LEGISLATIVE BUDGET BOARD
Austin, Texas

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March 25, 2013

TO: Honorable Bill Callegari, Chair, House Committee on Pensions

FROM: Ursula Parks, Director, Legislative Budget Board

IN RE: **HB3356** by Callegari (Relating to contributions to, benefits from, and the administration of certain public retirement systems.), **As Introduced**

No significant fiscal implication to the State is anticipated.

The bill would amend the Government Code to define a "defined contribution plan" as a plan in which contributions are made to an individual's account, by an individual, and upon retirement the individual receives their contributions plus any investment income.

The bill would also require the governing body of a public retirement system to approve, in writing, the assumptions adopted by an independent actuary prior to audit of the retirement system.

The bill would amend the Government Code to add Subchapter E, which would require public retirement systems to achieve and maintain a funded ratio of 100 percent by fiscal year 2045 and would require any unfunded liability generated after this time to be amortized over a period no greater than 15 years. If contributions to the system fall below normal cost, the bill would require the governing body of public retirement systems to produce a report that includes analysis pertaining to the underfunding. The bill would also require the governing body of public retirement systems with assets above $100 million to periodically conduct an actuarial experience study and a study of the system's assets and liabilities. The bill would also require the governing body of public retirement systems to adopt ethic standards and conflict-of-interest policies. The bill would exempt the Employees Retirement System (ERS), the Teachers Retirement System (TRS), the Texas Municipal Retirement System, and the Judicial Retirement System – Plan II, as well as any volunteer firefighter retirement systems under the Texas Local Fire Fighters Retirement Act from the requirements in Subchapter E.

ERS and TRS anticipate that any costs associated with implementing the bill could be absorbed within existing agency resources. It is assumed that the bill would have little or no impact on the Judicial Retirement System – Plan One because of the few number of judges still participating in the system as of fiscal year 2045.

The bill would require the Texas Emergency Services Retirement System (TESRS) to achieve a 100 percent funded ratio, meaning that assets equal actuarial liabilities, by fiscal year 2045. The fiscal year 2012 actuarial valuation estimates the additional funds required to amortize the unfunded liability in 30 years to be approximately $900,000 per fiscal year. This amount would be in addition to all other contributions, including the anticipated statutory state contribution of one-third of total local contributions. Ultimate responsibility for any unfunded liability, however,

is unclear. It could be addressed by increased state contributions, plan benefit changes, or increased local contributions specifically directed for the unfunded liability instead of benefits; each of which could require additional statutory changes. Under the current law, however, increases to local contributions have a correlated impact to the state's statutory obligation of one-third of all contributions. For example, unless changed, the state's obligation could increase by one-third of the amount of a local contribution increase. If local contributions increase by an additional $900,000 as noted above, the statutory state contribution would increase by an additional $300,000.

The bill would take effect September 1, 2013.

Local Government Impact

The bill would require that local government pension funds achieve a 100 percent funded ratio, meaning that assets equal actuarial liabilities, by 2045. This would mean that affected plans would have a closed funding period to pay off any liabilities.

The requirement could result in plan cost increases if there is unanticipated adverse plan experience. For example, if investment returns fall short of what is estimated, the actual experience of the plan would be negatively impacted. In this case, the sponsoring entity would have to either increase contribution rates or change the benefit design to achieve the 100 percent funding goal. Depending on the severity of the difference in actuarial assumptions and actual plan experience, local governments may have to significantly increase contribution rates.

Even if overall plan experience meets assumptions, plan sponsors could face increased costs if payroll growth assumptions are not met for salary based plans. Contributions to amortize unfunded liabilities are assumed to grow with payroll, or 3 to 3.5 percent for most plans. Thus, over 30 years such contributions are assumed to almost triple. If payroll grew more slowly than assumed, plan sponsors would have to increase contribution rates to keep up under a closed funding period. For example, Houston Municipal has had payroll shrink over the last two years.

According to the Texas Association of Counties, no significant fiscal impact to counties is anticipated. El Paso County indicated no fiscal impact is anticipated.

According to the Texas Municipal Retirement System and the Texas County and District Retirement Systems, no fiscal impact is anticipated.

According to the City of Houston, the city's estimated payroll is $1.3 billion. Beginning in fiscal year (FY) 2017, there would be an additional funding of one percent of the city's overall payroll expense which would be $13.0 million; the city's estimated contribution to pension would be $262.4 million; and the estimated contribution with the additional one percent of payroll would be $275.4 million.

Source Agencies: 304 Comptroller of Public Accounts, 323 Teacher Retirement System, 327 Employees Retirement System

LBB Staff: UP, RB, EP, EMo, PFe, WM, TP, JJO, JW