HOUSE RESEARCH ORGANIZATION bill analysis | 5/20/2013 | SB 1459 Duncan, et al. (Callegari, et al.)

SUBJECT: ERS contributions and benefits

COMMITTEE: Pensions — favorable, without amendment

VOTE: 6 ayes — Callegari, Alonzo, Branch, Frullo, P. King, Stephenson

0 nays

1 absent — Gutierrez

SENATE VOTE: On final passage, May 13 — 31-0

WITNESSES: *(On House companion bill, HB 1882)*
For — Maura Powers, AFSCME; Lindsay Vogtsberger, Cerner Corporation; (*Registered, but did not testify*: Doug Ervin, Cerner Corporation; Ann Hettinger)

Against — (*Registered, but did not testify*: Deborah Ingersoll, Texas State Troopers Association)

On — Gary Anderson, Texas Public Employees Association; Ann Bishop, ERS; Elizabeth Blount, Retired State Employees Organization; Shea Guinn, Game Warden Peace Officers Association; Ray Hymel, Texas Public Employees Association; Jimmy Jackson, Department of Public Safety Officers Association; Harry Nanos, Texas Alcoholic Beverage Commission Officers Association; Derrick Osobase, Texas State Employees Union; (*Registered, but did not testify*: Mike Ewing, ERS; Christopher Hanson, Pension Review Board)

DIGEST: SB 1459 would make numerous changes to the Employees Retirement System of Texas (ERS), including:

- raising the contribution rates for members and requiring a new contribution from state agencies;
- increasing the minimum retirement and the calculation of final average salary for employees hired after September 1, 2013;
- implementing tiered retirement health insurance premium contributions for employees who were not vested as of August 31,

2014; and

- separating the accounting and actuarial functions of ERS and the Law Enforcement and Custodial Officers Supplemental Retirement Fund (LECOSRF) for fiscal 2014-15.

Contribution rates. SB 1459 would phase in an increase in contribution rates for ERS members from 6.5 percent of the member's annual compensation to 6.6 percent in fiscal 2014, 6.9 percent in fiscal 2015, 7.2 percent in fiscal 2016, and 7.5 percent in fiscal 2017.

Contribution rates for members of LECOSRF would increase an additional 0.5 percent in each fiscal year.

Contribution rates for judges in Judicial Retirement System Plan 2 would increase from 6 percent to 6.6 percent in fiscal 2014, 6.9 percent in fiscal 2015, 7.2 percent in fiscal 2016, and 7.5 percent in fiscal 2017.

After September 1, 2017, member contribution rates would drop to correspond with any decrease in the state's contribution rate from the level set in fiscal 2015.

Beginning September 1, 2103, state agencies would make monthly contributions equal to 0.5 percent of their total payroll.

Pension benefit structure. For employees hired after September 1, 2013, the bill would:

- base their retirement annuity on the 60 highest months of compensation, rather than the 48- or 36-month calculations used for current employees, depending on when they were hired;
- set age 62 as the threshold below which a civilian retiree's annuity would be subject to a 5 percent reduction per year; and
- set age 57 as the threshold below which a law enforcement retiree's annuity would be subject to a 5 percent reduction per year; and
- eliminate unused sick and annual leave from calculations for retirement eligibility, and disallow annual leave for which an employee has been compensated from also being used to calculate pension benefit compensation.

Retiree health care. SB 1459 would implement tiered health insurance premium contributions for some future retirees. Employees with five years of service as of August 31, 2014 would be exempted from these provisions.

Instead of covering 100 percent of the premium costs of employees who retire with 10 years of service, which is required under current law, SB 1459 would require the state to pay 100 percent of premium costs for those with 20 years of service; 75 percent for those with 15 years of service; and 50 percent for those with 10 years of service.

Other provisions. The bill would authorize a 3 percent cost-of-living increase for those who had been retired for 20 years if certain actuarial conditions were met.

It would decrease from 5 percent to 2 percent the annual interest on money in each member's individual account that is used to compute the amount paid when an employee withdraws accumulated funds in lieu of receiving a retirement annuity. The provision would apply only to interest accrued after January 1, 2014.

The bill would make a new employee eligible to participate in the group benefits program no later than the 90th day after the employee's first work date, rather than on the first day of the calendar month that begins after that 90th day.

SB 1459 would decrease from 40 to 30 the minimum number of hours per week an employee had to work in order to be considered a "full-time employee." It would add a definition of eligible dependents to include a child for whom the member served as managing conservator.

Retirees could opt to receive service credit instead of a lump-sum payment for accrued vacation time and could make changes related to divorce decrees.

ERS would be entitled to obtain criminal history record information on candidates for appointment or election to the ERS board or a board advisory committee. The information also would be allowed for consultants, contract employees, independent contractors, interns, and volunteers.

The bill would extend liability protection to advisory committee members appointed by the board.

ERS would be required to conduct an interim study on the feasibility of adding custodial officers employed by the Texas Juvenile Justice Department to LECOSRF.

The bill would take effect September 1, 2013.

SUPPORTERS SAY:

SB 1459 would put ERS back on the path to long-term solvency while allowing state employees to keep the benefits they have earned. All current employees would be grandfathered into the changes in retirement age and pension benefit structure. This would be a unique opportunity to correct course before pension costs become unsustainable. Groups representing active and retired state employees have expressed support for the bill.

The bill would increase employee contributions and provide incentives to the state to maintain a reasonable contribution rate. For too long, the state has been relying on investment gains without ensuring sufficient contributions. It also would create an opportunity for a cost-of-living increase to older retirees if the fund became actuarially sound in the future.

The bill would gradually increase employee contributions from 6.5 percent to 7.5 percent over the next five years so that state workers would not be burdened by a sharp increase. With the addition of the 0.5 percent state agency contribution, the total employer contributions would be 8.0 percent in fiscal 2015. Additionally, the budget conferees have a rider that would raise the fiscal 2014 state contribution from 6.5 percent to 7.5 percent contingent on enactment of SB 1459.

The proposed changes in minimum retirement ages for employees hired after September 1, 2013 are reasonable. Retirees are living longer, and the fund will be unsustainable if the Legislature does not modestly increase the retirement age. Law enforcement officers have physically demanding jobs and legitimately need to retire earlier than average civilian employees, and age 57 would be a good compromise.

Currently, employees who retire with at least 10 years of service receive 100 percent state-paid health insurance premiums. SB 1459 would make adjustments so that employees who spent only part of their careers with the state would share in this cost in retirement. This cost-sharing would be a step to help stabilize the health fund prior to next session, when major changes will be necessary.

The bill initially would increase the ERS and LECOSRF actuarial costs because current employees are exempted from the benefit changes. Over the long term, however, the restructured benefits for new employees and higher contribution rates should begin to decrease the funds' actuarial costs.

The bill would lay the groundwork for establishing a separate pension fund to meet the unique needs of law enforcement officers. Separating the books for these two funds would provide an immediate actuarial benefit to the main ERS fund and a longer-term benefit to LECOSRF in the form of enhanced flexibility and faster growth.

A provision that would direct ERS to analyze and model what would be required actuarially and legally to include juvenile corrections officers in the LECOSRF would help lawmakers decide this issue.

OPPONENTS SAY:

SB 1459 would not adequately address the real problem of chronic state underfunding. For 18 of the past 20 years, the Legislature has failed to contribute at levels that could have made the fund actuarially sound.

The bill would lower the take-home pay of state employees, who already are paid less than their counterparts in the private sector. The increased ERS contributions would hurt the lowest-paid state workers the most.

Some current employees would not be grandfathered into changes in the retirement health care program. The bill would end a longstanding benefit of no-cost health insurance for employees who retire after working at least 10 years. SB 1459 would retain this benefit only for employees with at least 20 years of service, and those with less would pay 50 percent to 75 percent of the premium cost. This change would affect current employees with less than five years of service as of August 31, 2014.

The changes to pension and retiree health care could make it more difficult for the state to recruit employees. State workers generally are paid less than their counterparts in the private sector, but their pension benefits have long been viewed as an important part of their overall compensation.

OTHER OPPONENTS

SB 1459 represents a failed opportunity to make more significant changes that would improve the stability of ERS and LECOSRF. The inclusion of

SAY: a cost-of-living increase for the state's oldest retirees is meaningless because it could not be paid until the fund became actuarially sound.

An earlier version of the bill would have lowered the actuarial costs of ERS by $989 million and represented a significant move toward actuarial soundness, according to the Legislative Budget Board (LBB). The difficulty in gaining a consensus to implement those changes resulted in a watered-down effort.

NOTES: The LBB fiscal note said the bill would increase the ERS unfunded actuarial liability by about $406.1 million and decrease the funded percentage of the system from 79.3 percent to 78.3 percent. The funding period would remain "infinite," meaning that with current contributions to the plan, the unfunded liabilities cannot be eliminated, according to the LBB. However, due to increases in the total contribution rate, the LBB said the actuarial health of the plan would improve under the bill.

For LECOSRF, SB 1459 would increase the unfunded actuarial liability by about $29 million and decrease the funded percentage of the system from 77.2 percent to 75.2 percent. The funding period would remain infinite, LBB said. The actuarial analysis does not address the bill's impact on the Judicial Retirement System Plan 2.