ERS
EMPLOYEES RETIREMENT SYSTEM OF TEXAS

Retirement Benefits Study Findings

September 2012

The 82nd Texas Legislature directed ERS to study and report on the State of Texas retirement program. The report is the result of a year-long research process designed to be transparent and inclusive to all stakeholders with an interest in the future of the state retirement plans.

The report analyzes 14 options to increase revenue, modify benefits, or establish an alternative plan. It also compares the state's pension benefits to other large defined benefit plans.
The findings are:

Without action, the unfunded liability will continue to increase and make today's situation unmanageable.

- The ERS pension plans have enough assets to pay benefits for the next 70 years, but they are not operating on an actuarially sound basis.
- Investment returns alone cannot fill the funding gap.
- State contributions of 10% and employee contributions of 6.5%, could pay down the unfunded liability within a measurable period of 55 years.

A good balance can make the current plan sound.

- The report analyzes options to increase plan revenue, lower expenses through plan design modifications, and create alternative plan designs. Balancing options could move the plan in the right direction while decreasing the likelihood of unintended consequences.

Establishing an alternative retirement plan could fulfill specific workforce needs; however, it does not erase the unfunded liabilities in the existing Defined Benefit (DB) plan and could cost more.

- An alternative retirement plan—such as a defined contribution (DC) plan (like a 401(K), cash balance or hybrid plan—could be valuable to employees who do not plan a career with the state, or those who like controlling their own investments.
- The value of a DC plan depends on how well the individually controlled investments perform. Studies show that individually managed accounts have higher fees and lower overall performance of any type of retirement plan
- Implementing an alternative plan structure does not automatically lower costs or erase the existing unfunded liability. In fact, all the alternative plan structures modeled in the report show increased costs in order to achieve a sound new benefit structure.

Prefunded pooled investing increases value to the members and the state.

- Employee contributions and investment earnings do most of the work, producing 82% of the benefits.
- The state contribution is lower and member contribution higher than the median public sector pension plan.
- Pooled trust fund dollars are invested in Texas companies through stock, bond and real estate portfolios.
- Private equity investments provide capital to local companies.
- About 30% of the trust's equity investments are in companies with Texas headquarters or with 200 or more Texas workers.

Retirement benefits are critical to attracting and retaining qualified employees.

- The state agency workforce is already lean, having grown by only 2% over the past decade, even as Texas' population grew 20%—10 times faster.
- Turnover rates in Texas agencies increased significantly in FY2011, with employees citing new jobs with better pay and benefits as their primary reason for leaving. Some positions and locations face 40% turnover rates.
- Turnover costs money -- agencies lose training in terms of dollars and time when valuable knowledge walks out the door. For example, the state invests about $30,000 over seven months to train each Department of Public Safety trooper. That investment is lost if the troopers go to work for county and municipal employers.
- State employers say that lowering benefits will increase these costly turnover rates.

It is difficult to make direct comparisons between private and public sectors workers.

- Manufacturing and sales jobs, a large part of private industry work, typically do not exist in state government. A 2010 State Auditor's Office market analysis showed that almost 40% of state jobs do not have a close equivalent in the rest of the job market.
- According to SAO, almost one-fifth of general state employees in positions that can be compared to private sector positions are paid salaries more than 20% behind market rates.
- Private employer compensation packages often include rewards not available to public employees, such as stock options, expense accounts, and annual bonuses.

Changes to other parts of the employee compensation package can impact the retirement plan.

- Changes to the insurance benefits that encourage employees to work longer can help the retirement plans. For example, tying insurance coverage to tenure will encourage employees to work longer. On the other hand, changing insurance eligibility could cause a "rush to retirement" which could cost the pension plan.
- Any plan modification or structural change carries legal risks that increase as more members are included.
- Benefits for vested members have a number of protections and changing them could have legal and tax consequences.

For a copy of the full report, please visit our website
www.ers.state.tx.us