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To: Chairman and Members
House Committee on Pensions, Investments, & Financial Services
House Committee on Appropriations

From: Texas Public Employees Association (TPEA)
Ann Bishop, Executive Director

Date: August 25, 2020

Subject: Joint Interim Charge 4
ERS Pension Fund—Actuarial Soundness

On behalf of the 11,000 active state employee and retiree members of the Texas Public Employees Association, thank you for this opportunity to submit comments on Joint Interim Charge 4. This charge calls for a review and evaluation of the pension funds administered by the Employees Retirement System (ERS) and Teachers Retirement System, the cost and potential strategies for achieving and maintaining the actuarial soundness of the funds, and the state's investment policies with respect to the funds. TPEA's comments will be limited to the ERS portion of the charge.

Established in 1946, the Texas Public Employees Association is a voluntary, non-profit and nonpartisan organization to advocate for the interests of active state employees and retirees before the Legislature and executive branch of Texas government. In that year TPEA successfully promoted voter approval of the constitutional amendment creating the ERS pension fund. In 1975 TPEA led the effort to establish paid health care coverage through ERS for state employees. For almost 75 years TPEA has worked to provide competitive compensation to attract and retain qualified employees, preserve and improve retirement benefits for those who have dedicated their careers to public service, and protect and enhance health insurance benefits for active state employees and retirees.

Article XVI, § 67, Texas Constitution, directs the Legislature to finance benefits of the ERS Retirement Trust "on sound actuarial principles." But as you know, ERS's actuary, Gabriel Roeder Smith & Company, has estimated that, as of the end of FY 2019, the ERS Trust will run out of funds in 2061. Since 1999, ERS's funded ratio has declined from approximately 105% to about 70% today. The unfunded liability of the trust currently stands at $13.6 billion. Investment returns over the past 20 years have not met current assumptions, leaving the fund to rely more heavily on state and member contributions to make up the difference. Despite increasing contribution rates, however, actual contributions continue to lag actuarial contributions by nearly 4%. Even more troubling is the fact that ERS as a mature pension fund has almost as many retirees and beneficiaries taking money out of the trust as active employees paying in. This means not only that

ERS is emptying the fund almost as quickly as it is replenished, but that the negative cashflow position reduces the amount remaining for long-term investment.

By contrast, in 2019 the Legislature infused TRS with more than $1.1 billion and raised the state contribution rate, restoring the fund to actuarial soundness and reducing the period for paying off TRS's unfunded liability from 90 to 29 years. TPEA applauds the Legislature for its forward-looking intervention on behalf of active and retired Texas teachers.

We now urge you to take similar action on behalf of your own workforce, the approximately 146,000 state employees who deliver the vital basic services necessary to keep the state economy up and running. The Legislature has every reason to be proud of the work your employees are doing every day. Despite the dizzying population growth in the state over the past 25 years, the number of state employees has remained the same since 1993. Rather than a bloated bureaucracy, Texas government is lean and efficient. Your employees work harder and smarter than in any other state in the country. They also show up in times of unprecedented crisis, as we are now experiencing. Despite thousands who have tested positive for the novel coronavirus, state employees continue to perform the jobs necessary to protect public health and safety, process desperately needed unemployment benefits, provide health care for the most vulnerable Texans, and serve the businesses and occupations that rely on them to keep the doors open. These men and women, many of whom are working under extreme duress, have earned your attention to the long-term viability of their hard-earned retirement benefits.

So, what should be done? At the very least, as it did last session with the TRS, the Legislature should make a substantial cash investment in the ERS Retirement Trust to stem the downward spiral and reduce the unfunded liability. Last session, for example, the House committee substitute for S.B. 500, the supplemental appropriations bill, allocated $150 million for ERS. If even this modest amount of funding had survived and been committed on an ongoing basis, it would bring the fund to actuarial soundness in approximately 15 years and, all other things being equal, would fully fund the trust in about 50 years. If the Legislature, however, commits the same amount to ERS in 2021 as it did to TRS in 2019, it would have a far bigger impact and establish ERS on a firmer financial footing going forward.

Second, the Legislature should consider adopting an actuarially determined contribution formula that adjusts contribution rates according to changes, positive or negative, in investment performance or liabilities. Currently, contribution rates can only be determined by the Legislature on a biennial basis. Making such a change would by no means remove the Legislature from control over ERS funding policy, but it would provide a reasonable fail-safe for determining actuarially appropriate funding targets and enable ERS to adapt to market conditions in a predictable way. Moreover, a contribution formula approach would go a long way toward satisfying the constitutional requirement that the trust be financed on an actuarially sound basis without the Legislature having to make expensive lump sum contributions to meet funding crises, such as the one we now face. In the long run, this approach will save taxpayer dollars by increasing the trust's investment revenues, strengthening the state's credit rating, and reducing interest costs on an unfunded liability that is growing at a clip of $750 million per biennium.

Doing nothing is a bad solution for everyone. A stable and financially sound retirement plan is one of the things that makes a career in public service more attractive. Remember that while the average state employee salary is about $48,000, almost two-thirds of state employees make less than that, and 25% make less than $36,000. State employee pay is generally uncompetitive with private sector employment, but that does not mean that we have to accept 20% employee turnover rates and the loss of 41% of new employees who move on within two years of entering service. No business could possibly operate this way for very long, no more can the business of state government. We are appreciative and cognizant of the fact that taxpayers pay the bills, but taxpayers also deserve a state government that is responsive to their needs and delivers services efficiently, promptly, and cost-effectively. If we do nothing to stop this terminal decline in the primary long-term benefit available to your workforce, we will come to a day when we have no workforce at all, at least not one that can do what the people of Texas want and expect it to do.

TPEA and its members stand ready to work with you next session to move ERS down the road toward the constitutional mandate of actuarial soundness. We understand that you will have very tough choices to make in the budget process come spring, but as our state grapples with the economic, social, and personal suffering brought on by the novel coronavirus, we cannot afford to leave behind those who put themselves on the line so that we can all pursue a better life. Thank you for your attention and for your dedicated service to our state.