CALSTRS
HOW WILL YOU SPEND YOUR FUTURE?

STATE AND CONSUMER SERVICES AGENCY

BILL ANALYSIS

Bill Number: AB 194 (Torrico) as amended August 27, 2010

SUMMARY

AB 194 limits the retirement benefit of a person who becomes a member of a public retirement system, such as CalSTRS, on or after January 1, 2011 to 125 percent of the California State Governor's salary set by the California Citizens Compensation Commission effective December 2009 and adjusted annually consistent with changes to the All Urban California Consumer Price Index.

PURPOSE OF THE BILL

This bill addresses the concerns related to increased costs and abuse of public pensions at both the state and local level, especially as it relates to recent controversy surrounding compensation paid to officials in the City of Bell.

LEGISLATIVE HISTORY

AB 334—Peschetti (2000, Held) required the salaries of persons employed in permanent positions in the state civil service be indexed to the California Consumer Price Index for the previous calendar year, as determined by the Department of Industrial Relations, and would require those salaries to be adjusted as of July 1st of the fiscal year to reflect any increase in the consumer price index.

AB 3254—Haynes (1994, Held) required that the annual percentage increase in average annual compensation per full time employee not exceed the annual percentage increase in average compensation per employee in the private sector for the same time period. Would require each state agency to: 1) annually calculate a public pay equity ceiling, 2) file an annual public pay equity report with the Controller, and 3) make equitable adjustments in arbitration awards and labor contracts.

PROGRAM BACKGROUND

CalSTRS Members

CalSTRS administers the State Teachers' Retirement Plan, a federally tax-qualified defined benefit plan that consists of the CalSTRS Defined Benefit (DB), Defined Benefit Supplement (DBS), and the Cash Balance Benefit (CB) programs. These programs provide guaranteed retirement, disability and survivor benefits to California's public school teachers from kindergarten through community college, serving more than 847,000 members and their families. The Board applies strict guidelines for investing these assets, including standards of safety, diversification and liquidity, in order to protect the Teachers' Retirement Fund and the benefits of CalSTRS members.

Members participating in the DB Program are eligible to receive a lifetime monthly retirement benefit at age 55 with 5 years of service or as early as age 50 with at least 30 years of service. The years of service include partial and full time service.

Internal Revenue Code section 401(a)(17) limits the compensation that can be used to provide a benefit by a governmental plan, such as CalSTRS and CalPERS. Since July 1, 1996, the limit has increased annually and applies to members participating in a public retirement system on or after July 1, 1996. Those who became members prior to that year are not limited to a specific amount that can be included as compensation for the purposes of computing retirement benefits. The current compensation limit is $245,000. Currently, CalSTRS ensures that member benefits do not exceed the current $245,000 limit imposed by the Internal Revenue Code.

CalSTRS Employees

The Board has the responsibility for the compensation paid to the Chief Executive Officer (CEO), System Actuary, Chief Investment Officer (CIO), other investment officers and portfolio managers whose positions are designated as managerial, and the General Counsel.

ANALYSIS:

Existing Law:

Currently, CalSTRS benefits are paid to retiring members of the DB Program based on age, service credit and final compensation at retirement. Final compensation is based on the average annual full-time salary rate (or “compensation earnable”) over one or three years, depending on the number of years of service.

The California Citizens Compensation Commission (Commission) was established by the voters to set the salaries and medical, dental, insurance and other similar benefits of members of the Legislature and the State's other elected officials. The Commission is prohibited from increasing elected officials' salaries during budget deficit years. The Commission is also required to meet by June 30 of each year to decide what changes to make, if any, the following December. Actions of the Commission are effective on a December-to-December basis, with the Commission setting the Governor’s current salary of $173, 987, effective December 2009.

This bill:

AB 194 limits the retirement benefit of a new member of a public retirement system on or after January 1, 2011 to 125 percent of the California State Governor’s salary set by the California Citizens Compensation Commission effective December 7, 2009. This amount would be adjusted annually consistent with changes to the All Urban California Consumer Price Index. Currently, the Governor’s salary is $173, 987, which is the base amount, and 125 percent of that or $217, 484, would be adjusted annually.

This bill would apply only to those who become members of CalSTRS on or after January 1, 2011, and the full impact of this bill would be unknown for at least five years, or until he or she becomes vested or is eligible to retire. Although, most new members are not likely to have an allowance near the new limit after five years, some may reach it after 25 or more years of service. It appears as though member contributions would continue to be collected up to the current 401(a)(17) although the final compensation amount would be limited to the new limit.

The provisions of this bill would affect relatively few members. As an indication of this, of the nearly 500,000 active members of the DB Program, the compensation paid to only 165 members exceed the proposed limit, and, due to the existing federal compensation limit, the impact on final compensation would not exceed the current equivalent of about $28,000.

In addition, this bill would impact CalSTRS' ability to attract and retain high level Investment staff. The retirement benefits of working for a state entity are used to entice and recruit individuals that are paid at a higher rate during their career in the private sector. These individuals often take pay cuts and relocate in order to obtain the retirement benefits that are currently offered by CalPERS, which is similar in structure to CalSTRS' DB Program.

As a result, any potential new CalSTRS employees that are hired on or after January 1, 2011, that were not previously a member of CalPERS which are hired at a rate of $217,484 or higher or have the potential to earn a salary rate at or above that level during their career. This maximum allowance could potentially hinder recruitment and retention efforts and not afford the Teachers' Retirement Board (Board) the ability to establish a competitive pay program which is critical to hire and retain high-quality executive management and investment staff.

OTHER STATES' INFORMATION

The National Conference of State Legislators has compiled a report of legislation enacted from January 2010 through September 2010 looking at various state pension and retirement legislation. As outlined in their report, several states are pursuing or enacting legislation making benefit and contribution changes in statewide retirement plans, which are summarized below.

In Illinois, final compensation cannot exceed $106,800 and is to be annually adjusted by the Consumer Price Index, which is lower than the current federal indexed salary limit of $245,000. Both Colorado and Vermont limited compensation that counts toward final compensation to 8 percent annually and 10 percent annually, respectively.

FISCAL IMPACT

Benefit Program Cost – An estimated savings between $5-10 million over the next 30 years.

Administrative Costs/Savings – Minor costs related to system updates.

SUPPORT

N/A

OPPOSITION

California State University (unless amended)

SUPPORTING ARGUMENTS

PROS:

- Addresses concerns related to increased costs and abuse of public pensions at both the state and local level.

CONS:

- The new limit is less than the current federal limit, which requires additional monitoring and compliance efforts for CalSTRS and may prohibit the Boards ability to hire and retain high level executive and investment staff.

LEGISLATIVE STAFF CONTACT

Melissa M. Tanner
Legislative Advocate,
CalSTRS Legislative Affairs,
(916) 414-1982
mtanner@calstrs.com

Mary Anne Ashley
Assistant Director,
CalSTRS Governmental Affairs and Program Analysis,
(916) 414-1981
mashley@calstrs.com

Berman Obaldia
Director,
CalSTRS Governmental Affairs and Program Analysis,
(916) 414-1977
bobaldia@calstrs.com