

FY 2023-2024 Employer Contribution Rate

What is the FY 2023-24 Employer Contribution Rate?

On December 16, 2022, the Public School Employees' Retirement System (PSERS) Board of Trustees certified the FY 2023-24 employer contribution rate (ECR) at 34.00%. The ECR is the percentage of payroll that local school employers and the Commonwealth share and pay toward retired and current school employees' benefits.

- The 34.00% ECR represents the first year-to-year decline for school employers and the Commonwealth in more than a decade.
- The FY 2023-24 ECR is 3.6% lower than the current FY 2022-23 rate of 35.26%.
- Total employer contributions are projected to be \$126 million lower (\$5.188 billion) in FY 2023-24 compared to FY 2022-23 (\$5.314 billion).
- School boards set their budgets based on the ECR percentage rate, and a lower ECR will equal real multi-year budgetary savings for their local taxpayers.

Why did the FY 2023-24 Employer Contribution Rate decrease when the Fund did not meet its 7.00% investment rate of return in FY 2021-22?

The ECR decrease, the first since 2008-09, was caused in large part by PSERS' employers strong payroll growth and favorable demographic changes involving mortality and retirement experience, according to the Board's actuarial firm, Buck. Those same factors and sustained actuarial ECR funding contributed to a \$1.5 billion decrease in the System's long-term unfunded actuarial liability, the largest decline since 2006-07.

- The ECR is made up of several actuarial components, not just net investment returns. Other components impact the ECR including, school employer payroll, demographic factors like mortality and projections of retirements and terminations.
- All components, including net investment gains and losses, are amortized over 24 years per Act 120 of 2010.
- Net investment gains and losses are also subject to another actuarial method known as “smoothing.”
 - Under Act 120 of 2010, annual net investment returns are actuarially smoothed into the Fund over a decade or in 1/10th increments per year. The smoothing process means PSERS annual net returns, whether negative (such as the years impacted by the Great Recession) or positive (such as FY 2021's 24.58%) are recognized slowly over time (currently 10 years).
- This smoothing helps to stabilize the budgeting process for school employers and the Commonwealth, which could otherwise vary widely from year to year if recognized immediately. The investment return impact to the ECR is recognized over ten years since investment returns over ten-year periods are historically much less volatile than one-year returns. By comparison, payroll and demographic changes do not have a smoothing factor – and all their year-to-year changes immediately factored into the total pension liability and impacts the 24-year amortization of unfunded liability used to set next year's ECR.

What does this mean for the future?

- The decline in the FY 2023-24 ECR is a one-year decline and ECR rates are expected to rise again slowly. Future increases, however, will start from the lower FY 2023-24 base ECR of 34.00%. This means projected ECR increases are expected to remain lower than previous projections over the next few years.
- The System's funded ratio is expected to reach 80.5% in FY 2031 as more workers who join the System do so under the reduced retirement benefit structures enacted by Act 120 of 2010 and Act 5 of 2017 and full annual funding continues to reduce the unfunded liability.
- Full annual funding since July 1, 2016, favorable long-term investment returns, and a declining cost of current benefits continue to make a positive difference on the financial health of PSERS.

How does smoothing work in practice?

Page 13 of [PSERS June 30, 2022, Valuation](#) (pictured below) shows, in the Recognized Amount – FY21/22 column, the \$151 million investment loss is the net result of adding and subtracting 1/10th of the net investment gains/losses from FY 2012-13 to FY 2021-22.

Actuarial Value of Assets Ten-year asset smoothing method

1. Market value of assets June 30, 2022				\$ 70.664 Bil
2. Determination of deferred gain (loss)				
Fiscal Year	Gain (Loss)	Recognized Amount – FY21/22	Percent Deferred	Deferred Amount
2021/2022	\$ (4.985) Bil	\$ (0.499) Bil	90.00 %	\$ (4.487) Bil
2020/2021	10.116	1.012	80.00	8.093
2019/2020	(3.440)	(0.344)	70.00	(2.408)
2018/2019	(0.600)	(0.060)	60.00	(0.360)
2017/2018	0.551	0.055	50.00	0.275
2016/2017	0.847	0.085	40.00	0.339
2015/2016	(3.794)	(0.379)	30.00	(1.138)
2014/2015	(2.918)	(0.292)	20.00	(0.583)
2013/2014	2.864	0.286	10.00	0.286
2012/2013	<u>(0.153)</u>	<u>(0.015)</u>	0.00	<u>(0.000)</u>
	\$ (1.512) Bil	\$ (0.151) Bil		\$ 0.017 Bil
3. Preliminary actuarial value of assets June 30, 2022: (1) – (2)				\$ 70.647 Bil



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How does smoothing impact other ECR components?

The impact of other ECR components is not smoothed in over ten years. All respective positive or negative changes are calculated and immediately reflected in the total pension liability and fully impact the calculation of the next year's ECR. Page 21 of PSERS June 30, 2022, Valuation (pictured below) shows individual salary increases, retirement changes and mortality changes and shows immediate actuarial gains of \$182 million, \$483 million, and \$86 million, respectively, which brings cumulative net actuarial gains to \$1.1 billion.



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2022 Net Actuarial Gain

1. Investment return loss ¹	\$ 151 Mil
2. Accrued liability experience (gains) and losses ²	
- New entrants and pickups	98
- Individual salary increases	(182)
- Mortality	(86)
- Retirement/disability/terminations	(483)
- Miscellaneous	<u>(213)</u>
- Total	\$ (866) Mil
3. Actual contributions greater than expected	\$ (322) Mil
4. Net actuarial experience gain: (1) + (2) + (3)	\$ (1,037) Mil

1 6.77% actual rate of return on the Actuarial Value of Assets vs. the assumed 7.00% rate of return.

2 Experience (gains) reduce the System's unfunded accrued liability and experience losses increase the System's unfunded accrued liability.



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