

STATE TEACHERS' RETIREMENT SYSTEM

BILL ANALYSIS

Assembly Bill 884, Assembly Member Honda (As Amended 03/02/98)

Position: Support, if Amended

Proponents: CFT (Sponsor), ACSA, ART, BOG, CRTA, CTA, FACCC, FCPHE, UTLA

Opponents: Cal-Tax, DOF

SUMMARY

This bill would amend the Education Code to provide that, beginning September 1, 1999, the "2% improvement factor" applied to benefit payments from the State Teachers' Retirement System (STRS) Defined Benefit (DB) Plan will be compounded.

BACKGROUND

Chapter 1305, Statutes of 1971, provided for the 2% simple annual improvement factor, beginning September 1, 1973.

AB 2911 (Epple, 1990), which failed passage, would have compounded STRS' benefit improvement factor, funded through employer contributions to cover increases to the normal cost rate.

SB 2016 (O'Connell, 1995), which failed passage, like this bill would have provided for a 2% compounded improvement factor.

CURRENT PRACTICE

Under current law, the STRS DB Plan benefit payments are increased by a 2% improvement factor each year beginning on September 1 following the first anniversary of the effective date of the benefit. The factor, however, is not compounded and does not apply to annuities payable from the accumulated annuity deposit contributions.

DISCUSSION

STRS' current 2% simple benefit improvement factor has not kept pace with inflation over the years. Retired members and other benefit recipients, however, receive supplemental purchasing power payments when their allowance has eroded to 75% of the original allowance. This is approximately 17 years after retirement based on recent inflation experience.

The compounded improvement factor proposed by AB 884 would be applied beginning September 1, 1999, to all current and future benefits payable and would provide improved protection against inflation for all benefit recipients, including those who began receiving their allowances more recently.

FISCAL IMPACT

Program - Currently there are an estimated 150,805 individuals receiving benefits from the System's DB Plan. In any given year the majority of these recipients are eligible to receive an annual 2% improvement factor.

Using information from STRS' 1997 actuarial valuation, the estimated additional program costs for compounding the 2% improvement factor would be 0.944% of payroll or an annual cost of \$154,344,000 (1998/99 payroll estimated at \$16,355,000,000).

AB 884, however, does not provide funding for the increased cost of compounding the improvement factor. Some of the cost would be offset by a decrease in the amount of supplemental payments, as fewer benefit recipients would have allowances with purchasing power below 75%, though funding for the benefit improvement is separate from funding for supplemental payments. If this bill were enacted without adequate funding, STRS' unfunded obligation would be increased and the amortization period extended.

Administrative - There would be one-time administrative costs for implementing this legislation of approximately \$196,000 including development, testing and implementation of modifications to the automated system, updating procedures, and revisions to member communications. The bill does not, however, provide for the payment of the administrative costs that STRS would incur in implementing the compounded improvement factor.

POSITION

Support, if amended - AB 884 should be amended to provide adequate funding of increased program and administrative costs. If amended, the bill would provide for a funded increase in the permanent benefit maintenance for retired members and other benefit recipients who receive payments from the STRS DB Plan.