CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM

BILL ANALYSIS

Senate Bill 499 **Senator Soto (Amended 4/5/01)**

Position: **Sponsor**

Proponents: **None known**

Opponents: **None known**

SUMMARY

Senate Bill 499 makes the following minor changes to the laws governing of the California State Teachers' Retirement System (CalSTRS):

- Eliminates the requirement that beginning January 1, 2002 a dependent child between the ages of 18 and 22 must maintain full-time student status to remain eligible for the child's portion of a disability or family allowance under Coverage A of the Defined Benefit (DB) Program.

- Increases the loan limit for home loans under CalSTRS' Home Loan Program (HLP) from $350,000 to two times the conforming loan limits set by Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Association (Freddie Mac), whichever is higher.

- Allows Cash Balance (CB) Benefit Program participants to purchase DB Program service credit on their prior CB-based employment, after they become DB Program members.

HISTORY

Chapter 1165, Statutes of 1996 (AB 3032—Burton) eliminates the requirement that a dependent child between the ages of 18 and 22 must maintain full-time student status to remain eligible for the child's portion of a disability or family allowance under Coverage A, with the provisions sunsetting 2002.

Chapter 392, Statutes of 1984 (AB 1872—Elder) establishes the CalSTRS HLP to provide financing to active and retired members who purchase homes in California.

Chapter 419, Statutes of 1998 (SB 1945—Karnette) establishes a 100 percent financing option for participants in the CalSTRS HLP, whereby active members may obtain personal loans of up to 5 percent of the purchase price or value of the home, using their retirement contributions as collateral. It also limited loan amounts to the fair market value of the property, not to exceed $350,000.

Chapter 592, Statutes of 1995 (AB 1298—Ducheny) establishes the CB Benefit Program for part-time public school employees which employers may elect to provide for persons employed less than half-time at a contribution rate that is lower than the Social Security tax.

CURRENT PRACTICE

Requirements for dependent children receiving a disability or family allowance under Coverage A

The statutory requirement that a child between 18 and 22 be a full-time student in order to be eligible for a child's portion under Coverage A Disability Allowance or Family Allowance was repealed in 1996, but that repeal has a sunset date of January 1, 2002. As a result, until 2002, a monthly family allowance is payable to a dependent child who is under the age of 22, unmarried at the time of the member's death and financially dependent upon the member on the date the member died, or (if the member died while receiving a disability allowance) on the effective date of disability. Beginning January 1, 2002, the law will again require that a child between 18 and 22 be a full-time student to meet the definition of a dependent child and be eligible for a child's portion under Coverage A. Eligibility for benefits under Coverage B of the DB Program (which applies to members who joined CalSTRS after October 1992) does not require children under the age of 21 to be full-time students to be eligible for additional disability or survivor benefits.

Prior to 1996, if a CalSTRS member who was under Coverage A became disabled or died while an active member, a child who was between 18 and 22 was eligible to receive a monthly disability child's portion or family allowance only if the child was registered as a full-time student on the effective date of the member's disability allowance or the date of the member's death. When a student fell below the full-time requirement, dropped out for the term, or decided not to continue attending school, the child's portion of the disability or family allowance was discontinued. If the student was the only child or the only remaining child receiving a benefit, the total family allowance ceased until full-time status had been reestablished. CalSTRS monitored the status of children to verify their continued eligibility for benefits. CalSTRS would also make necessary adjustments to disability and family allowances when students fell below full-time status. This usually required manual calculation of an overpayment and subsequent establishment of a receivable to collect the amount of the allowance the family was not entitled to receive.

The CalSTRS Home Loan Program

The CalSTRS Mortgage HLP was established in 1984 to provide CalSTRS with a mortgage backed investment opportunity, as well as an additional source of home financing for its members. Subsequent legislation enabled the Teachers' Retirement Board (Board) to enter into correspondence agreements with private lending institutions to facilitate the implementation of the HLP. In 1986, CalSTRS began making 15 and 30 year fixed interest rate mortgage loans to refinance or purchase one to four-family owner-occupied properties within California.

SB 1945 (Karnette—1998) established the loan limit of $350,000 primarily to codify the existing loan limit, which had been part of the HLP since the late 1980's. Since that time, median home prices in California have increased by over 40 percent. In certain areas of the state, the median price for single family homes has doubled since the current limit was set, and exceeds $450,000 in San Francisco and Santa Clara.

CB Benefit Program vs. DB Program Participation by Part-Time Members

The CB Benefit Program was established as the CB Plan in 1995 to provide a retirement system for substitute, part-time and adjunct instructors as an alternative to the DB Program and Social Security. Since its inception in 1996, CB Benefit Program has been steadily growing and currently has over 10,000 participants.

Currently, DB Program members may purchase service credit for specific kinds of service performed in the past, including creditable service performed prior to becoming a member, out-of-state public school service, sabbatical leave, military leave, maternity/paternity leave or family care and medical leave and out-of-state public school. To purchase permissive service, the member pays, prior to retirement, all contributions at the contribution rate for additional service credit at the time of election. In 2000-01, that rate is 15.664 percent of the highest full-time salary rate over the past three years.

Although current law permits a participant in the CB Benefit Program to elect to have future service credited to the DB Program, it does not authorize CB Benefit Program participants to convert their prior CB-based employment to DB service credit after they become DB Program members. This affects CB Benefit Program participants that have obtained full-time status and face mandatory membership in the DB Program, as well as those participants that simply elect to change their retirement coverage to the DB Program.

DISCUSSION

Specifically, this measure:

- Eliminates the requirement that beginning January 1, 2002 a dependent child between the ages of 18 and 22 must maintain full-time student status to remain eligible for the child's portion of a disability or family allowance under Coverage A.

- Increases the loan limit for the CalSTRS HLP to two times the conforming loan limits of Fannie Mae or Freddie Mac, whichever is higher.

- Permits a DB Program member to purchase his or her service credited to the CB Benefit Program in lieu of receiving a benefit under the CB Benefit Program.

Eliminating the requirement that a dependent child must be a full-time student to receive a disability or family allowance under Coverage A

This bill eliminates the sunset clause of January 1, 2002 for Coverage A eligibility for all children under age 22. This eligibility is consistent with Coverage B in which all children under age 21 are eligible for disability and survivor benefits. By eliminating the sunset clause for the current eligibility requirements for dependent children under Coverage A, CalSTRS would be able to continue to pay benefits to these dependent children without excessive monitoring of their eligibility based on their full-time student status.

If the January 1, 2002 sunset date is not removed, CalSTRS would need to reestablish 6 to 7 full-time positions to once again monitor the eligibility of dependent children for Coverage A benefits. Past experience in this program has shown that staff verifies student status three to four times per year by sending forms to potentially eligible students. The forms are designed to verify student status for the preceding period. The responses from the students are often incomplete or unclear, which requires follow-up by CalSTRS staff. Because the status of the student may change from quarter to quarter, his or her eligibility for benefits may change several times a year. If children who have lost their eligibility are not identified promptly, benefits will be overpaid. Overpayments result in establishing accounts receivable and subsequent reductions in the disability or family allowances. This cycle of changing eligibility is damaging to the family because the Coverage A allowance can be discontinued and started several times during any given year, depending on the child's eligibility and student status. The collection of overpayments also creates a hardship because a family allowance can be reduced by 5 to 15 percent until the overpayment is paid off.

Increasing the Loan Limit for the CalSTRS Home Loan Program
This bill deletes the current $350,000 loan limit set in statute, and instead gives CalSTRS the authority to set the loan limit at two times the conforming loan limits of Fannie Mae or Freddie Mac, whichever is higher. Imposing the loan limit in this manner permits the CalSTRS HLP to respond to future economic changes without having to amend state law further. Because the current loan limit for both Fannie Mae and Freddie Mac is $275,000, this bill increases the HLP loan limit to $550,000. SB 499 will allow many qualified homebuyers who were previously excluded from the HLP due to the high cost of housing in their communities to participate in the program.

Converting CB Benefit Program Participation into DB Program Service Credit
Current law does not allow CB-covered service to be credited to the DB Program. A CalSTRS member working less than half-time usually decides in which program to participate based on whether he or she anticipates working more than half-time in the future. By allowing a DB member to purchase service credit they previously earned as a CB Benefit Program participant, there is less guesswork in deciding whether to participate in the CB Benefit Program or the DB Program.

Although the member that purchases their CB-covered service is, in effect, paying about half of the employer's contribution for the service that is credited to the DB Program, they will be better off than if he or she couldn't have the prior service credited to the DB Program at all. While the total cost to the member who purchases their CB-covered service under the DB Program is greater than the amount they would have paid had they begun as a member of the DB Program, they will still receive a larger retirement allowance by consolidating their service credit in the DB Program than by continuing in both plans.

In order to conform to current requirements that a member not accumulate more than 1.0 years of service in any one year, this measure allows members to purchase only the CB Benefit Program service that is not in excess of a full-time assignment.

FISCAL IMPACT

Benefit Program Costs – The System Actuary estimates that eliminating the sunset clause that limits the eligibility of dependent children for a family allowance under Coverage A will increase the annual cost in benefit payments by $900,000. Some of this payment probably would occur as an overpayment even if the sunset date is not repealed, and written off as uncollectible. Consequently, the net costs would likely be less than $900,000.

There are no program costs associated with raising the loan limit for the CalSTRS HLP or converting CB Benefit Program participation into DB Program service credit.

Administrative Costs – Eliminating the sunset clause that specifies the eligibility of dependent children for a family allowance under Coverage A would avoid the need for CalSTRS to re-establish seven positions necessary to monitor student status and fund other ongoing administrative costs, which represents a savings of approximately $369,000 per year and $97,000 in start-up costs. If this measure is approved, the total net increase cost to the System (benefit increase less avoided operating costs) is estimated to be $464,000 in the first year and $531,000 per year (less an unspecified amount for overpayment write-offs) thereafter.

There are no administrative costs associated with raising the loan limit for the CalSTRS HLP. There are however, minor and absorbable costs associated with billing CalSTRS members that convert from the CB Benefit Program to the DB Program.

BOARD POSITION

Sponsor. This bill is consistent with the Board's previous actions to enhance the services provided to CalSTRS members.