ISSUE BRIEF: PENSION FUND

ISSUE: State employee retirement benefits are not sustainable.

Retirement plans help employers hire and keep employees and helps those employees retire with a base level of financial security. While the plans administered by ERS are in relatively good condition compared to many state and municipal plans, the fund must become actuarially sound to be able to pay out to those who have paid in.

The State must modify its current retirement plans and/or increase funding. Each plan design and funding option has features that affect the employer, workforce, employees, and retirees differently. Texas policymakers should base their choices on a clear understanding of past decisions, overall goals, and future implications for all parties involved.

There are several options for bringing the fund to actuarial soundness. Efforts have been made in past legislative sessions to improve the financial health of the ERS Trust Fund. Yet, through the course of the legislative process, the content has changed and the impact has lessened (see following page). While there are varying levels of how to adjust benefits and contributions to restore the fund, the lower-impact/lower-risk options are no longer enough to make a real impact.

The 84th Texas Legislature can address the long-term health of the ERS Trust. Delaying action will cost significantly more and could put the state's financial ratings in jeopardy.

> With 78 cents on hand for every dollar needed to pay benefits, the fund will run out of money in 38 years. Alternative measures claim the deficit is even higher and could affect Texas' bond rating.

RESOLUTION: Take the necessary steps to balance the fund.

In its simplest terms, balancing the fund requires increasing revenues and/or decreasing costs.

To increase revenues, the plan could use higher contributions, investment earnings, dedicated revenue sources, or a lump-sum cash deposit. Revenue generators could include long-term bonds as a one-time or ongoing alternative source.

To decrease costs, the plan could lower the cost of existing benefits, or design a new benefit plan with lower costs, such as a defined contribution or hybrid (combination) plan. Benefit changes could also be designed to adjust behavior so that people are required to work longer before receiving retirement benefits.

Understanding the implications of an unbalanced fund and the options to bring it to financial soundness is imperative to the health of the fund. Not only will Texas state employers lose a valuable tool to secure a qualified workforce that provides critical services to Texas, but the state will pay far more than they do now to provide this benefit.

DEFINED BENEFIT PLAN:

Prefunded by employer and employee rewarding long-term service with a lifetime established monthly benefit.

DEFINED CONTRIBUTION PLAN:

Includes 401(k) and 457 plans, among others, where tax-deferred contributions are made by employer and employee. At retirement, the account balance is distributed until it is gone.

HYBRID PLAN:

Combines elements of both the defined benefit and defined contribution plans. State employees are enrolled in a Defined Benefit plan (mandatory participation) and a Defined Contribution plan (automatic enrollment with opt-out ability).

ERS
EMPLOYEES RETIREMENT SYSTEM OF TEXAS

EVOLUTION OF HB1882 AND SB1459: ACTUARIAL SOUNDNESS NOT ACHIEVED

HOUSE BILL 1882

February 26, 2013
The bill is filed with no benefit changes included.

April 22, 2013
HB1882 is reported from the House Pensions committee as substituted (now called CSHB 1882)
*SEE CHANGES BELOW

May 9, 2013
HB1882 is brought to the House floor on the final day. No vote is taken, and it dies on the House floor.
**SEE AMENDMENTS BELOW

SENATE BILL 1459

March 7, 2013
The bill is filed with no benefit changes included.

April 24, 2013
SB1459 is reported from the Senate State Affairs committee as substituted, with the same retirement and retiree insurance changes as in CSHB 1882.
*SEE CHANGES BELOW

May 13, 2013
SB 1459 is brought to the Senate floor for a second reading.
***SEE AMENDMENTS BELOW
May 21, 2013 the bill is passed.
June 14, 2013 the bill is signed into law

April 22, 2013 — HB1882

***The following retirement benefit changes proposed:**

Retirement

- Sick or annual leave cannot be used to meet retirement eligibility.
- Annual leave can be refunded or used to calculate annuity payments, but not both.
- The final average salary (FAS) calculation is based on the highest 60 months of salary.
- The annuity payment is reduced by 5% per year for each year the member retires before age 62 (age 57 for LECOS), with no cap on the reduction.
- The employee contribution increased to 7%.
- A cost-of-living adjustment (COLA) can be provided under the following conditions:
  - an increase of 3% or $100 per month, whichever is less;
  - for annuitants with 20 years of service or more; and
  - paid only when the fund is actuarially sound, and can remain sound after payment.

The changes would apply to all active employees, except those who, on August 31, 2014:

- are age 50 (45 for LECOS) or older or
- have at least 20 years of service (15 for LECOS).

Insurance

A retiree's insurance premium contribution would be based on years of service, with the State paying:

- 50% of the contribution for retirees with 10 years of service,
- 75% of the contribution for retirees with 15 years,
- and 100% of the contribution for retirees with at least 20 years.

The change would apply to all active employees, except those with 10 years of eligible service on August 31, 2014.

May 9, 2013 — HB1882

****The following amendments are made on the floor:**

- Retirement changes would apply only to employees hired after August 31, 2013.
- The employee contribution is raised to 7.5%.

No vote is taken on the amended bill before midnight, and it dies on the House floor.

May 13, 2013 — SB1459

*****The following amendments are made on the floor:**

Retirement

- Retirement changes apply only to employees hired after August 31, 2013.
- The employee contribution is raised in increments, to reach 7.5% by fiscal year 2017.
- Each state agency employer will make an additional contribution, equal to .5% of its payroll, to the retirement fund.

Insurance

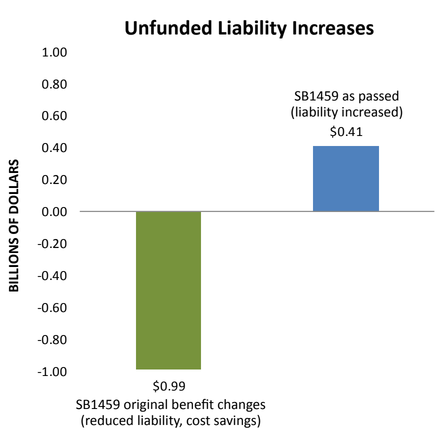
- Retiree premium contributions based on years of service would apply to all active employees, except those with five years of eligible service on August 31, 2014.

The bill passes the Senate.

Final appropriations bill passed with 6.5% employer contribution rate in FY14. This rate will increase to 7.5% with unexpended balances and stay at 7.5% in FY15.

Final bill changes to retirement benefits not enough to bring the fund to actuarial soundness.

PASSED BILL INCREASES LIABILITY, LOWERS NORMAL COST, INCREASES ASC



NORMAL COST LOWERED

FUNDING GAP LOWERED FROM 5.25% TO 4.13% OF PAYROLL