LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS
54th Legislature, 1st Session, 2019

Bill Number HB360/HAFCS/aSFC **Sponsor** HAFC

Tracking Number .214621.3 **Committee Referrals** HSEIC/HAFC; SFC

Short Title Educational Retirement Changes

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BILL SUMMARY

Synopsis of SFC Amendment

The Senate Finance Committee Amendment to House Appropriations and Finance Committee Substitute for HB360 (HB360/HAFCS/aSFC) would amend the Educational Retirement Act (ERA) to provide for employer contribution of 14.15 percent of annual salary, rather than 14.4 percent of annual salary, eliminate contribution increases in FY21 and FY22, require that a retired employee working 0.25 FTE or less make nonrefundable contributions to the educational retirement fund, and delayed the date for which substitute teachers with a FTE of more than 0.25 FTE would be required to become a member of the Educational Retirement Board (ERB) to July 1, 2020.

Synopsis of Original Bill

The House Appropriations and Finance Committee Substitute for HB360 (HB360/HAFCS) would amend the Educational Retirement Act (ERA) to increase employer contributions to the educational retirement fund; increase the salary level employees would be required to reach before paying a higher contribution rate; increase the age or years of service requirements for new members to be eligible for retirement and reduce retirement benefits for new employees who work for less than 30 years; make changes to the return-to-work program; require most retirees from the Public Employees Retirement Association (PERA) to make contributions to the educational retirement fund if they become employed by an ERA-covered employer; change the salary calculation for determining retirement benefits for employees that receive a salary increase of more than 30 percent, also known as "pension spiking;" and require substitute teachers to become members of the Educational Retirement Board (ERB) if they are employed at least one quarter time (0.25 FTE).

FISCAL IMPACT

HB360/HAFCS/aSFC makes several changes to improve the long-term sustainability of the educational retirement fund. As a result, the bill would increase costs for public school employers covered by the ERB, for public school employees hired on or after July 1, 2019, and for some current school employees.

Employer Contribution Increase. HB360/HAFCS/aSFC would increase employer contributions to the educational retirement fund by 0.25 percentage points in FY20, with total employer contributions at 14.15 percent of salary. Legislative staff estimate the general fund impact of these increases at $6.4 million per year, including contributions for higher education institutions. Staff estimate the general fund impact on public schools to be $4.3 million in FY20. HB360/HAFCS/aSFC would have an impact on federal and other funds received by public schools of $500 thousand in FY19, based on FY18 expenditure data from PED.

The Senate Education Committee Amendment for House Appropriations and Finance Committee Substitute for HB2 (HB2/HAFCS/aSFC) includes a $4.3 million increase to the state equalization guarantee distribution for FY20 to increase employer contributions to ERB by 0.5 percentage points.

HB360/HAFCS/aSFC would also increase employer contributions for members participating in the alternative retirement program, a defined contribution plan available to some higher education employees. Current law requires employers to make a contribution to the educational retirement fund equal to 3 percent of salary for members in an alternative retirement plan. HB360/HAFCS/aSFC would increase that contribution to 3.25 percent in FY20.

Contributions for PERA Retirees and Substitutes. HB360/HAFCS/aSFC would also increase costs for some employees currently working for public schools but not currently required to make contributions to the fund. Under current law, retired PERA members are allowed to work for an ERB-covered employer, not make contributions to the educational retirement fund, and continue to receive their PERA retirement. Current law requires employers to make employer contributions for an employee who is a PERA retiree, but the employee receives no benefits from ERB.

HB360/HAFCS/aSFC would require most PERA retiree employed by an ERB-covered employer make contributions to the educational retirement fund without receiving service credit from ERB, similar to an ERB-member who retires and is re-employed under the return-to-work program. HB360/HAFCS/aSFC includes an exception for police officers hired by an ERB-covered employer prior to July 1, 2019. HB360/HAFCS/aSFC would require some PERA retirees to make contributions to the educational retirement fund without receiving any benefits from the fund. Alternatively, a PERA retiree could suspend his or her PERA benefits and earn service credit through the reciprocity program currently in law.

HB360/HAFCS/aSFC would also require substitute teachers who work at least one quarter time (0.25 FTE) become members of ERB and make contributions to the fund beginning in FY21. Current ERB rules require any substitute teacher "engaged to fill a vacant position" join ERB and make contributions to the fund, but substitute teachers engaged on a "day-to-day basis" are not eligible to join ERB. Typically, public schools pay substitutes a daily rate, ranging from $60 per day to $115 per day in FY17. Assuming a 180-day school year, a substitute teacher could reach 0.25 FTE by serving 45 days per year.

In analysis of HB360 prior to substitution, ERB indicated requiring PERA retirees to contribute to ERB could bring an additional $2.2 million to the educational retirement fund, and including substitute teachers, could bring an additional $3 million, $1.7 million from public school employers and $1.3 million from substitute teachers. Public school employers might need to increase compensation to retain employees impacted by the change. HB360/HAFCS/aSFC could also make it more difficult for school districts and charter schools to hire retired law enforcement officers, who are typically retired PERA members, for school security positions.

Employee Contribution Threshold. Under current law, ERB members who earn $20,000 or less make ERB contributions of 7.9 percent of their annual salary, 2.8 percentage points less than employees earning more than $20,000. This can result in a significant increase in employee contributions to ERB when an employee receives a raise that takes their salary from just below the $20,000 threshold to just above the $20,000 threshold. HB360/HAFCS/aSFC would increase the threshold to $24,000, which could help some employees that receive pay raises in FY20 that would increase their salary from just below $20,000 to just above $20,000. However, this could also make the impact of moving from just below the threshold to just above the threshold more costly because ERB contributions are based on a percentage of the employee's salary. At $20,000, 2.8 percent of salary represents $560, while at $24,000, 2.8 percent of salary is $672. Increasing the threshold would also reduce contributions to the educational retirement fund and could negatively impact the fund. ERB analysis of the substitute bill is not yet available and it is unclear how much this would impact the fund. Staff estimate the reduced contributions at between $600 and $720 per employee with a salary between $20,001 and $24,000. The employer contribution rate to the educational retirement fund do not vary based on the employee's salary.

SUBSTANTIVE ISSUES

Changes to Retirement Benefits. HB360/HAFCS/aSFC would change the retirement benefits calculation for future ERB members. ERB calculates a member's pension as follows:

average salary in five highest years * pension multiplier * years of service

Those hired on or after July 1, 2019, would be subject to a tiered retirement multiplier, rather than the flat 2.35 percent multiplier currently used to calculate a retiree's pension benefit. The pension multiplier would vary based on how long the person was employed and paying into the system. The first 10 years of service would be calculated at 1.35 percent, service between 10 and 20 years would be calculated at 2.35 percent, service between 20 and 30 years would be calculated at 3.35 percent and service over 40 years would be calculated at 2.4 percent. This would result in a retirement multiplier of 2.35 percent for any member with exactly 30 years of service credit. Members with less service would have a lower multiplier, while those with more than 30 years would have a higher multiplier. HB360/HAFCS/aSFC could have the effect of incentivizing more years of service from ERB employees and provide additional payouts for those who pay into the system for longer than 30 years. These provisions of HB360/HAFCS/aSFC would not apply to current ERB members.

HB360/HAFCS/aSFC would also change the minimum age for "normal" retirement from ERB. Under current law, employees who started on or after July 1, 2013 are eligible to retire after 30 years of service, but members under age 55 have their pension benefit reduced. HB360/HAFCS/aSFC would require members with 30 years of service who are under age 58 to have their pension benefit reduced. According to ERB, members are living longer in retirement. In 1962, men lived an average of 13.2 years in retirement and women lived an average of 17.4 years. By 2013, men lived an average of 20.2 years in retirement and women lived an average of 23.1 years. The change in retirement age included in HB360/HAFCS/aSFC would only impact those first employed on or after July 1, 2019, many of whom will not retire until 2050 or later.

Return-to-Work Program. Since 2003, ERB has allowed retired members to return to work and continue to receive retirement benefits under certain conditions. Under current law, an employee may return to work under one of two programs: the return-to-work program in state law, or the return-to-work exception in ERB's administrative rules. HB360/HAFCS/aSFC would reduce the length of time an employee must wait before qualifying for the return-to-work program to six months from the current 12 months. ERB's retirees must wait before returning to work due to regulations from the Internal Revenue Service. Under the return-to-work exception, an employer may return to work immediately but may not work more than 0.25 FTE or earn more than $15 thousand. HB360/HAFCS/aSFC would eliminate the return-to-work exception and require all employees wishing to return to work to qualify for the return-to-work program by waiting six months. Under ERB rules, those employed less than 0.25 FTE are not eligible to join ERB, so retirees working less than 0.25 FTE would not need to qualify for the return-to-work program.

Under the return-to-work program, both employers and employees are required to make contributions to the educational retirement fund, but the employee does not accrue additional service credit for their continued employment. Alternatively, a member can suspend his or her retirement benefit and return to work to receive additional service credit.

HB360/HAFCS/aSFC would not extend the return-to-work program beyond its current sunset date of January 1, 2022. Should the return-to-work program expire in FY21, retired employees working for school districts and charter schools may be required to suspend their pension benefits to remain employed.

Anti-Spiking Provisions. HB360/HAFCS/aSFC would limit the extent to which salary increases count towards pension calculations for employees making more than $60 thousand. These provisions of the bill aim to prevent "pension spiking" – the deliberate manipulation of salary for the purpose of increasing a member's retirement benefit. Under HB360/HAFCS/aSFC, salary increases of greater than 30 percent would not be used in the calculation of average salary.

OTHER SIGNIFICANT ISSUES

According to ERB financial reports, as of June 30, 2018, the educational retirement fund held $12.996 billion in assets, equal to 63.5 percent of estimated liabilities of $20.458 billion and ERB's actuaries estimate it will take 70 years to pay off the unfunded liability, based on current actuarial assumptions. Combined employer and employee contributions total 24.6 percent of salary for members earning more than $20 thousand per year, but ERB's actuaries estimate the total cost of providing benefits earned in the current year is 13.68 percent. The remainder is directed to paying down the plan's unfunded liability. ERB's current board policy calls for the unfunded liability to be paid down in 24 years, but ERB's actuaries estimate this would require a 20.78 percent employer contribution, based on current policies.

RELATED BILLS

HB360, as introduced, was identical to SB14.

The requirement that PERA retirees contribute to the educational retirement fund may conflict with the intent of SB148, which attempts to reduce barriers to employing retired law enforcement officers in school security positions by allowing law enforcement retired from PERA to receive annual cost of living adjustments.

SOURCES OF INFORMATION

- LESC Files
- Educational Retirement Board (ERB)

JWS/mc