Bill Number: **Assembly Bill 1389 (Budget) as amended 9/15/08**

SUMMARY

Sections 4 through 17 of Assembly Bill 1389 (Committee on Budget) amend provisions related to the purchasing power benefit paid by the Supplemental Benefit Maintenance Account.

PURPOSE OF THE BILL

The purpose of AB 1389 is to facilitate state government and reduce the amount of General Fund appropriations to the Teachers' Retirement System.

Board Position

The Teachers' Retirement Board has not taken an official position on AB 1389.

ANALYSIS

Existing law:

(All references are to the California Education Code)

Section 22954 establishes the rate of the General Fund appropriation to the Supplemental Benefit Maintenance Account as being equal to 2.5 percent of the total of creditable compensation for the prior fiscal year. The SBMA provides quarterly payments to retired and disabled CalSTRS members and their beneficiaries when the purchasing power of their benefit falls below 80 percent of its original value.

Section 22954.1 requires the Board to report annually to the Legislature and the Director of Finance on the ability of CalSTRS to pay SBMA benefits to retired and disabled members and their beneficiaries. If the Board reports that the Teachers' Retirement Fund has insufficient funds to pay these supplemental benefits, the General Fund will appropriate the necessary funds.

Section 22955 establishes an annual General Fund appropriation to the Teachers' Retirement Fund equal to 2.017 percent of the total of creditable compensation for the prior fiscal year, to be calculated annually on October 1.

Section 24411 authorizes the State General Fund to appropriate an annual cost-of-living-adjustment equal to 5 percent of the average annualized statewide increase in payroll for certificated employees over the previous 3 years. This appropriation, if made, is to be included in the State Budget and made to the Purchasing Power Protection Account for the benefit of retired and disabled members, beneficiaries, and former spouses with their own accounts. This COLA is separate from the purchasing power benefit that is provided by the SBMA.

Section 24415 establishes payment of SBMA benefits to retired and disabled members and their beneficiaries on a quarterly basis in an amount equal to what is necessary to restore the purchasing power of benefits up to 80 percent of their original value.

This bill:
Amends Section 22954 to reduce the annual General Fund appropriation to the SBMA by a specified amount each year and to change the date on which the appropriation is made from a single payment to two equal payments made on November 1 and April 1 of each year. The reduction to the 2.5 percent General Fund contribution is as follows:

$66,386,000 in 2008-09
$70,000,000 in 2009-10
$71,000,000 in 2010-11
$72,000,000 in 2011-12

Amends Section 22954.1 to eliminate the annual report to the Legislature and Director of Finance and instead require that the Board adopt an actuarial projection as to the ability of the Teachers' Retirement Fund to make supplemental benefit payments and the sufficiency of those payments to make the purchasing power payments. The actuarial projections are to be developed through the regulatory process, as provided by Section 24415.1, which is added by AB 1389.

Adds Section 22954.5 to require the General Fund make an annual appropriation of $56,979,949 from 2009-10 through 2012-13 to the SBMA to satisfy the ruling of the Sacramento County Superior Court.

Amends Section 22955 to change the schedule for calculating the amount of the 2.017 percent annual General Fund appropriation to provide the Board until April 15 of each year to revise the amount calculated on October 1 of the preceding year.

Repeals Section 24411 to eliminate the 5 percent COLA that the General Fund may appropriate to the Purchasing Power Protection account. Conforming changes are made by AB 1389 to Sections 22664, 24412 and 24600.

Amends Section 24415 to provide SBMA purchasing power equal to 85 percent of the benefit's original value, rather than the current rate of 80 percent. AB 1389 also makes conforming changes to this section to reflect the reduction in the General Fund contribution to the SBMA, as established by AB 1389.

Adds Section 24415.5 to establish the authority of the Board to promulgate regulations to enable the Board to adjust the supplemental benefit, within a range of 80 to 85 percent, to maintain the ability of the Board to make the payments.

PROGRAM BACKGROUND

When the inflation-adjusted value of the current monthly Defined Benefit (DB) Program benefit, as measured by the California Consumer Price Index (CPI), is less than 80 percent of the value of the initial benefit, a quarterly payment is made from the SBMA in the Teachers' Retirement Fund to restore purchasing power to the 80 percent level. About 56,000 of the 216,000 current benefit recipients received a purchasing power benefit payment in 2006-07, with the supplemental payment averaging about $4,100 per recipient annually. The benefit is currently paid to those whose benefit effective date is 1989 or earlier.

The benefit is primarily paid from a General Fund contribution equal to 2.5 percent of the compensation credited to the DB Program two years earlier. For example, the 2008-09 contribution will be based on the total compensation credited to the DB Program in 2006-07. That contribution is paid on July 1 of each fiscal year (although Chapter 6 of the Third Extraordinary Session (AB3x 8) was enacted in mid-February to delay the 2008-09 payment from July 1, 2008 payment until November 1, 2008), and is guaranteed pursuant to a contractual agreement made in statute. (A $500 million reduction in the 2003-04 contribution was the subject of successful litigation brought by the Board. The state has paid the $500 million, but the interest on the reduced contribution has not yet been appropriated by the Legislature). The benefit is guaranteed to the benefit recipient to the extent that there are sufficient funds in the SBMA to make the payment. If there are insufficient funds to make the full payment, the Board has a variety of options, including:

- Reducing the benefit payment to a percentage that can be paid from available funds
- Subject to Budget Act authorization, increasing the employer contribution rate
- Using any DB Program resources in excess of the amount needed to pay DB Program actuarial liabilities
- Interest is credited to the SBMA at an 8 percent annual rate, reflecting the actuarially assumed return on investments for the DB Program. Staff estimates that the balance of the SBMA, which is used to pay benefits in the future, will be $4.6 billion as of June 30, 2008.

Due to the structure of the purchasing power program, in which benefits are only paid to the extent that program resources are sufficient to pay those benefits, the fiscal viability of the purchasing power program is measured by the probability that the benefit can be paid over an extended period of time. Under the current program, in which 80 percent of the original purchasing power is protected if the 2.5 percent annual state contribution is sufficient to pay the benefit, there is a 69 percent chance that program resources are sufficient to pay that benefit over at least the next 75 years. Under AB 1389, the level of purchasing power protection is increased to 85 percent; therefore, the probability of sustainability is reduced to 51 percent.

AB 1389 will take effect upon the signature of the Governor; therefore, the increase in the purchasing power benefit will likely be in effect when the next payment of the SBMA payment is made on October 1. Under the current production schedule, the SBMA payment is processed at CalSTRS in early September, so that the necessary information is sent to the Controller to issue the actual payment for October. In order to make the required payment of the current benefit by October, the increased payment that would be the result of AB 1389, which would average about $300 per recipient (including payments made to those receiving SBMA funds for the first time because of the increase in the purchasing power percentage), will not be reflected in the October payment. The increased payment will be sent as a separate payment to recipients.

Because AB 1389 specifically exempts the regulatory process from the Administrative Procedure Act, the process will be expedited quicker than the process by which the campaign contribution regulations were promulgated. A similar expedited process occurred in 2003, when the Board promulgated its election regulations, which also were statutorily exempt from the APA. Under that process, once the Board conducts at least one public hearing, and adopts the regulations, the regulations are filed with the Secretary of State, and become effective, without any involvement of the Office of Administrative Law.