

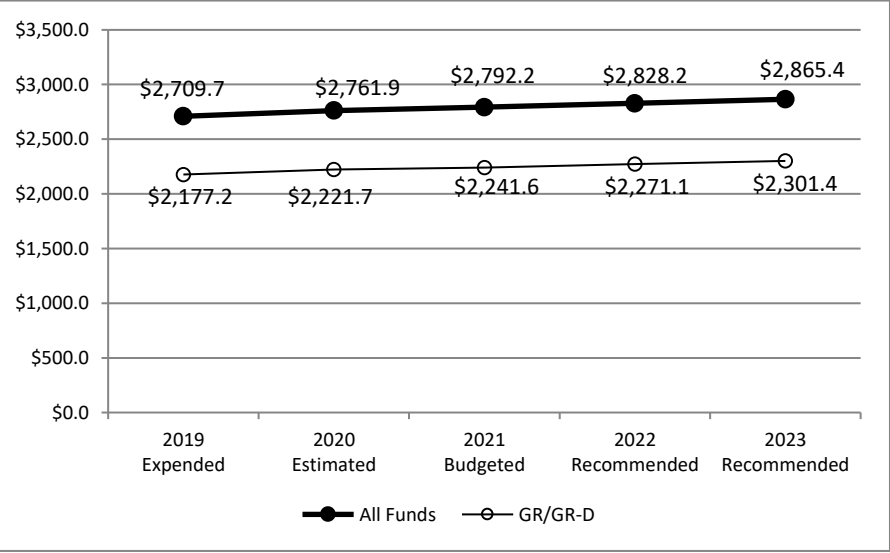
Employees Retirement System **Summary of Budget Recommendations - House**

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Porter Wilson, Executive Director
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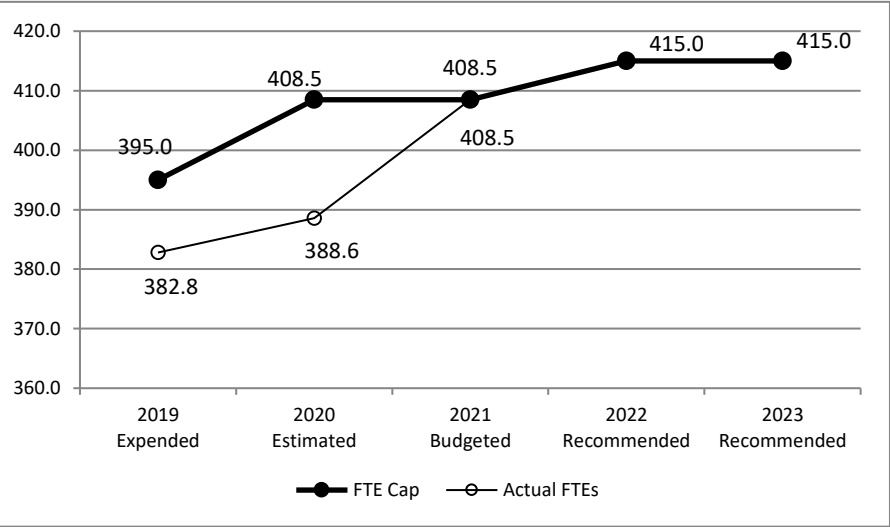
Method of Financing	2020-21 Base	2022-23 Recommended	Biennial Change (\$)	Biennial Change (%)
General Revenue Funds	\$4,165,385,465	\$4,264,372,817	\$98,987,352	2.4%
GR Dedicated Funds	\$298,002,344	\$308,076,987	\$10,074,643	3.4%
Total GR-Related Funds	\$4,463,387,809	\$4,572,449,804	\$109,061,995	2.4%
Federal Funds	\$462,188,347	\$471,354,053	\$9,165,706	2.0%
Other	\$628,600,919	\$649,722,934	\$21,122,015	3.4%
All Funds	\$5,554,177,075	\$5,693,526,791	\$139,349,716	2.5%

	FY 2021 Budgeted	FY 2023 Recommended	Biennial Change	Percent Change
FTEs	408.5	415.0	6.5	1.6%

Historical Funding Levels (Millions)



Historical Full-Time-Equivalent Employees (FTEs)



The bill pattern for this agency (2022-23 Recommended) represents an estimated 10.2% of the agency's estimated total available funds for the 2022-23 biennium.

Employees Retirement System
Summary of Funding Changes and Recommendations - House

Section 2

Funding Changes and Recommendations for the 2022-23 Biennium compared to the 2020-21 Base Spending Level (in millions)	General Revenue	GR-Dedicated	Federal Funds	Other Funds	All Funds	Strategy in Appendix A
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SIGNIFICANT Funding Changes and Recommendations (each issue is explained in Section 3 and additional details are provided in Appendix A):

A)	Increase for ERS Retirement Program contributions due to payroll growth.	\$8.8	\$1.1	\$0.7	\$2.1	\$12.7	A.1.1
B)	Increase for Group Benefits Program contributions due to growth among retired members.	\$91.0	\$9.6	\$8.5	\$19.0	\$128.1	B.1.1

OTHER Funding Changes and Recommendations (these issues are not addressed in Section 3 but details are provided in Appendix A):

C)	Decrease in JRS 1 retirement program due to a decrease in membership in this plan provided for certain state judicial officers who held office before September 1, 1985.	(\$0.5)	\$0.0	\$0.0	\$0.0	(\$0.5)	A.1.4
D)	Decrease in Public Safety Death Benefits due to anticipated reduced claims.	(\$0.5)	(\$0.6)	\$0.0	\$0.0	(\$1.1)	A.1.5
E)	Decrease for Retiree Death Benefits due to anticipated reduced claims.	(\$1.3)	\$0.0	\$0.0	\$0.0	(\$1.3)	A.1.6
F)	Increase for Probation Health Insurance contributions due to anticipated growth among retired members.	\$1.2	\$0.0	\$0.0	\$0.0	\$1.2	B.1.2

TOTAL SIGNIFICANT & OTHER Funding Changes and Recommendations (in millions)	\$98.7	\$10.1	\$9.2	\$21.1	\$139.1	As Listed
<i>SIGNIFICANT & OTHER Funding Increases</i>	\$101.0	\$10.7	\$9.2	\$21.1	\$142.0	As Listed
<i>SIGNIFICANT & OTHER Funding Decreases</i>	(\$2.3)	(\$0.6)	\$0.0	\$0.0	(\$2.9)	As Listed

NOTE: Totals may not sum due to rounding.

Employees Retirement System
Selected Fiscal and Policy Issues - House

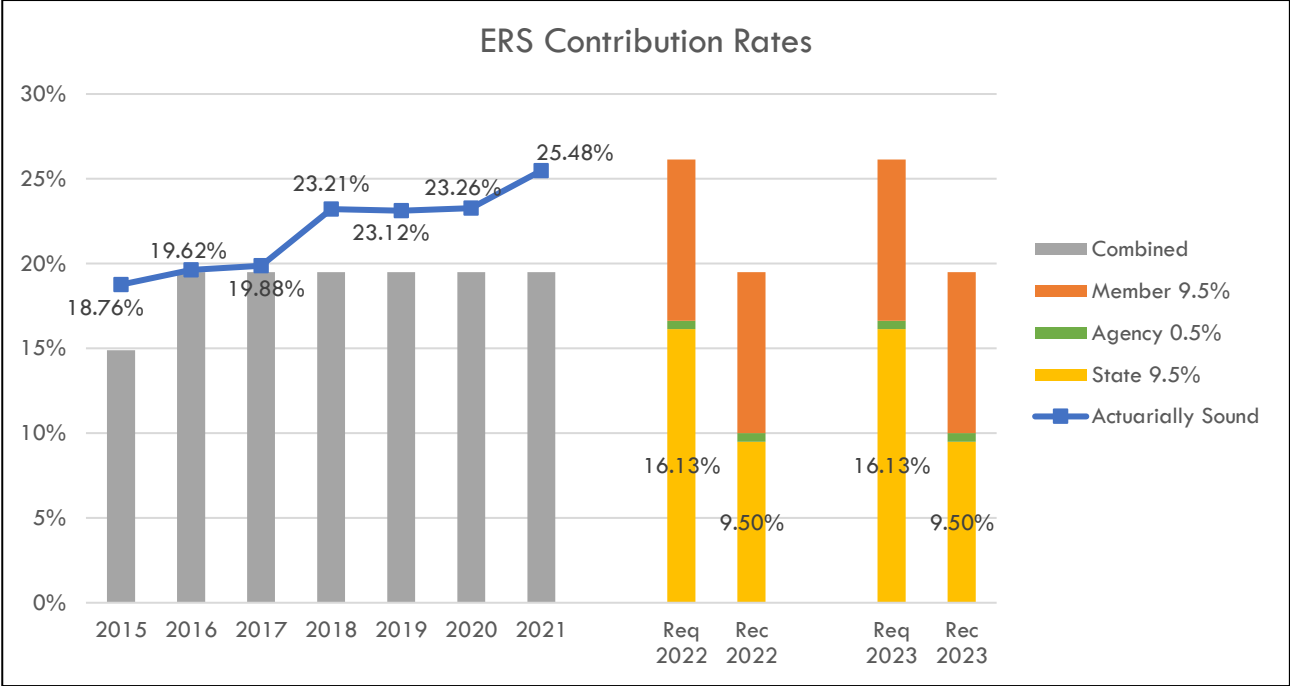
1. **Employees Retirement System.** Recommendations for the 2022-23 biennium total \$1.4 billion in All Funds (\$1.1 billion in General Revenue-Related Funds) for the system that provides a defined retirement benefit to state employees and elected officials. This is an All Funds increase of \$12.7 million (0.9 percent) and a General Revenue-Related increase of \$9.9 million (0.9 percent).

Recommendations assume 0.5 percent payroll growth in fiscal years 2021, 2022 and 2023. In addition, they assume FTE increases at the Department of Motor Vehicles, General Land Office, Texas Division of Emergency Management, and the Water Development Board. They also assume FTE decline at the Department of Criminal Justice. Recommendations maintain the current contribution structure that has been in place since fiscal year 2016, as depicted on the right.

According to the 2020 Actuarial Valuation and the 2020 Experience Study (which examines economic and demographic assumptions), the current total contribution rate, 19.5 percent, is 6.63 percent lower than the contribution required for the fund to be actuarially sound, 26.13 percent. Statute defines actuarial soundness as having contributions that are sufficient to amortize the unfunded accrued liability during no more than 31 years. The funding period at the end of fiscal year 2020 is infinite, meaning the liability is expected to grow indefinitely. Furthermore, the assets are anticipated to be depleted in fiscal year 2061. The valuation also assessed the unfunded actuarial accrued liability at \$14.7 billion. The plan's funded ratio, assets divided by liabilities, was 66.0 percent.

The significant differences in unfunded liability and funded ratio are due primarily to changes in actuarial assumptions. In particular, the Board of Trustees in August 2017 decreased the investment return assumption from 8.0 percent to 7.5 percent, and in May 2020 the board decreased the rate to 7.0 percent. The agency's first exceptional item request is for \$952.5 million All Funds and \$688.6 million General Revenue-Related Funds to increase the state's contribution rate from 9.5 percent to 16.13 percent, to reach the combined Actuarially Sound Contribution (ASC) rate of 26.13 percent anticipated for fiscal years 2022 and 2023. The ASC rate assumes a payroll growth of 2.7 percent for those years.

2. **Constitutional Maximum Contribution.** The current state and agency contribution rates of 9.5 and 0.5 percent respectively together equal 10.0 percent, which is the maximum contribution rate according to the Texas Constitution (Article XVI, Sec. 67 (b)(3)). The provision reads, "the amount contributed by the state may not be less than six percent nor more than 10 percent of the aggregate compensation paid to individuals participating in the system." The Constitution also provides that if



the governor determines the situation an emergency, “the legislature may appropriate such additional sums as are actuarially determined to be required to fund benefits authorized by law.”

In February 2015, the Attorney General offered an informal letter of legal advice which guided that should the state appropriate funds that exceed the ten percent limitation without the governor having declared an emergency, it would “effectively rewrite... the constitutional provision,” concluding that state appropriations may not exceed the ten percent limitation unless the governor has declared an emergency. The agency’s first exceptional item, to increase the state’s contribution rate from 9.5% to 16.13 percent for the Employee Retirement System, appears to violate this constitutional provision.

3. **Law Enforcement and Custodial Officers Supplemental (LECOS) Retirement Fund.** Recommendations for the 2022-23 biennium total \$17.4 million in All Funds and \$17.3 million in General Revenue-Related Funds, which continue the base amount and contribution structure from the 2020-21 biennium. LECOS provides a supplemental retirement benefit to law enforcement and custodial officers in addition to their benefit as state employees through the ERS plan.

The current state contribution rate and member contribution rate are each 0.5 percent. In addition to state and member contributions, the fund also receives court fees. In fiscal year 2020, ERS received \$13.5 million in court fees for this fund. These fees are a reduction from previous years, presumably due to a decrease in court filings as a result of the COVID-19 pandemic. Court filings are expected to resume to higher levels during the 2022-23 biennium.

The 2020 Actuarial Valuation found that the LECOS funding period is infinite with an expected depletion date of 2041. The unfunded liability in 2020 is \$642 million, and the funded ratio is 60.1 percent. The 2020 Actuarial Valuation and 2020 Experience Study indicated that the actuarially sound contribution rate for fiscal year 2022 is 3.57 percent, which is in addition to court fees projected to be \$17 million annually. The agency is requesting \$89.4 million in All Funds and \$88.8 million in General Revenue-Related Funds to increase the state contribution from 0.5 percent to 3.07 percent in order to achieve actuarial soundness.

4. **Judicial Retirement System Plan Two (JRSII).** Recommendations for the 2022-23 biennium total \$28.5 million in All Funds and \$20.1 million in General Revenue Funds to continue the contribution structure from the 2020-21 biennium. Judicial Fund No. 0573 comprises the remainder of the appropriation. JRSII provides a defined retirement benefit to state judicial officers who first took office on or after September 1, 1985.

The 2020 Actuarial Valuation found that the period is infinite with an expected depletion date of 2059. The unfunded liability is \$104 million, and the funded ratio is 82.3 percent. The 2020 Actuarial Valuation and 2020 Experience Study indicated that the actuarially sound contribution rate for fiscal year 2022 is 33.94 percent.

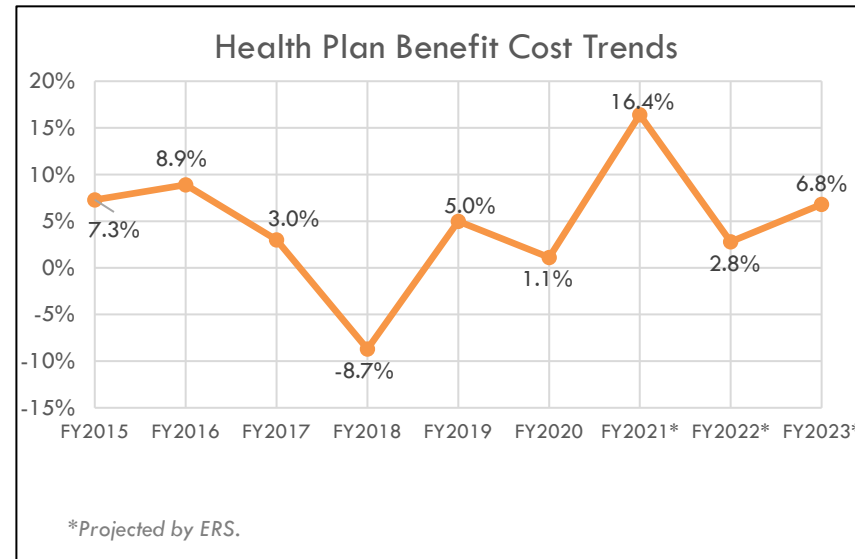
While the member contribution rate is 9.5 percent, the effective member contribution rate is 9.42% as some active members elect to cease contributions and cease to accrue additional benefits. In order to achieve soundness, the agency assumes that the current effective contribution rate of 9.42 percent remain the same, and the agency requests that the state increase its contribution from the current 15.663 percent to 24.52 percent. This exceptional item request is for \$16.1 million in All Funds and \$11.4 million in General Revenue Funds.

5. **Group Benefits Program and Contingency Reserve Fund Balance.** Recommendations include \$4.0 billion (\$3.2 billion in General Revenue-Related Funds) to provide state employees and retirees with health and life insurance. This is an increase over the previous biennium of \$128.1 million All Funds (3.3 percent) and \$100.5 million General Revenue-Related Funds (3.2 percent). Recommendations assume that:
 - the state will continue to contribute the full cost of member-only group insurance and fifty percent of family coverage;
 - full-time-equivalent employment levels will grow at the Department of Motor Vehicles, General Land Office, Texas Division of Emergency Management, and the Water Development Board and will decrease at the Department of Criminal Justice;
 - retiree membership will grow 3.9 percent in fiscal years 2021, 2022 and 2023; and
 - the state’s per-member contribution to insurance will not increase in fiscal years 2021, 2022 and 2023.

Recommendations align with ERS's Legislative Appropriations Request which indicates that no additional per-member state contributions above the base level would be necessary. The ERS request did not include member growth.

HealthSelect of Texas® combined medical and pharmacy plan costs increased 6.2% through the first half of Plan Year 2020. Beginning in March 2020, medical utilization dropped sharply with the impact of the COVID-19 pandemic, while pharmacy trend increased significantly in the same month as many members stock piled medications. According to the agency, the projected fiscal year 2021 cost trend is high due to the expectation of delayed services from the prior year occurring in fiscal year 2021. The agency expects fiscal year 2022 will not have the issue of delayed services so the cost trend is low, while fiscal year 2023 costs are expected to resume to their normal trend.

The Contingency Reserve Fund receives all revenues for the Group Benefits Program (GBP) and makes expenditures to cover claims costs. Chapter 1551.211(a) of the Texas Insurance Code requires ERS to maintain funds in the reserve to cover expenditures for an average 60 day period. According to the agency, this fund totaled \$2.7 billion at the end of FY 2020 and is expected to have ending balances of \$2.9 billion at the end of FY 2021; \$3.0 billion at the end of FY 2022; and \$3.0 billion at the end of FY 2023. The report projects the fund would be fully depleted during FY 2027, mostly due to the projected increases in health care expenditures.



6. **Article IX, Section 10.06: Cross Agency Coordination on Healthcare Strategies and Measures.** The 2020-21 General Appropriations Act (GAA), House Bill (H.B.) 1, 86th Legislature, Regular Session, 2019 (Article IX, Health Related Provisions, Section 10.06) requires state agencies that pay for the health care of Texans to coordinate data to identify outliers and improvements for efficiency and quality that can be implemented within each healthcare system. The first report was submitted September 1, 2020. Highlights of the report included the following:

- Data from the five agencies involved (DSHS, ERS, HHSC, TDCJ, TRS) has been aggregated into comparable models, allowing agencies to identify interventions to reduce cost and improve quality of care in each health care system.
- The data will allow agencies to develop common strategies for responding to critical, emerging health care issues.
- The data will help to identify the critical factors that have the greatest impact within a strategy or program and monitor the effects of interventions across time.
- Recommendations to reduce cost and improve quality of care in each health care system are expected in fiscal year 2021.

7. **Legal Authority and Trust.** The Texas Constitution directed the Legislature to establish the Employees Retirement System and Government Code §815.103 provides that the ERS Board of Trustees 1) shall hold all retirement system assets in trust for the exclusive benefit of the members and annuitants, and 2) administer all operations funded by trust assets for the same purpose. Statute specifies that the Board and executive director may acquire, manage, and sell any of the system's assets, and exempts ERS from some statutory requirements such as certain contracting and risk management practices.

ERS's status as a constitutionally-created agency and its trust fund structure are both uncommon among state agencies. In practice, ERS operates from three pension trusts and the Group Benefits Program trust. Legislative appropriations made to ERS are deposited into the appropriate trust and administrative expenses are allocated across respective funds. The balance at the beginning of fiscal year 2022 is estimated to be \$33.0 billion for these four funds.

8. **New Building Project.** ERS has continued work on a new 11-story mixed-use building to replace the current annex. The project is funded by the Trust, and lease income is projected to cover the cost and earn excess returns. The cost of the building is approximately \$80 million and is expected to be completed in early Spring 2021.

**Employees Retirement System
Rider Highlights - House**

Modification of Existing Riders

2. **Informational Listing of Appropriated Funds.** Revise rider to reflect benefit recommendations for 2022-23.

Article IX.

- 17.03. **Payroll Contribution for Group Health Insurance.** Revise rider to reflect estimates for 2022-23.
- 17.06. **Additional Payroll Contribution for Retirement Contribution.** Revise rider to reflect estimates for 2022-23.

Employees Retirement System
Items Not Included in Recommendations - House

		2022-23 Biennial Total			Information Technology Involved?	Contracting Involved?	Estimated Continued Cost 2024-25
		GR & GR-D	All Funds	FTEs			
Agency Exceptional Items Not Included (in agency priority order)							
1)	ERS Actuarially Sound Level. Funding request would increase the state's contribution to 16.13 percent. This rate, when combined with agency contributions of 0.5 percent and member contributions of 9.5 percent, would allow the plan to achieve the Actuarially Sound Contribution (ASC) rate of 26.13 percent of payroll. The Constitution limits the state's contribution to ten percent of compensation.	\$688,599,320	\$952,544,662	0.0	No	No	\$954,938,860
2)	LECOS Actuarially Sound Level. Funding request would increase the state's contribution to 3.07 percent from the current 0.5 percent. This contribution rate, combined with the 0.5 percent member contributions, would equal the ASC rate of 3.57 percent.	\$88,804,592	\$89,374,278	0.0	No	No	\$89,374,578
3)	JRS 2 Actuarially Sound Level. Funding request would increase the state's contribution to 24.52 percent from the current 15.663 percent. This increased state contribution rate, along with the effective member contribution rate, would equal the ASC rate of 33.94 percent.	\$11,379,226	\$16,108,368	0.0	No	No	\$16,108,368
TOTAL Items Not Included in Recommendations		\$788,783,138	\$1,058,027,308	0.0			\$1,060,421,806

**Employees Retirement System
Appendices - House**

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* Appendix is not included - no significant information to report

Employees Retirement System
Funding Changes and Recommendations by Strategy - House -- ALL FUNDS

Strategy/Goal	2020-21 Base	2022-23 Recommended	Biennial Change	% Change	Comments
ERS RETIREMENT PROGRAM 1.1.1	\$1,353,048,917	\$1,365,735,371	\$12,686,454	0.9%	Recommendations reflect an increase of \$12.7 million in All Funds over the 2020-21 biennium based upon the following assumptions: - Continued state contribution of 9.5 percent of salary; - 0.5 percent payroll growth in fiscal years 2021, 2022, and 2023; - FTE growth at the Department of Motor Vehicles, General Land Office, Texas Division of Emergency Management, and the Water Development Board; and - FTE decline at the Department of Criminal Justice.
LECOS RETIREMENT PROGRAM 1.1.2	\$17,123,268	\$17,387,992	\$264,724	1.5%	Recommendations reflect an increase of \$0.3 million from the 2020-21 biennium as projected contributions are assumed to remain at the 2021 levels, which were slightly higher than those in 2020.
JUDICIAL RETIREMENT PROGRAM-PLAN 2 1.1.3	\$28,458,403	\$28,486,548	\$28,145	0.1%	Recommendations reflect almost no change from the 2020-21 biennium as the number of active members and their salaries are assumed to remain almost the same.
JUDICIAL RETIREMENT PROGRAM-PLAN 1 1.1.4	\$39,477,751	\$38,929,520	(\$548,231)	(1.4%)	Recommendations reflect a decrease of \$0.5 million from the 2020-21 biennium due to a decrease in membership in this pay-as-you-go retirement plan provided for certain state judicial officers who held office before September 1, 1985.
PUBLIC SAFETY DEATH BENEFITS 1.1.5	\$28,669,597	\$27,572,616	(\$1,096,981)	(3.8%)	Recommendations reflect a decrease of \$1.1 million over the 2020-21 biennium as claims are assumed to remain at the 2021 levels, which were slightly lower than those in 2020.
RETIREE DEATH BENEFITS 1.1.6	\$28,788,215	\$27,500,000	(\$1,288,215)	(4.5%)	Recommendations reflect a decrease of \$1.3 million over the 2020-21 biennium as claims are assumed to remain at the 2021 levels, which were slightly lower than those in 2020.
Total, Goal 1, ADMINISTER RETIREMENT PROGRAM	\$1,495,566,151	\$1,505,612,047	\$10,045,896	0.7%	

Employees Retirement System
Funding Changes and Recommendations by Strategy - House -- ALL FUNDS

Strategy/Goal	2020-21 Base	2022-23 Recommended	Biennial Change	% Change	Comments
GROUP BENEFITS PROGRAM 2.1.1	\$3,915,326,698	\$4,043,398,312	\$128,071,614	3.3%	Recommendations reflect an increase of \$128.1 million from the 2020-21 biennium based upon the following assumptions: - No state contribution increases in fiscal years 2021, 2022 and 2023, which provide the full cost of member-only coverage and 50 percent of family coverage; - 3.9 percent member growth among retirees in fiscal years 2021, 2022, and 2023; - FTE growth at the Department of Motor Vehicles, General Land Office, Texas Division of Emergency Management, and the Water Development Board; and - FTE decline at the Department of Criminal Justice.
PROBATION HEALTH INSURANCE B.1.2	\$143,284,226	\$144,516,432	\$1,232,206	0.9%	Recommendations reflect an increase of \$1.2 million from the 2020-21 biennium based upon no state contribution increases in fiscal years 2021, 2022, and 2023 and retiree growth.
Total, Goal B, EMPLOYEES RETIREMENT SYSTEM	\$4,058,610,924	\$4,187,914,744	\$129,303,820	3.2%	
Grand Total, All Strategies	\$5,554,177,075	\$5,693,526,791	\$139,349,716	2.5%	

**Employees Retirement System
FTE Highlights - House**

Full-Time-Equivalent Positions	Expended 2019	Estimated 2020	Budgeted 2021	Recommended 2022	Recommended 2023
Cap					
Actual/Budgeted	395.0	408.5	408.5	415.0	415.0
	382.8	388.6	408.5	NA	NA
Schedule of Exempt Positions (Cap)					
Executive Director	\$357,120	\$357,120	\$357,120	\$357,120	\$357,120
Director of Investments	\$416,401	\$416,401	\$416,401	\$416,401	\$416,401

Notes:

- a) The agency is not requesting any changes to its exempt position. The State Auditor's Office Report, Executive Compensation at State Agencies (Report 20-706, August 2020), indicates a market average salary of \$301,880 for the Executive Director position at the Employees Retirement System and does not indicate a market average for the Director of Investments position.
- b) The State Auditor's Office is the source for the FY 2019 and FY 2020 annual average (actual) FTE levels.