HOUSE RESEARCH ORGANIZATION bill analysis | 5/18/2001 | SB 273 Armbrister, et al. (Tillery) (CSSB 273 by Rangel)

SUBJECT: Changes to the Teacher Retirement System

COMMITTEE: Pensions and Investments — committee substitute recommended

VOTE: 5 ayes — Tillery, Woolley, Salinas, Rangel, Telford

0 nays

4 absent — Crownover, George, Goodman, Williams

SENATE VOTE: On final passage, May 3 — voice vote

WITNESSES: No public hearing

BACKGROUND: The Teacher Retirement System (TRS) is the retirement system for public school teachers and school personnel of Texas. Funded by a combination of teacher and state contributions, the system provides retirement annuities and death and disability benefits for its members and designated beneficiaries. Any public-school employee who works at least 20 hours a week and all bus drivers are eligible to participate in TRS.

The standard service retirement annuity is computed by multiplying the system member's average yearly salary over the three years of the member's highest salary by the multiplier for each year of service credit. The retirement multiplier was raised to 2.2 by the 76th Legislature in SB 1128 by Armbrister.

DIGEST: CSSB 273 would authorize the TRS board of trustees to:

- review and certify financial companies offering investment products such as annuities or investments to teachers through a 403(b) program;
- increase the multiplier to 2.3 for computing retirement benefits;
- provide that premiums or contributions to insurance policies or contracts would not be subject to tax; and
- require the confidentiality of individual records.

403(b) plans. *Review and certification of investment products.* The TRS board would have to compile and maintain a list of companies that would be eligible to sell annuities and investments to teachers and other school district employees as part of a "salary reduction agreement." Under "salary reduction agreement," the school district would remit a portion of the teacher's salary directly to the company to purchase the annuities and investments. The salary reduction agreement would offer additional benefits by reducing the gross salary subject to federal income taxes.

Eligibility standards. To be certified, the investment company selling annuities would have to demonstrate that during the past five years:

- none of the company's actuarial opinions required in its annual report to the commissioner or in its standard valuation of reserves were adverse or qualified;
- all annual independent audits had been timely filed, and none indicated any material adverse financial conditions;
- the company had not been the subject of a Texas Department of Insurance (TDI) administrative or regulatory action;
- the company had maintained at least 400 percent of the authorized control level, as calculated according to the TDI's risk-based capital and surplus requirements; and
- the company had not fallen below 300 percent of the of the authorized control level, as calculated according to the TDI's risk-based capital and surplus requirements.

Other investment products. TRS also would be able to certify companies offering qualified investment products other than annuities according to rules based on the financial strength of the companies and the administrative costs to employees. CSSB 273 would prohibit TRS trustees from unreasonably restricting a teacher's or school district employee's access to a reasonable variety of qualified investment products.

Cooperation with other state agencies. TRS would be allowed to work with TDI and the State Securities Board on developing rules on administering the program. TRS would be required to refer complaints about investment companies to TDI or the securities board, and those agencies would be required to inform TRS about any of their enforcement actions or determinations regarding a product or company that violates the eligibility standards. TRS would be required to remove the certification of any company violating the standard, but the company would be able to recertify.

Fees. TRS could collect a fee of up to $5,000 to cover the administrative costs to certify or recertify an investment company.

Restrictions on school districts. A school district could not:

! refuse to enter a salary reduction agreement with a teacher or district employee for an eligible investment product;
! require or coerce an employee's attendance at a meeting where investment products were marketed;
! limit an employee's ability to initiate, change, or terminate a qualified investment product contract at any time the employee chose;
! grant exclusive access to employees by discriminating against or imposing barriers to any agent, broker or company;
! grant exclusive access to information about an employee's financial information;
! accept any benefit from an investment company; or
! use public funds to recommend a specific investment product.

Activities subject to criminal penalties. A person would commit a class A misdemeanor (up to one year in jail and/or a maximum fine of $4,000) if the person, with regard to qualified investment products to be offered through a salary reduction agreement:

! sold or offered for sale an investment product that was ineligible for a salary reduction agreement;
! violated a prohibition against selling insurance without a license or unlawfully acting as an agent (under other circumstances, punishable by a $500 to $1,000 fine); or
! engaged in unfair and deceptive practices.

Other penalties. CSSB 273 also would amend Business and Commerce Code, sec. 17.46 (b) to expand the definition of "a false, misleading, or deceptive act or practice" to include the selling, offering to sell, or illegally promoting an investment product not certified by TRS for a salary reduction agreement. Violators of this section would be jointly and severally liable for actual damages, court costs, and attorney's fees. Exemplary damages would be awarded in cases of fraud and malice.

Website information. CSSB 273 also would require that the list of eligible companies be available on the TRS Internet website. The notice would have to be in at least 14 point type and contain space for:

- name, address, telephone number of the agent and company offering the investment product;
- name, address, and telephone for the company underwriting the annuity;
- license number of the salesperson and the agency who issued the license;
- information about the annuity, including current rate of interest, how the interest was compounded, amount of fees or value adjustments charges, accumulated value information, loans available as part of annuity; restrictions, and amount of any fee, costs, or penalties; and
- and additional information, in plain language, regarding how the company would have to comply with the eligibility standards, how the a purchaser could contact TRS about eligible companies, civil remedies available to an employee, and name and telephone numbers of the TDI and attorney general's consumer protection divisions.

Additional notice and information. A prospectus and other information would have to be provided with any variable interest annuity and any equity-based index must state how the annuity contract would be credited with growth. If notice and other information were not provided, the purchase contract would be voidable by the purchaser within 30 days. The seller also would be liable for the amount of all consideration paid, plus 10 percent interest. The seller would not have to provide the refund if the seller could provide a notice signed by the purchaser.

Tax status of employee insurance premium. The bill also would provide that any premium or contribution to a policy, insurance contract, or agreement would not be subject to any state tax, regulatory fee, or surcharge.

Benefit increases. CSSB 273 would increase the multiplier to calculate retirement benefits from 2.2 percent to 2.3 percent, which would be equivalent to a 4.5 percent increase. The monthly benefit payment for beneficiaries would be increased $50 a month. Other provisions would add a 6 percent inflation adjustment for persons retired before August 31, 2000. On top of the 6 percent inflation adjustment, current retirees would receive an additional 4.5 increase that would correspond to the increase in the multiplier for future retirees.

Other provisions. CSSB 273 also would do the following:

- maintain the confidentiality of member, retiree, annuitant, beneficiary or alternative payee records;
- require benefit payments to retired teachers who were rehired by a school district where there was an acute shortage of teachers or for a teacher rehired as a full-time bus driver;
- require that a school district remit retirement payments or insurance premiums to TRS within five days rather than 11 days as long as the district did not request a waiver because of the district's financial or technological resources;
- allow a teacher with at least seven years of service to purchase up to three years of retirement service credit by paying the actuarial present value of the additional retirement annuity benefits; and
- permit a member participating in the plan on September 1, 2001, to discontinue participating in the TRS plan before December 31, 2001.

CSSB 273 would repeal:

- Government Code, sec. 823.502, which allows an eligible person who had terminated TRS membership to reestablish service credit;
- Government Code, sec. 824.306, which requires a income report from disability retirees under the age of 60.

The overall effective date of the bill would be September 1, 2001.

The provision that would require TRS to describe the mandatory notice to those selling annuity contracts would be effective on December 1, 2001. The provisions related to the 403(b) programs would be effective on June 1, 2003.

Changes in the return to work provisions would apply to the beginning of the 2001-2002 school year. This provision would take immediate effect if finally passed by a two-thirds record vote of the membership of each house. Otherwise, it would take effect September 1, 2001.

SUPPORTERS SAY:

CSSB 273 would increase retirement benefits to Texas teachers and other public education employees participating in TRS. Enhanced retirement benefits would help improve the state's traditionally low rank in the compensation it provides teachers. The bill also would offer a workable proposal to certify 403(b) plans as eligible. These plans would provide additional benefits for teachers.

403(b) plans. CSSB 273 would provide sufficient safeguards to minimize the risk of these annuities and investment plans. Companies would have to be certified before selling investment products to teachers through local school districts. TRS already has expertise in evaluating investment plans from management of the billions of dollars in its own portfolio. The oversight would be supplemented by the Texas Department of Insurance and the State Securities Board. Only companies with proven track records over the past five years would be eligible to participate in the program.

TRS would provide complete and easy to understand information about the investment options offered through 403(b) plans. The information would be readily accessible through the TRS website.

CSSB 273 would provide criminal and civil sanctions for those who tried to sell unsound or dubious investment products to teachers or who otherwise betrayed their trust. Teachers would be able to void purchase contracts when no information was provided. Those engaging in deceptive trade practices would be subject to stiff civil sanctions, including exemplary damages in cases of fraud or malice.

Increased benefits. CSSB 273 would give teachers and other school personnel a much-deserved increase in the retired service credit multiplier from 2.2 percent to 2.3 percent. The multiplier increase would come from within the system, with no increase in member or state contributions. Thus, teachers would receive greater retirement monthly payments within an actuarially sound retirement system.

Current retirees would receive an ad hoc 6 percent increase in their monthly benefits along with a 4.5 percent increase that corresponds to the increase in the multiplier for future retirees. Overall, current retirees will receive a benefit increase of 10.77 percent. Increasing benefits for older retirees, many who worked for extremely low wages in the 1960s or 1970s, maintains a rough parity among all retirees. A teacher who retired in 1971 would receive a benefit check only $50 a month less than one who retired in 2001, despite the wide disparity in their original salaries.

OPPONENTS SAY:

403(b) plans. TRS should not be in the "blue sky" business of certifying investment products or overseeing insurance companies. This type of authority would dilute its original purpose of managing the funds' assets to benefit retired teachers. The state should leave this kind of oversight to the Texas Department of Insurance or the State Securities Board.

All investment products, including relatively safe and secure annuities, pose risks, especially for non-professional investors. Unexpected losses from supplemental retirement programs could put more political pressure to increase guaranteed benefit rates in the future.

Benefits. CSSB 273 would increase the TRS actuarial accrued liability by $4.6 million. Provisions that would allow members to buy up to 36 months of service also could lead to substantial losses over time. The increase in TRS assets resulted as much from the bullish stock market over the past several years as it did from the fund's conservative investment policies. It would not be prudent to increase unfunded liability of the fund during a time of market uncertainty.

NOTES:

The House committee substitute differs from the Senate-passed bill by deleting sections that would:

- provide for cancellation of a teacher certificate;
- provide for "membership service previously waived;"
- allow a one-year window for the purchase of previously withdrawn

service by former higher education teaching assistants; and

! allow transfer of service credit for certain higher education employees.

The substitute would require TRS to maintain a list of eligible annuity companies and posting of detailed information on its website. It added penalties for unlawfully acting as an agent or an agent without a license. It also added selling ineligible annuity contracts to the definition of a deceptive trade practice and provided for a person to be held jointly and severally liable for violations.

The House committee substitute added the increase in the multiplier and the inflation adjustment for benefits for those who retired before August 31, 2000.