CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM

BILL ANALYSIS

Assembly Bill 2646	**Assembly Member Liu (As introduced 2/22/02)**
Position:	**Support, if amended**
Proponents:	**ACSA, CFT, and CTA**
Opponents:	**None known**

SUMMARY

Assembly Bill 2646 eliminates the current 25-year credited service requirement to base final compensation for active members of the California State Teachers' Retirement System (CalSTRS) Defined Benefit (DB) Program on the highest average annual compensation earnable by the member during 12 consecutive months, rather than the highest average annual earnable compensation during any period of three consecutive years.

HISTORY

Chapter 840, Statutes of 2001 (AB 135—Havice), prior to its enactment, would have eliminated the 25-year credited service requirement to base final compensation for active members of the DB Program on the highest average annual compensation earnable by the member during 12 consecutive months, rather than the highest average of the last three years.

Chapter 1028, Statutes of 2000 (AB 821—Assembly PER&SS) bases "final compensation" on the highest average annual compensation earnable by a member during a consecutive 12 month period of employment rather than highest three consecutive years for members with at least 25 years of credited service.

AB 2201 (Honda—2000), among other provisions, would have calculated final compensation on the highest 12 consecutive months. This bill was held in the Assembly Appropriations Committee.

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 2001, final compensation was generally the highest average annual earnable compensation during any period of three consecutive years of paid employment covered by CalSTRS. Beginning January 1, 2001, for those members with at least 25 years of service credit, final compensation is calculated using the highest average annual compensation earnable during any period of 12 consecutive months while an active member of the DB Program. In addition, classroom teachers can qualify for highest single year final compensation 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 highest single year final compensation.

For classified members of the California Public Employees Retirement System (CalPERS), such as clerical support and janitorial staff in the school districts, the highest annual compensation for 12 consecutive months is used to calculate final compensation. Prior to January 1, 2000, the highest average annual compensation over three years was used for classified and many other CalPERS members.

DISCUSSION

This bill extends the basis of "final compensation" on the highest average 12 consecutive months to all DB Program members, without regard to the number of years of credited service. Changing the definition of final compensation from a three-year average to the highest single year for all CalSTRS members would create a basis for determining final compensation that is consistent with that used for state and classified workers covered by CalPERS, as well as an equitable method for all CalSTRS members. This change would affect about 32 percent of the members who retire.

FISCAL IMPACT

Benefit Program Costs – Based on the June 30, 2000 actuarial valuation, this bill would have the following actuarial impact:

	Present value cost (in millions)	**Increase in annual contributions needed as a percent of payroll**
Normal cost increase of future service	$985	0.291%
Actuarial obligation for prior service[1]	$1,093	0.323%
Total costs	$2,078	0.614%

[1] Amortized over 30 years

This actuarial impact would result in the following expenditures over the first three full fiscal years (in millions of dollars):

	2003-04	**2004-05**	**2005-06**
Total benefit payment increase	$2.7	$7.4	$12.8
Annual increase in contributions (funding) needed to fund benefit[2]	--	$130	$135

[2] Based on a payroll of $21.1 billion in 2003-04, increasing by 4.25 percent annually

An estimate based on the upcoming June 30, 2001 valuation would likely be higher. The bill expresses legislative intent that the costs of the proposed benefit be paid from existing funds in the Teachers' Retirement Fund. The June 30, 2001 actuarial valuation indicates that there are insufficient resources available in the DB Program to fund this benefit.

Administrative Costs – CalSTRS anticipates that the total one-time costs required to make changes to the System's corporate database would exceed $150,000. Ongoing costs would be minor and absorbable.

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.