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Teacher Pension Preferences:

Pilot Study Results

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Teacher Pension Preferences: Pilot Study Results

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Abstract

Teacher pensions are fast becoming a significant issue in education policy. Mounting unfunded pension financial liability, likely larger numbers of retiring teachers, increasing mobility among existing teachers, and unfavorable comparisons with less generous private sector pension plans all contribute to putting pedagogues pensions in the public spotlight. Little is known, however, about the actual pension preferences of current and potential teachers. To this end, this paper provides results from an exploratory survey designed to probe the preferences of current and prospective teachers, the results of which may eventually illuminate the role of pensions in attracting and retaining a higher-quality teaching force.

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Background

In order to understand what pensions teachers prefer (and what plans they logically *should* prefer), one must first understand the current structure of teacher pension plans. In the United States, state government has the constitutional authority for most of education policy and regulation. Thus, the specific features of teacher pension plans vary across the fifty states, and even among school districts within states.

One difference is whether teachers participate in Social Security. When Social Security was initially established, state employees (including teachers) were not included. However, legislative changes in the 1950s permitted individual states to participate if

they chose. Today, teachers in most states do participate in Social Security, but those in 15 states and the District of Columbia do not (Hansen, 2008). To make matters more complicated, selected school districts within nonparticipating states do participate in Social Security.

Another difference among state pension plans is the level at which teachers contribute to the plan. In most states, teachers contribute a percentage of their salaries to their pension. In states without Social Security this percentage is typically higher to compensate for the income that would otherwise be provided by this program. Teacher contributions range from 2% in Indiana to 12% in Missouri with most states requiring contributions approximating 6% (Hansen, 2008). However, some states vary employee contribution according to years of service or plan type, and other states do not require any employee contribution at all. In addition to teacher contributions, states contribute a varying percentage to its employees' pensions. Again, these contribution levels vary widely, from 24.13% in West Virginia to 1% in New Jersey (Hansen, 2008). The ratio of teacher contribution to employer contribution also varies.

Despite variance among states, teacher pension plans today are more similar than they are different. The main explanation for such similarity is that they are almost all defined benefit (DB) plans (as opposed to the defined contribution (DC) plans that are more prevalent in the private sector). Defined benefit plans are those in which employees receive a specified amount of money every year from retirement until death (often with cost of living adjustments). This amount is determined by multiple factors, including number of years of employment as a teacher or other education employee and final salary. Costrell and Podgursky (2008) represent this in equation form as:

Annual Benefit = (years of service) x (r) x (final average salary)

Where r is the "replacement factor," the percentage of her final salary a teacher receives as her pension. Before a teacher can receive any pension at all she must become vested in the pension system by working for a minimum period of time, which again varies by state, up to as long as ten years (Hansen 2008).

In contrast to the defined benefit system, most private sector employees, as well as those employed in post secondary education, participate in defined contribution plans. These are plans where the employer and employee each contribute a specified percentage to a fund that the employee can access upon retirement. Defined contribution plans entail a certain amount of risk for the employee because of the fluctuations of the stock market, but employees are free to choose the types of investments and the level of risk of the fund. Additionally, if an employee leaves her job, the money in the fund travels with her. Finally, the vesting period is typically much shorter than in defined benefit plans, and often immediate.

Why Study Teacher Pensions?

In broad terms, there seem to be two major problems with the current system of defined benefit teacher pensions. First, the current system may not much longer be financially sustainable as large numbers of teachers retire in the coming years. Second, the current pension structure may not be providing the necessary incentives to recruit and maintain a high-quality teaching force in the twenty-first century.

On a basic level, the funding problems with defined benefit pensions are quite easy to understand. Defined benefit plans pay a predetermined amount each year from retirement until death. The current benefit structure in many states encourages teachers

to retire earlier than individuals in other professions, often in their early fifties. Add to this the fact that individuals in the United States are living longer and it is easy to understand how such plans could be in financial peril. A traditional guideline for teacher retirement has been "the rule of eighty," making a teacher eligible for retirement benefits when her age plus years of teaching add up to eighty. This means that a teacher who entered the profession at twenty-two and teaches for twenty-nine years is eligible for retirement at age 51. If she lives to be eighty, she will collect her pension for as long as she taught. While some states have replaced the rule of eighty with the rule of eighty-five or the rule of ninety, many others offer full retirement benefits after 30 years of service at any age, again allowing a teacher who started working right out of college to retire in her early fifties and collect a pension for thirty years or more.

While many teachers may be willing and able to stay in the classroom past the point of retirement eligibility, they have a financial disincentive in many systems to do so. As long as a teacher continues to teach, she does not receive any pension. At some point, this will actually cause her to lose money. Costrell and Podgursky explain in detail how this operates in Ohio (2007b) and in four other states (2007a), and it is likely that many other states follow patterns similar to these. With these systems in place, teachers have strong incentives to leave the profession early, resulting in many additional years of pensions to be funded.

In addition to funding issues, currently operating teacher pension plans exist simply may not be offering proper incentives to attract and maintain a high quality teaching force. As mentioned previously, present arrangements may be offering financial incentive to retire when a teacher may have many productive years left in the classroom.

There is no reason for a dedicated and enthusiastic teacher to be induced to leaved the profession in her fifties, when she may have a great deal of wisdom and experience to share with colleagues. In fact, this practice may contribute to teacher shortages (Hansen, 2008). On the flip side, because defined benefit plans are heavily back-loaded, they may encourage teachers who no longer truly want to teach to remain in the classroom for a few more years in order to receive greater retirement benefits.

Another problem is the issue of mobility. According to the Bureau of Labor Statistics, the average person changes jobs 11 times during his or her working life. While the current defined benefit system may be advantageous for teachers who work in one school district or state for their entire career, it penalizes peers that do not. If a teacher does not stay in a system for a sufficient period to become vested in the retirement system (sometimes as long as ten years), she will receive no retirement benefits at all. Even if she is vested, her benefits if she leaves will be much lower than if she stays.

While encouraging employee retention is one of the key purposes of pensions, it is not always a positive in the teaching profession. Many programs, such as Teach for America, encourage talented and motivated people who might not otherwise consider teaching to do so for a few years. These programs have shown many positive results (Glazerman et. al. 2006, Miller et. al. 1998) and help provide proficient teachers for hard-to-staff urban and rural areas. In Washington D.C., for example, more than 25% of newly hired teachers in 2004 and 2005 came from Teach for America and the D.C. Teaching Fellows (Rotherham & Sullivan, 2006). The current pension system punishes these teachers by offering them no retirement benefits if they do not remain in teaching long enough to become vested.

The current pension system may also contribute to teacher shortages, as those who do not plan to spend thirty years in the teaching profession may be discouraged from teaching at all (Gustman et. al., 1994). Even if a teacher enters the profession intending to teach long term, many career teachers may need to move for personal or family reasons and are then penalized by their pensions. Finally, defined benefit plans may discourage competent individuals from becoming teachers later in life, as they would have to teach for a long time in order to qualify for retirement.

In short, today's teaching force is not homogenous, and many teachers are penalized under a defined benefit plan. Therefore, according to Gustman et. al., "it has been argued that the increasingly popular 401(k) plan, a type of defined contribution plan that, within limits, allows the benefit to vary among covered workers as the firm matches some portion of the worker's chosen contribution, may better meet the needs of today's heterogeneous work force than do more traditional defined benefit pension plans, in which benefits are more similar across all workers (Gustman et. al., 423)."

The Peabody Pension Preference Poll

In order to determine what type of pension today's teachers actually prefer, we created the Peabody Pension Preference Poll. The survey consists of two parts: an informational video and a computer-based questionnaire. The video portion briefly and simply outlines the three main types of pension plans (defined benefit, defined contribution, and cash balance). It is important to note that the survey is not intended to measure teacher knowledge of their current plan or of possible alternatives- this information is presented up front. Instead, the poll or survey attempts to uncover what

type of plan teachers and potential teachers would choose if presented with a range of options.

After the video, survey respondents are migrated to a brief questionnaire. The first questions in the survey is:

> Suppose that in your retirement plan you contribute 10 percent of your pay and your employer also contributes 10 percent. Suppose also that you have a choice among three different options for retirement benefits. Both your own and the district's contribution will remain at 10 percent regardless of the plan you select. Which would you choose?

After responding to this prompt, respondents are probed about why they chose the plan they prefer. They are then directed to a series of background questions covering demographic characteristics, education, and teaching experience. The full survey is available for review at http://sitemason.vanderbilt.edu/site/hH2LxC.

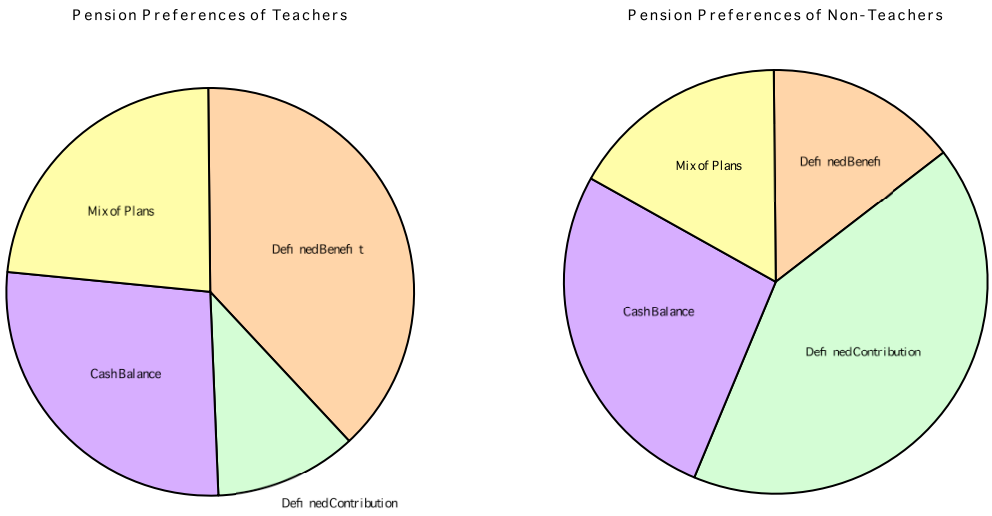
The survey was piloted using a convenience sample of current teachers and administrators from various locations across the United States, as well as students in Vanderbilt University's teacher preparation programs and non-teachers (including Vanderbilt MBA students) to use as a comparison group. A special effort was made to include teachers from alternative certification programs such as Teach for America and Teaching Fellows. Not surprisingly, the response rate for the pilot survey was quite low. While not formally tracked, the response rate is estimated to be well below 50%, resulting in a final sample of 100. Due to the small size of the sample as well as its non-random nature, the findings presented here should be viewed as preliminary and intended to direct further research rather than an indication of the true pension preferences of American teachers.

Preliminary Findings

Teachers vs. Non-Teachers

We begin our analysis by comparing the pension preferences of teachers (including school administrators) to those of non-teachers. Prior to conducting the survey, the intuitive hunch was that teachers may be more risk-averse than individuals in other professions, and therefore more likely to choose a defined benefit pension plan where the risk resides with the employer, not the individual. Pilot poll results suggest this is accurate. The majority of teacher respondents preferred a defined benefit plan while the majority of non-teachers preferred defined contribution (see Figure 1). Additionally, when probed on the reason for their choice, the number most popular response among teachers who chose a defined benefit or a cash balance plan was "I prefer a low-risk option." It is important to note, however, that this survey was conducted in the fall of 2008 when the stock market was at its lowest point since 1931 and many had lost money on their investments. In this economic climate, it is possible that teachers and non-teachers alike might be more risk-averse than they would be otherwise.

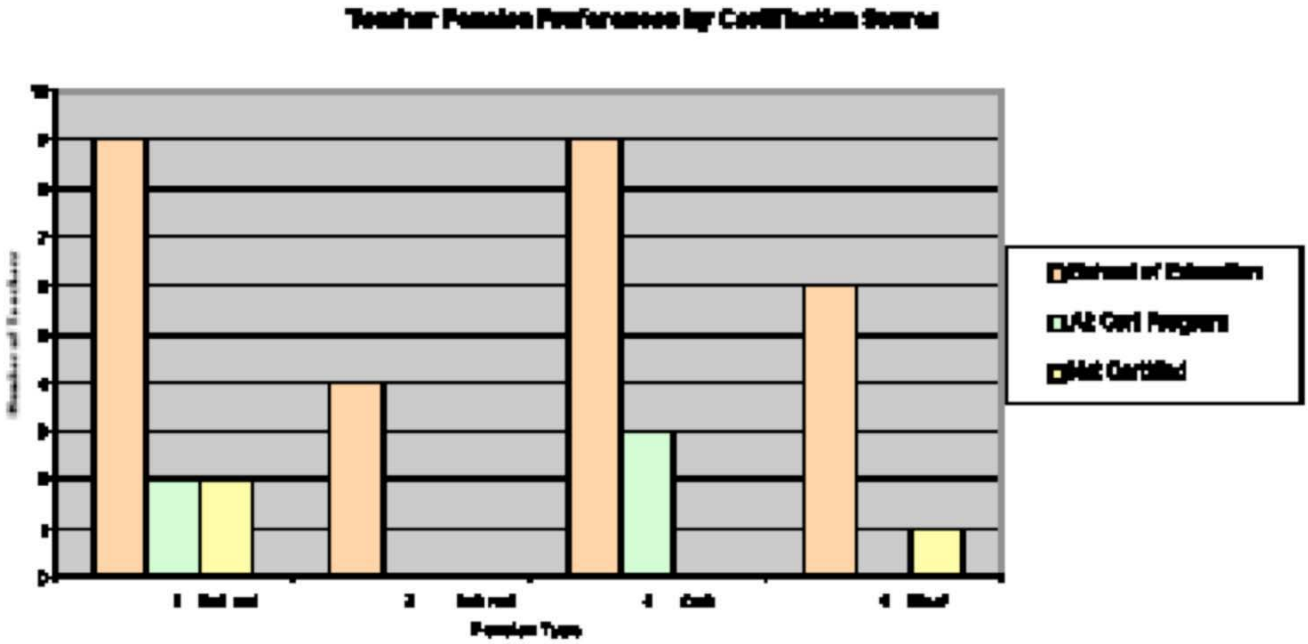
Figure 1- Pension Preferences of Teachers and Non-Teachers



Traditional vs. Alternative Certification

One argument for defined contribution plans is that they are portable, which benefits those teachers who do not plan to spend their entire career in one district or state, as well as those who do not plan to stay in teaching long-term. It was hypothesized that teachers from alternative certification programs such as Teach for America or Teaching Fellows might fall into this group. Therefore, these individuals were specifically targeted when piloting the survey. The poll obtained only a small number of alternatively certified teachers (N=5), their responses were, nevertheless, quite interesting. *None* of the alternatively certified teachers who responded to the survey chose a defined contribution pension plan (see Figure 2). While this may seem counterintuitive, the two alternatively certified teachers who chose defined benefit plans indicated that they did so because they "plan to stay in teaching a long time," which makes their choice a more logical one. With such a small sample, it is unlikely that respondents were representative

of alternatively certified teachers in general- more data must be collected to determine if these patterns persist.

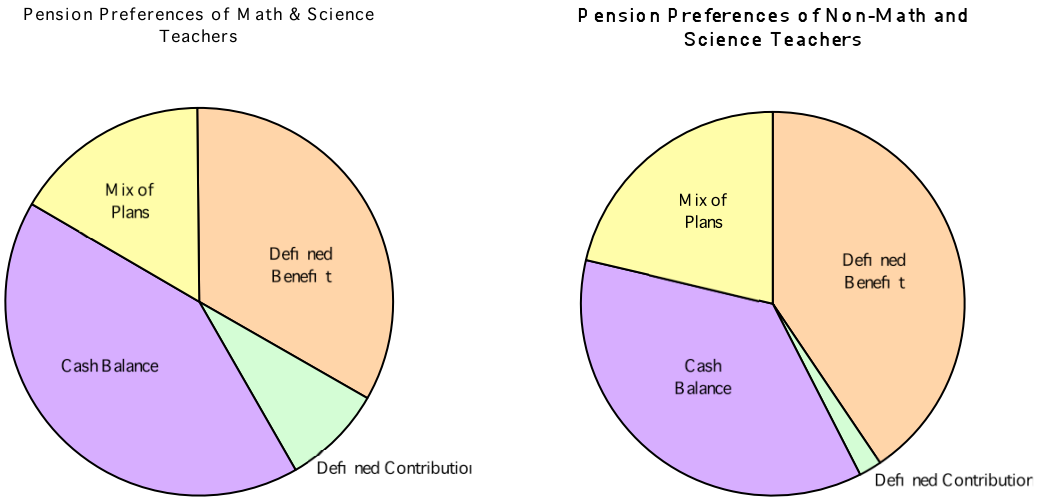


Attracting Math and Science Teachers

Many districts face a shortage of qualified math and science teachers, and attracting these teachers can be particularly difficult. Could a different pension structure help recruit math and science teachers? It was hypothesized that math and science teachers might be more likely to come from, or go back into private sector employment rather than spending their whole career in teaching and therefore be more likely to prefer defined contribution pension plans. In order to test this idea, the survey compared the pension preferences of math and science teachers to those of teachers of other subjects (see Figure 3). Overall, the results were quite similar between the two groups. While

more math and science teachers did prefer defined contribution and cash balance plans, these differences represent only one or two individual teachers in each case. A larger sample is needed to determine if there are, in fact, differences in the pension preferences of math and science teachers.

Figure 3- Pension Preferences of Math & Science Teachers vs. Other Teachers

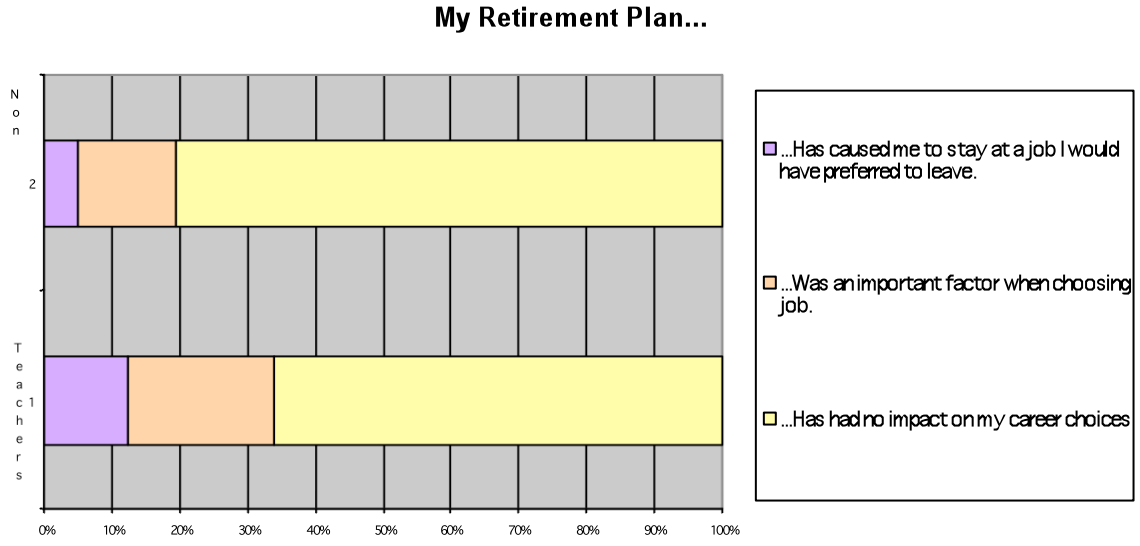


Do Pensions Matter?

Finally, the survey attempted to ascertain whether retirement plans are actually an important factor for teachers when making employment decisions. It could be the case that pensions matter more to teachers than to non-teachers because they may represent a larger percentage of their overall compensation package. The final survey question addressed this issue by asking both teachers and non-teachers, "How has your pension or retirement plan impacted your career choices?" While the majority of respondents in both groups indicated that retirement had not impacted their career decisions, it is interesting to note that more teachers than non-teachers considered their retirement plan

when making these choices (see Figure 4). More teachers than non-teachers reported that their retirement plan had caused them to stay at a job they preferred to leave as well as that retirement was an important factor when choosing a job. While these results are preliminary, they do align with the incentives created by the traditional defined benefit plan in which most teachers participate.

Figure 4- The Impact of Retirement on Career Decisions



Directions for Future Research

Analysis of this pilot study has been severely limited by the small and non-random nature of our sample. The results only serve to hint at the pension preferences of teachers in the United States. In addition to the results reported here, the survey collected information on teacher age and experience, teacher degree level, teacher college selectivity, and other variables that could not be analyzed due to the size of the sample. Therefore, the next priority is to obtain a large, representative sample of teachers. The pilot testing demonstrated that motivating teachers to respond to this survey is not easy.

They have many demands on their time, and we will need to determine which incentives will best encourage participation.

The pilot survey also revealed a need to add and refine demographic questions in order to better understand the data. For example, there is a need to add a question regarding the state in which a respondent lives in order to identify differences between states. This may be particularly interesting because varying states have different pension plans, and a teacher's existing plan will most likely be a key factor in her responses.

Finally, a parallel video may be developed for non-teachers. If a comparison of teachers to non-teachers on a large scale is desirable, it makes sense to produce a video that contains the same information but does not assume the viewer is a teacher. It may also assist if survey questions define "teacher" to identify former teachers and prospective teachers, since the current survey is not able to distinguish these groups but they may provide interesting avenues for analysis in a larger sample.

Though this pilot survey was conducted on quite a small scale, much thought went into its development and much was learned from the initial data. Based data collected so far, there is support for some initial hypotheses (teachers and non-teachers have different pension preferences and retirement plans are more of a consideration for teachers than non-teachers) but not for others (math and science teachers and alternatively certified teachers have different pension preferences than other teachers). Collection of a larger, representative data set will allow us to determine if these patterns persist as well as to understand these and other preference patterns in grater detail.

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