the policies they choose to implement. To date, there is a paucity of data with which to measure the effects of the strategies outlined in this article. Moreover, most of these policies have not been in place long enough to accurately determine their effectiveness in meeting the challenges posed by teacher shortages. Only by careful study will it be possible to devise satisfactory solutions to a growing problem that—although nationwide in scope—varies from state to state, district to district, and subject to subject. ■■

NOTES

- ¹ Teaching positions are listed in the “Largest Job Growth” category under the Census Bureau’s employment projections.
- ² Reconstituted: To constitute, or establish, again or anew. A school district or state decides to disband a school and replace all staff because the school is deemed to be failing.
- ³ National Education Association, Research, Washington, D.C., was a valuable source in locating state retirement policies.
- ⁴ Teachers’ Retirement System of Louisiana, *The Deferred Retirement Option Plan* (2000).
- ⁵ Ohio caps the retirement benefit at 100 percent of the highest three-year average salary.

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