HOUSE RESEARCH ORGANIZATION bill analysis 4/16/97

HB 2644
Telford
(CSHB 2644 by Telford)

SUBJECT: Revising the Teacher Retirement System and increasing benefits

COMMITTEE: Pensions and Investments — committee substitute recommended

VOTE: 5 ayes — Telford, Woolley, Rangel, Sadler, Tillery

0 nays

4 absent — Berlanga, Goolsby, Serna, Williams

WITNESSES: For — Mike Lehr and 44 other representatives of the Texas Retired Teachers Association; Gregg Brock, Association of Texas Public Educators; Lonnie Hollingsworth, Texas Classroom Teachers Association; Nelson Scott, Texas Community College Teachers Association; Johnny Veselka, Texas Association of School Administrators; Jack Kelly, Texas State Teachers Association

Against — None

On — Ronnie Gene Jung, Michael Carter, Patti Featherston and Robert J. Otto, Teacher Retirement System

BACKGROUND: The Teacher Retirement System (TRS) is a defined benefit program that provides retirement benefits based on salary and length of service. The Texas Constitution requires the Legislature to guarantee funding to meet TRS commitments. TRS members become vested, i.e., entitled to receive retirement benefits, after five years of service. Generally, members are allowed to purchase service credit in TRS for up to 10 years of out-of-state teaching service and five years of military service.

Members of TRS are eligible for full standard retirement benefits if they retire at age 65 with five or more years of service; at 60 with 20 or more years of service or at 55 with 30 years of service. The standard retirement benefit is two percent of the highest three-year average salary times the number of years of service. For example, a person retiring with 20 years of service whose salary averaged $30,000 over the last three years would received a standard annual annuity of $12,000. Retirees may choose to receive benefits under five plans ranging from full monthly benefits that stop when the retiree dies to reduced monthly benefits with survivor benefits.

The Legislature created the Texas Public School Retired Employees Group Insurance Program (TRS-Care) in 1985 to provide health insurance for retirees. To be eligible for TRS-Care, retirees must have 10 or more years of service and not be eligible for other public health insurance. The program is funded by a state contribution of 0.5 percent of total salaries of public school employees, a public school employee contribution of 0.25 percent of each employee's salary, payments from retirees, and earnings on investments.

DIGEST:

CSHB 2644 would increase benefits for TRS retirees, beginning with the retirement payments due at the end of September 1997. The benefit increase would range from two percent to 14 percent, depending on the participant's retirement date.

The bill also would require an actuarial audit and actuarial experience study of TRS every five years. The audit would have to include an analysis of the appropriateness of the actuarial assumptions; a review of the assumptions and methodology; verification of demographic data and confirmation of the valuation results, including a determination of actuarial accrued liability, normal cost, expected employee contributions, and effects of any recent legislation.

CSHB 2644 would make a number of changes to TRS-Care. It would allow the program to self-insure, contract with any entity to provide health insurance benefits, and offer long-term care. School districts would only have to pay 75 percent of the costs of participating in TRS-Care, instead of the current requirement of 100 percent, and could offer alternative health care plans in addition to TRS-Care. The state also could contribute a lump-sum amount to TRS-Care in addition to current state contributions of 0.5 percent of total salaries of public school employees.

The bill also would amend TRS eligibility requirements and benefits. Retirement annuities could not be less than $150 per month, and members could retire if their age plus years of service equalled 80. Members who retired with a disability benefit could change their retirement option if they later married, and retirees could have the TRS withhold from their monthly annuity checks dues for a nonprofit association of retired school employees in Texas.

CSHB 2644 would permit salary supplements for driver's education courses to be part of compensation base for retirement benefits; allow membership service credit for time worked in a school funded by the U.S. government regardless of location; and specify that payment for out-of-state service credit be based on all full-time annual pay, plus any other compensation received.

Under the bill, persons employed in a job covered by TRS could not receive retirement benefits. Past membership fees would no longer have to be paid to reinstate service in the system.

CSHB 2644 would take effect September 1, 1997.

SUPPORTERS SAY:

CSHB 2644 represents the third installment of a four-pronged plan by the Legislature to increase retirement payments to keep up with inflation. Most teachers do not receive social security benefits, so the TRS pension is their sole source of income. The bill would increase retirement benefits for all retirees who retired before September 1, 1996, giving them 75 percent of the purchasing power lost to inflation. The benefit increase would raise the amortization period from 5.8 years to 24.1 years, six years below the statutory limit of 31 years, and would increase the unfunded actuarial accrued liability by $1.878 billion. TRS participants who retired prior to 1971 have already caught up with inflation and would receive an additional 5 percent increase, which would have the effect of increasing the unfunded actuarial liability by $1.3 billion.

Allowing TRS members to retire with full benefits once their age and years of service add up to 80 would provide more flexibility for teachers to retire when they wish. For example, currently teachers can retire with 30 years of service at age 50; this bill would allow them to retire at age 49 with 31 years of service. This provision would increase the unfunded actuarial liability by about $460 million and the normal cost of the plan by 0.07 percent, or about $11 million per year under current payroll rates. (Normal cost is the current cost as a percentage of payroll that is necessary to pre-fund pension benefits adequately during the course of an employee's career.)

The bill would allow teachers to apply service for teaching driver's education courses in summer months, which was eliminated last session. Driver's education is a type of curriculum, and teachers should get retirement credit for those courses as for any other course they teach. The local school district would pay the employer portion of driver's education compensation because the salary supplement is above the salary base for state contributions. The Legislative Budget Board estimates the cost to be about $360,000 per year to school districts.

Historically, the Legislature has been the body to decide the level of retirement benefits allowed TRS members, and it would be inappropriate to give the TRS trustees the authority to increase the retirement benefit multiplier from 2 percent to 2.25 percent, as some have suggested. The Legislature is the body politic and should be the body lobbied to increase the multiplier if the money is available, not the TRS trustees.

The audit report required in the bill would ensure that the system continues to be financially sound by providing important information on which to base future decisions. It would require that the audit be performed in conjunction with the actuarial experience study and set out specific parameters to be used in the audit.

The bill also would implement many of the recommendations on TRS-Care made by Value Health Management in a study commissioned by the Legislative Audit Committee last interim. The new provisions would give TRS the flexibility needed to administer TRS-Care and make it more competitive. It would allow school districts to have alternative health plans, including HMOs, that currently are prohibited; reduce the school district cost of participating in TRS-Care from 100 percent to 75 percent; and allow TRS-Care to self-insure. The bill would also allow TRS-Care to contract for health insurance benefits with any health care provider, not just insurance companies.

The bill would allow the Legislature to contribute a lump-sum amount to TRS-Care in addition to current state employer contributions of 0.5 percent of public school payroll. TRS-Care is projected to be depleted in December 2000 under current operating conditions, and this provision would allow the Legislature to properly fund the program. Many retired teachers are not eligible to receive Medicare because school districts did not participate in the social security, and TRS-Care is the only health insurance available.

Some have proposed the idea of providing retiring teachers with an optional deferred retirement option (DROP), which would permit teachers to retire and continue working for five years and receive a lump-sum payment or periodic payments from the accrued retirement benefits paid out for the five years. This may be a laudable idea, but such a plan would be too expensive for Texas and the system cannot afford to provide the option. The plan would provide an incentive for teachers to retire earlier, which would increase the normal costs and actuarial liability to the system. According to the actuaries, a DROP plan would increase the normal costs by about $220 million a year, with an additional unfunded actuarial liability to TRS of $4.4 billion.

Furthermore, DROP plans reduce retirees' annuities because they do not receive credit for the years they worked under the deferred plan. Although they would get a large sum of money initially, ultimately they would receive more money by not not retiring early.

The bill would also make a number of technical changes to improve administration of the retirement program.

OPPONENTS SAY:

The TRS trustees should be given the authority to raise the retirement benefit multiplier from 2 percent to 2.25 percent if the money is available. The trustees have fiduciary responsibility for investing funds and administering the system and giving them this responsibility would be not be departing from prudent policy. The increase could only be made if it would not affect the actuarial soundness of the system.

The state should increase its contribution rate to the TRS, which is now at the constitutional floor of 6 percent, to provide increased retirement benefits to retires. If the state increased its contribution rate sufficiently it could help fund the additional benefits provided by a 2.25 multiplier. The state has been lowering its contribution rate since the mid-1980s, when it was at 8 percent.

Providing retiring teachers with a DROP plan would give teachers the opportunity to have a nice nest-egg when they retire, plus a retirement annuity. A DROP plan would be an additional benefit members could avail themselves of when they retired. DROP plans are popular retirement options and many retirement systems are making DROP plans available to their members.

NOTES: The substitute would allow members to retire with full benefits if their age plus service equalled 80. The substitute also provided for a dues checkoff on retirement checks, and decreased the multiplier used to determine benefits to 2.0 from 2.25.

The companion bill, SB 1122 by Armbrister, has been referred to the Senate State Affairs Committee.