CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM

BILL ANALYSIS

Assembly Bill 135	**Assembly Member Havice (As amended 3/22/01)**
Position:	**Support, if amended**
Proponents:	**ACSA, ART, CFT, CRTA, CTA, FACCC, LA Community College Faculty Guild, UTLA**
Opponents:	**None known**

SUMMARY

Assembly Bill 135 bases "final compensation" on the highest average compensation earnable for 12 consecutive months, rather than three consecutive years, for all California State Teachers' Retirement System (CalSTRS) Defined Benefit (DB) Program members. Currently, such a definition of final compensation only applies to members with at least 25 years of credited service.

This bill also increases the supplemental payments made from the Supplemental Benefit Maintenance Account (SBMA) to restore purchasing power of initial allowances to 80 percent of the member's initial monthly allowance, rather than the current 75 percent.

HISTORY

Chapter 1028, Statutes of 2000 (AB 821—Assembly PER & SS) changes the definition of "final compensation" from the highest average annual compensation earnable by a member during any period of three consecutive school years to any period of 12 consecutive months for those members with 25 or more years of credited service.

SB 1693 (Ortiz—2000) would have increased quarterly payments made from the SBMA to restore purchasing power of current allowances to 80 percent of the member's initial allowance. SB 1693 was held on the Senate Appropriations Committee Suspense file.

Chapter 1006, Statutes of 1998 (AB 1102—Knox) vests the 2.5 percent General Fund contribution to fund SBMA payments and the purchasing power payments payable from that contribution.

Chapter 939, Statutes of 1997 (SB 1026—Schiff) increases purchasing power protection to up to 75 percent of the benefit recipient's original purchasing power from 68.2 percent. It also authorizes the Teachers' Retirement Board to transfer funds from the Teachers' Retirement Fund, increase employer contributions, and reduce or terminate distributions, if the resources in the SBMA were insufficient to maintain the 75 percent purchasing power payments.

CURRENT PRACTICE

The formula for calculating an unmodified allowance under the DB Program consists of three elements: (1) service credit, which is the number of full and partial years of credited service accumulated while employed for a school or community college; (2) age factor, which is the percent of pay for each year of service credit; and (3) final compensation. Up until this year, final compensation was generally the highest average annual earnable compensation during any period of three consecutive years of paid employment covered by CalSTRS. Current law, however, also provides for one-year final compensation to classroom teachers upon execution of a written agreement between the exclusive representative and the employer. The employer pays the present value cost of the increased benefit provided by one-year final compensation.

Beginning this year, for those members with at least 25 years of service credit, final compensation is calculated using the highest annual compensation earnable during any period of 12 consecutive months while an active member of the DB Program.

For members covered under the California Public Employees Retirement System (CalPERS), including classified members (such as clerical support and janitorial staff), the average monthly pay for 12 consecutive months is used to calculate final compensation. Prior to January 1, 2000, highest average pay over 36 months was used for many CalPERS members.

The current purchasing power guarantee maintains a recipient's allowance at 75 percent of the purchasing power of their initial allowance. Purchasing power is measured by changes in the All-Urban California Consumer Price Index, and reflects changes in the cost-of-living since the benefit first became effective. When the purchasing power of a recipient's current allowance, including the two percent annual adjustment, is less than 75 percent of the original allowance an annual supplemental benefit payment (paid in quarterly installments) is made to raise the annual benefit to the 75 percent level.

Supplemental payments are paid from (1) contributions continuously appropriated from the General Fund to the SBMA in an amount equal to 2.5 percent of the prior calendar year CalSTRS' member payroll, and (2) payments from the sale or use of land granted to the state by the federal government to support schools.

DISCUSSION

Final Compensation
This bill extends the basis of "final compensation" on the highest average 12 consecutive months to all CalSTRS members, without regard to the number of years of credited service.

Purchasing Power
This bill raises the purchasing power protection guarantee from 75 percent to 80 percent of a member's initial allowance through quarterly payments distributed from the SBMA.

As of February 2000, approximately 40,000 members and beneficiaries with benefit effective dates of 1981 or earlier receive quarterly supplemental payments. Raising the level of purchasing power protection from 75 percent to 80 percent would increase the number of supplemental benefit recipients by about 16,000 and would include all members and beneficiaries whose benefit effective date was 1985 or earlier. Basing the final compensation on the highest 12 consecutive months for all members would affect about 2,800 members who retire annually.

FISCAL IMPACT

Final Compensation

Benefit Program Costs – Basing final compensation on the highest 12 consecutive months for all members would have the following actuarial impact:

Present value cost:	
Normal cost increase of future service:	$985 million
Actuarial obligation for prior service (30-year amortization):	$1.093 billion
Total costs:	$2.078 billion

Increase in annual contributions needed as percent of payroll:	
Normal cost increase of future service:	0.291%
Actuarial obligation for prior service (30-year amortization):	0.323%
Total costs:	0.614%

This actuarial impact would result in the following expenditures over the first three full fiscal years:

Total benefit payment increase:

- In 2002-03: $2.7 million
- In 2003-04: $7.4 million
- In 2004-05: $12.8 million

Annual increase in contributions (funding) need to fund benefit:
(Based on payroll of $20.7 billion in 2002-03, increasing by 4.25 percent annually)

- In 2002-03: --
- In 2003-04: $127 million
- In 2004-05: $132 million

Administrative Costs – CalSTRS anticipates that it could absorb any increased administrative cost to implement this proposal.

Purchasing Power

Increasing the level of purchasing power protection from 75 percent to 80 percent would increase purchasing power payments as follows:

Total benefit payment increase:

- In 2002-03: $69.4 million
- In 2003-04: $76.2 million
- In 2004-05: $82.4 million

Given existing actuarial assumptions, the funds that are available in the SBMA under current law are sufficient to pay the increased cost for at least 30 years.

BOARD POSITION

Support, if amended to identify a funding source to pay the cost of extending the basis of final compensation to all CalSTRS members. Basing final compensation on the highest 12 consecutive months would provide consistency for all CalSTRS members and equity with CalPERS members. Increasing supplemental payments to restore 80 percent of the member's original purchasing power would provide additional protection against inflation in a manner that can be funded within existing resources. These increased payments would assist long-retired members whose retirement allowances have been the most eroded.