SUBJECT: Revising TRS retirement and benefit plans

COMMITTEE: Pensions and Investments — committee substitute recommended

VOTE: 7 ayes — Eiland, Flynn, Griggs, Krusee, McClendon, Rodriguez, Straus

0 nays

WITNESSES: For — Tim Lee, Tom Rogers, Derly Rivera, Texas Retired Teachers Association Legislative Committee; Anita Stipnieks, New Braunfels Retired Teachers; Zora Mae Hise; Anna Huckabee; Julia Mellenbruch; LaVonne Rogers

Against — Tim Bacon, Texas State Teachers Association; Ann Fickel, Texas Classroom Teachers Association; Gregg Brock, Association of Texas Professional Educators; Ted Melina Raab, Texas Federation of Teachers; Charles Zucker, Texas Faculty Association

On — Sandi Borden, Texas Elementary Principals and Supervisors Association; Ronnie G. Jung , Pattie Featherston, Teacher Retirement System of Texas; Beaman Floyd, Texas Association of School Administrators; Susan Brown, Alejandra A. Martin, Gary Reeves, Texas Association of School Personnel Administrators

BACKGROUND: The Texas Constitution, Art. 16, sec. 67, requires the Legislature to establish the Teacher Retirement System of Texas (TRS) to provide retirement and other benefits for persons employed in the public schools, colleges, and universities supported wholly or partly by the state. Government Code, ch. 821, governs the administration of TRS as well as required benefits for TRS participants.

Under current law, TRS members are eligible for full retirement benefits if their age and years of service total 80, known as the "rule of 80." For example, a member with 25 years of eligible service may retire with full benefits at age 55, while a member with 30 years of eligible service may retire with full benefits at age 50.

DIGEST:

CSHB 2568 would amend numerous provisions of Government Code, ch. 821, as well as other statutes governing TRS administration and benefits. The bill would:

- change eligibility for retirement benefits;
- specify that the TRS board of trustees has exclusive control of all assets held in trust and all operations funded by these assets;
- specify that TRS is exempt from requirements regarding the use of the services of certain other state agencies;
- transfer responsibility for supplemental payments such as the health insurance passthrough to the Texas Education Agency (TEA);
- change requirements related to rehiring retired employees and the purchase of service credits; and
- establish additional reporting and payment requirements for employers that participate in TRS.

Retirement eligibility and benefits. TRS members hired after September 1, 2006, would have to be 65 years old with 5 years of service, or at least 60 years old and qualified for retirement under the rule of 80, to be eligible for full retirement benefits. Employees hired before September 1, 2006, would not be subject to this change.

Members under age 60 eligible to retire under the rule of 80 would have their annuities reduced in 5 percent increments for each year under age 60. Retirement annuities would be based on the member's highest five years of salary, rather than the highest three years, as currently. These provisions would not apply to a member who was at least 50 years old as of August 31, 2005, satisfied a rule of 70 or had 25 years of service credit.

The bill would eliminate provisions in Government Code, sec. 823.006, that allow TRS employees to purchase additional service credits, also known as "air time," for up to five years. A member purchasing retirement credits for out-of-state service would have to pay the actuarial present value, based on rates and tables recommended by TRS's actuary and adopted by the TRS board. A TRS member who previously had earned service in another state before January 1, 2006, could buy that time under current rates at any time in the future. Air time and out-of-state service that a member already had purchased would be counted towards TRS care eligibility.

School districts would be prohibited from offering financial or other incentives to retire early from TRS.

To be eligible for a partial lump-sum payment at retirement, the sum of a member's age and amount of service would have to equal the number 90. These provisions would not apply to a member who was at least 50 years old, satisfied a rule of 70, or had 25 years of service credit as of August 31, 2005.

A retiree would have to elect to participate in the TRS DROP plan no later than December 31, 2005. A member currently participating in the DROP plan could revoke the decision to participate before December 31, 2005.

Control of TRS assets. The bill specifies that the TRS board would have exclusive control over all assets held in trust by the retirement system and all operations funded by trust assets, and that the board would have to administer TRS for the sole and exclusive benefit of the members and participants.

Exemption from use of other state agencies. The bill would exempt TRS from requirements regarding the use of services or functions of the State Office of Risk Management, the Texas Building and Procurement Commission, the Department of Information Resources, and the State Office of Administrative Hearings. TRS could use any service available through the agencies.

The bill would authorize TRS to choose to self-insure or purchase insurance and would specify that insurance contracts had to be awarded through competitive bidding, but the board would not have to select the lowest bid and could consider any relevant criteria, including a bidder's ability to service contracts, past experience, and financial stability.

The bill specifies that the TRS board could determine any salary paid from trust funds, but salaries and other expenditures paid from general revenue could not exceed those paid for similar services for the state.

Transfer of supplemental payments to TEA. The bill would transfer responsibility for supplemental payments, such as the health insurance passthrough, from TRS to TEA, and outline procedures for the distribution and use of these payments.

Employer payments for 90-day waiting period. For new members as of September 1, 2005, employers would have to pay TRS the amount that would have made up the state's share of contributions to TRS during a new employee's 90-day waiting period for retirement benefits.

Rehiring retired employees. School districts that hired a retired TRS member would have to pay both the state and employee's share of retirement contributions to TRS as if that person were an active employee, as well as the difference between the retiree's required payment to TRS-Care, the retiree health insurance program, and the full cost of that retiree's participation in TRS-Care, as determined by TRS. This requirement would not apply to retirees on the payroll in January, 2005.

TRS ActiveCare. The bill would increase the amount active employees contributed to TRS ActiveCare, the state group health insurance program for active employees, from 0.5 percent of the employee's salary to 0.65 percent.

A premium or contribution on a policy, insurance contract, or agreement for TRS ActiveCare would not be subject to state taxes, regulatory fees, or surcharges, including a premium or maintenance tax or fee.

Notice requirements. TEA would have to notify TRS in writing of a charter's school's revocation, denial of renewal, or surrender of a charter, or if the charter school no was longer receiving state funds, not later than the 10th business day after the event. TRS also would have to be notified within 10 days if funding was resumed.

The bill would take effect September 1, 2005, except as otherwise specified.

SUPPORTERS SAY:

CSHB 2568 would help improve the financial soundness of TRS and reduce escalating pressures on TRS that threaten the solvency of the fund. The bill also would improve the system's administrative efficiency and clarify the TRS board's authority to manage and protect pension assets.

Although TRS has experienced solid investment gains in recent years, the fund has about $11 billion less than the amount needed to pay current and future benefits to retirees. Under state law, TRS cannot increase pension payments to retirees unless the fund is deemed "actuarially sound," meaning that it is sufficiently funded to pay current and future benefits over the next 31 years. TRS needs to limit its costs in order to become actuarially sound so that it can provide annuity increases for current and future retirees. The bill would reduce future benefits for all current members by $1.5 billion, which in turn would reduce the state contribution rate that would be needed to make the fund actuarially sound from 8.11 percent to 7.01 percent. The cost of making the fund actuarially sound would be reduced by $250 million in fiscal 2006.

Current retirees would not be affected by changes in retirement eligibility related to the rule of 80. These changes would be phased in over future years and would affect only new hires.

The bill would help reverse a trend toward early retirement that is beginning to have a significant impact on TRS. Over the past decade, the average age of TRS retirees has dropped to from 61.7 years in fiscal 1998 to 59.4 years in fiscal 2004, in part as the result of early retirement incentives such as the purchase of "air time" and retire/rehire. As the retirement age decreases, TRS faces significantly higher health insurance costs for retirees who are not yet eligible for Medicare, as well as the loss of employee contributions to the pension fund.

Retirees should not be able to take advantage of these early retirement options while also expecting the state to shore up the pension fund. Changes should be made to discourage early retirement before the state commits to an increase in its contribution rates.

School districts already should be complying with federal law by paying contributing to Social Security or another retirement program during an employee's first 90 days of employment. The bill simply would ensure that TRS, rather than the federal government or another retirement plan, received this funding.

The bill would clarify the TRS board's authority as a trust to manage and protect pension assets by exercising authority over risk management, contract disputes, purchasing, contracting, administrative appeals, salaries and travel, and data management. These clarifications of board authority should raise awareness that TRS is distinguishable from state agencies. Provisions in the Texas Constitution and various statutes require pension assets to be held for the exclusive benefit of the members and cannot be diverted to other uses. Unlike state agencies, TRS cannot use fund money for expenses that do not benefit members of the pension fund, such as workers compensation costs spread over a large pool of state employees, many of whom are not TRS members.

OPPONENTS SAY:

CSHB 2568 would take benefits away from current and especially future retirees without making the pension fund solvent enough to provide annuity increases for current retirees. The real cause of the TRS solvency problem is that the Legislature has reduced its contribution rate from 8.5 percent to the constitutional minimum of 6 percent of payroll. This bill would reduce the state contribution required to make the fund solvent, but would not commit these state resources. Instead of reducing retirement benefits, the Legislature should address the TRS solvency problem by increasing its share of payments to the pension fund.

Early retirement incentives were adopted to allow school districts to save money in salary costs for experienced teachers, who generally are higher paid. The bill could increase costs for school districts if they were prohibited from encouraging these more expensive employees to retire early.

The Legislature last session effectively slashed the benefits of both active and retired school employees. Retirees' out-of-pocket costs increased 30 percent. Active employees' contributions to retiree health care were doubled. Active employees saw their $1,000 annual health care stipend reduced significantly. The Legislature also shortchanged the TRS pension fund by making no contribution for pension coverage for the first 90 days after a new school employee was hired.

If the purpose of reducing benefits this session is to ensure fund solvency and provide future benefit increases, this should be clearly stated in the bill. Current and future TRS members should be guaranteed annuity increases if the fund is deemed actuarially sound.

The state should pay its share of pension plan payments during a new employee's 90-day waiting period for retirement benefits, rather than requiring school districts to cover this cost. The 90-day waiting period was supposed to be temporary to address the state's 2003 budget shortfall, and continuing it will create another ongoing expense for school districts.

The bill does not address the problems of TRS-Care, the retiree health care plan, which is still underfunded and structurally unsound.

NOTES:

The committee substitute made significant changes to retirement benefits, added various “grandfather” provisions to protect current TRS members, added provisions to transfer responsibility for the administration of supplemental compensation from TRS to TEA, and made other nonsubstantive revisions.

A related bill, SB 1691 by Duncan, is currently pending in the Senate State Affairs committee.

HB 1579 by Kolkhorst, which would impose restrictions on retire-rehire provisions, passed the House on May 3 and is pending in the Senate State Affairs Committee.

HB 3169 by Crownover, which would eliminate the option of purchasing additional service credits, is on today's General State Calendar.

According to the fiscal note, the measures proposed in CSHB 2568 would result in a total gain to the state in fiscal 2006-07 of approximately $451 million in general-revenue related funds, mostly from the lower cost to the state of the contribution that would be required to achieve the 30-year funding period.